

# GRAMMARIANS AT THE GATE: THE REHNQUIST COURT'S EVOLVING "PLAIN MEANING" APPROACH TO BANKRUPTCY JURISPRUDENCE

*Walter A. Effross\**

I. INTRODUCTION .....	1638
II. CASE STUDIES .....	1640
A. <i>Midlantic National Bank v. New Jersey Department of         Environmental Protection</i> .....	1640
1. Background .....	1641
2. Honoring a Pre-Code Exception .....	1644
B. <i>Kelly v. Robinson</i> .....	1648
1. Background .....	1648
2. Adopting Precedent Contradicting the Bankruptcy Act .....	1652
3. Sounding the Retreat? <i>Pennsylvania Dept. of             Public Welfare v. Davenport</i> .....	1656
C. <i>U.S. v. Ron Pair Enterprises, Inc.</i> .....	1659
1. Background .....	1660
2. Reinterpreting <i>Midlantic</i> and <i>Kelly</i> .....	1663
D. <i>Toibb v. Radloff</i> .....	1669
1. Following the Logic .....	1670
E. <i>Union Bank v. Wolas</i> .....	1673
1. Background .....	1673
2. Upholding Implications, Even if Unintended .....	1675
F. <i>Dewsnup v. Timm</i> .....	1678
1. Background .....	1678
a. Split Between the Tenth and Third Circuits .....	1681
2. Resorting to a Subsection-by-Subsection Analysis? .....	1685
G. <i>Taylor v. Freeland &amp; Kronz</i> .....	1690
1. Background .....	1691

---

\* Associate, McCarter & English, Newark, New Jersey. B.A. (philosophy) *cum laude*, Princeton University 1984; J.D., Harvard Law School, 1987. Mr. Effross is a Co-author of the New Jersey Bankruptcy Manual of the New Jersey Institute for Continuing Legal Education.

2. Inviting Equitable Elaboration of Plain Meaning?	1697
H. <i>Barnhill v. Johnson</i>	1699
1. Background	1700
a. Conflict Among the Circuits	1701
i. Background	1701
ii. Sixth Circuit Precedent	1703
iii. Seventh Circuit Precedent	1705
2. Resolving the Limits of “Plain Meaning”?	1706
I. <i>Patterson v. Shumate</i>	1710
1. Background	1710
2. “Plain Meaning” Triumphant	1715
J. <i>Pioneer Investment Services v. Brunswick Associates Limited Partnership</i>	1718
1. Background	1719
2. Equitable Excuses and Dueling Dictionaries	1722
K. <i>Nobelman v. American Savings Bank</i>	1730
1. Background	1730
a. The District Court Opinion	1731
b. The Fifth Circuit Opinion	1734
2. Preferring “Plausible” to “Quite Sensible” Construction	1736
L. <i>Rake v. Wade</i>	1739
1. Background	1739
a. Circuit Court Precedent	1741
b. The Tenth Circuit’s Opinion	1743
2. Finding the “Most Natural” Meaning	1746
III. Internal Ambiguities of the “Plain Meaning” Approach	1747
A. The Six Stages of “Plain Meaning”	1749
1. One Subsection’s Language in a Vacuum	1749
2. Within One Section	1750
3. Across Different Sections	1750
4. In the Context of the Code’s Policies	1752
5. In Conjunction with Extra-Code Policies	1753
6. Consideration of the Equities	1754
B. Recourse to Legislative History	1754
1. Tacit Incorporation of Pre-Code Precedent	1755
2. Utility of Congressional Statements and Reports	1758
IV. Conclusion	1761

## I. INTRODUCTION

Humpty Dumpty was sitting, with his legs crossed like a Turk, on top of a high wall — such a narrow one that Alice quite wondered how he could keep his balance . . . .

"Why do you sit out here all alone?" said Alice, not wishing to begin an argument.

"Why, because there's nobody with me!" cried Humpty Dumpty. "Did you think I didn't know the answer to *that*? Ask another."<sup>1</sup>

Like Lewis Carroll's master of literalism, the Supreme Court sits alone and authoritative atop a precarious perch. Yet while Humpty Dumpty's unchallengeable definitions lend meaning to "the greatest of all nonsense poems in English,"<sup>2</sup> the Court faces the far more daunting task of providing a coherent hermeneutics for the Bankruptcy Code of 1978.<sup>3</sup>

To reconcile the conflicting goals of the Code and to coordinate the Code's interaction with other federal statutes and with state laws, the Court has increasingly embraced a "plain meaning" approach to the statutory text. As developed in a series of recent bankruptcy decisions under Chief Justice Rehnquist,<sup>4</sup> this doctrine emphasizes the literal interpretation of Code provisions, placing an "exceptionally heavy" burden on proponents of any other construction.<sup>5</sup> So long as the plain meaning of a Code section is "coherent

---

<sup>1</sup> LEWIS CARROLL, *THROUGH THE LOOKING-GLASS AND WHAT ALICE FOUND THERE* (1896), reprinted in *THE ANNOTATED ALICE* 261, 263 (Martin Gardner ed. 1960) (hereinafter *LOOKING-GLASS*).

<sup>2</sup> *Id.* at 191-92 & n.11. It is to Humpty Dumpty that Alice turns for an explanation of a work that, printed backwards, had required her to "hold up [the page] to a glass, [so that] the words will go all the right way again." *Id.* at 191.

"You seem very clever at explaining words, Sir," said Alice. "Would you kindly tell me the meaning of the poem called 'Jabberwocky'?"

"Let's hear it," said Humpty Dumpty. "I can explain all the poems that ever were invented — and a good many that haven't been invented just yet."

*Id.* at 270.

<sup>3</sup> 11 U.S.C. §§ 101-1330 (1988) (hereinafter, the "Code"). Generally, this Article denotes by "section" both sections (*e.g.*, "§ 550") and subsections (*e.g.*, "§ 547(b)(1)") of the Code. The term "subsection," however, will refer to subsections only.

<sup>4</sup> William H. Rehnquist was appointed Chief Justice of the Supreme Court of the United States on September 26, 1986. Of the opinions analyzed at length in Section II of this Article, only *Midlantic National Bank v. New Jersey Dep't of Environmental Protection*, 474 U.S. 494 (1986), which has been included as a point of reference and departure, was not decided by the "Rehnquist Court."

<sup>5</sup> *Union Bank v. Wolas*, 112 S. Ct. 527, 530 (1991) (footnote omitted) (ordinary course of business exception to avoidance of preferential transfers equally applica-

and consistent" with the remainder of the Code and with other statutes, the section's legislative history will generally be deemed irrelevant.<sup>6</sup>

However, if the provision as written is "open to interpretation," and if bankruptcy law under "the proposed interpretation, [(even if literal) is] in clear conflict with state or federal laws of great importance,"<sup>7</sup> the Court will review the provision's legislative history. The drafters' intent, as revealed by such an inquiry, will then take precedence over construction of the provision's "plain meaning."<sup>8</sup>

By encouraging a relatively straightforward reading of the Code, this approach in theory increases the predictability of bankruptcy decisions and thus decreases the volume of litigation over the statute's construction. In practice, though, the Court has arguably championed policy over punctuation, and pre-Code precedent over linguistic logic. The "plain meaning" approach, like the Code itself, appears structured and principled but actually remains susceptible to conflicting interpretations and applications.<sup>9</sup> Part II of this Arti-

---

ble to "long-term" and "short-term" debt). See *infra* notes 176-203 and accompanying text for a discussion of *Wolas*.

<sup>6</sup> *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235 (1989) (creditor may receive postpetition interest on nonconsensual oversecured claim). See *infra* notes 86-128 and accompanying text for a discussion of the *Ron Pair* decision.

<sup>7</sup> *Ron Pair*, 489 U.S. at 245.

<sup>8</sup> *Id.* at 245-46.

<sup>9</sup> Humpty Dumpty offers inspired and often colorful explanations of the "nonsense" words of "Jabberwocky":

Alice repeated the first verse:—

"'Twas brillig, and the slithy toves  
Did gyre and gimble in the wabe:  
All mimsy were the borogroves,  
And the mome raths outgrabe."

"That's enough to begin with," Humpty Dumpty interrupted:  
"there are plenty of hard words there. '*Brillig*' means four o'clock in  
the afternoon — the time when you begin *broiling* things for dinner."

... "and what are '*loves*'?" ...

"Well, '*loves*' are something like badgers — they're  
something like lizards— and they're something like  
corkscrews."

"They must be very curious-looking creatures."

"They are that," said Humpty-Dumpty: "also they make their  
nests under sundials — also they live on cheese."

LOOKING-GLASS, *supra* note 1, at 270-71.

However, by rejecting his interpretation of a more familiar word, Alice forces Humpty-Dumpty to reveal the true source of his hermeneutic confidence: "But 'glory' doesn't mean 'a nice knock-down argument,' Alice objected. 'When I use a word,' Humpty Dumpty said, in rather a scornful tone, 'it means just what I choose it to mean — neither more nor less.'" *Id.* at 269.

Indeed, the Supreme Court itself has moved from addressing the "plain mean-

cle analyzes the development of the "plain meaning" approach over the course of thirteen recent opinions, through the Court's 1992-93 term.<sup>10</sup> Part III discusses the ambiguities inherent in the "plain meaning" approach, and reviews the implications of this indeterminacy.

## II. CASE STUDIES

"The question is," said Alice, "whether you *can* make words mean so many different things."

"The question is," said Humpty Dumpty, "which is to be master — that's all."

Alice was too much puzzled to say anything; so after a minute Humpty Dumpty began again. "They've a temper, some of them — particularly verbs; they're the proudest— adjectives you can do anything with, but not verbs— however, *I* can manage the whole lot of them! Impenetrability! That's what *I* say!"

"Would you tell me, please," said Alice, "what that means?"

"Now you talk like a reasonable child," said Humpty Dumpty, looking very much pleased.<sup>11</sup>

### A. *Midlantic National Bank v. New Jersey Department of Environmental Protection*<sup>12</sup>

In *Midlantic*, the Court addressed the interpretation of a seemingly unambiguous Code provision that had neither a counterpart under the Bankruptcy Act nor a documented legislative history. Rejecting the literal reading of the Code section in question, the Court held that in enacting the Code, Congress had implicitly incorporated judicial precedent developed under the Code's predecessor, the Bankruptcy Act of 1898.<sup>13</sup>

Though responsive to emerging legislative concerns regarding environmental protection, the Court-created exception to the power of abandonment introduced ambiguities that are still be-

---

ing" of specialized terms of the Bankruptcy Code, as embedded in their statutory context, to interpreting more common phrases that are not regarded as bankruptcy's "terms of art." *See infra* notes 595-96. Arguably, a similar loss of interpretive certainty will result from this trend.

<sup>10</sup> Several other bankruptcy decisions of the Rehnquist Court have not been discussed in depth, but referred to solely for illustration of more general principles. *See, e.g., infra* notes 175, 247, 252, 659-76 and accompanying text.

<sup>11</sup> LOOKING-GLASS, *supra* note 1, at 269.

<sup>12</sup> 474 U.S. 494 (1986).

<sup>13</sup> Ch. 541, 30 Stat. 544 (generally dispersed throughout Title II).

ing resolved by lower courts. More generally, though reconfiguring a straightforward Code provision to conform both to pre-Code precedent and to post-Code legislation, *Midlantic* did not indicate the extent to which such extraneous material would be relied on by future interpreters of this statute.

### 1. Background

A processor of waste oil that was responsible for cleaning up at its New York and New Jersey facilities a total of "470,000 gallons of highly toxic and carcinogenic waste oil"<sup>14</sup> filed a Chapter 11 petition for reorganization and subsequently converted the case to a Chapter 7 liquidation. The environmental authorities of these two states asserted that the trustee's proposed abandonment of the facilities would contravene state laws and regulations concerning public health and safety. They argued that, if the trustee's security measures to prevent vandalism, fire, and public entry were discontinued, the leaking and deteriorating containers of oil would be far more likely to cause "explosion, fire, contamination of water supplies, destruction of natural resources, and injury, genetic damage, or death through personal contact."<sup>15</sup>

Under § 554(a) of the Code, "[a]fter notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate."<sup>16</sup> Observing that the abandonment power had not been statutory before the enactment of the Code, and that there existed no legislative history of this section, the Third Circuit concluded that this power had been derived from judicial precedent that had subordinated it to public health regulations.<sup>17</sup>

---

<sup>14</sup> *Id.* at 499 n.3.

<sup>15</sup> *Id.* (quoting Brief for United States as Amicus Curiae at 4, 23).

<sup>16</sup> 11 U.S.C. § 554(a) (1988). The words "and benefit" were added by the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, Tit. III, § 468(a), 98 Stat. 30. *Midlantic*, 474 U.S. at 496.

<sup>17</sup> *City of New York v. Quanta Resources Corp.* (*In re Quanta Resources Corp.*), 739 F.2d 912, 916 (3d Cir. 1984) (analyzing City and State of New York's conflict with trustee) (quoting *Otteneimer v. Whittaker*, 198 F.2d 289 (4th Cir. 1952):

It seems obvious to us that a rule which is not provided by statute but built up by the courts to facilitate the administration and distribution of the assets of a bankrupt estate should not be extended so as to reach such an unreasonable and unjust result. The judge-made rule must give way when it comes into conflict with a statute enacted in order to ensure the safety of navigation; for we are not dealing with a burden imposed upon the bankrupt or his property by contract, but a duty and a burden imposed upon an owner of vessels by an Act of Congress in the public interest.

*Id.* In *Otteneimer*, the Fourth Circuit had refused to allow the trustee to abandon

Those decisions revealed that "where important state law or general equitable principles protect some public interest, they should not be overridden by federal legislation unless they are inconsistent with explicit congressional intent such that the supremacy clause mandates their supersession by the abandonment power."<sup>18</sup>

Indeed, the Third Circuit construed at least three separate sections of the Code as indicating that the abandonment provision was not intended to preempt the exercise of state police power. First, the automatic stay of § 362 applies neither to a governmental unit's actions to enforce its police or regulatory power nor to the enforcement of judgments, except money judgments, obtained by the government in such proceedings.<sup>19</sup> Second, § 959 requires the trustee who manages or operates the debtor's

---

valueless barges that the bankrupt had insufficient funds to maintain or to remove from the harbor: the anticipated sinking of the barges would obstruct the passage of other vessels in the harbor, in violation of federal law.

In *In re Chicago Rapid Transit Co.*, 129 F.2d 1 (7th Cir.), *cert. denied*, 317 U.S. 683 (1942), the appellate panel, observing that the Bankruptcy Act by its own language did not explicitly supersede the state's power to regulate local railroads, subjected the trustees of a reorganizing railroad to regulations prohibiting the cancellation of service along a certain railway line. In like manner, the court in *In re Lewis Jones, Inc.*, 1 BCD 277 (Bankr. E.D. Pa. 1974), citing the equitable nature of the bankruptcy court, would allow the trustee to abandon underground steam pipes, vents and manholes only after the steam openings were filled and sealed.

The Third Circuit reached the same conclusions in the companion case concerning the New Jersey Department of Environmental Protection's suit against the trustee. *In re Quanta Resources Corporation*, 739 F.2d 927 (3d Cir. 1984). The majority held that the case "does not present us with a significantly different factual situation from that presented to us" by the companion case; nor did there appear a "principled distinction between the issues presented in this case and those presented in the companion *Quanta* case in which New York is the appellant. Thus the analysis and reasoning of 739 F.2d 912 apply equally to the case at bar." *Id.* at 928.

Similarly, Judge Gibbons's dissent "would affirm that bankruptcy court's order in this case for the same reasons stated in my dissent in the companion case." *Id.* at 929.

<sup>18</sup> *Quanta Resources Corp.*, 739 F.2d at 918. The Supremacy Clause of the United States Constitution states:

This Constitution, and the Laws of the United States which shall be made in pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. CONST. art. VI, § 2.

<sup>19</sup> 11 U.S.C. § 362(b)(4) & (5) (1988), respectively, provide that the automatic stay does not apply to "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power" or to "the enforcement of a judgment, other than a money judgment,

property to obey relevant state laws.<sup>20</sup> Finally, § 105 authorizes the bankruptcy court to “issue any order, process or judgment that is necessary or appropriate to carry out the provisions” of the Code.<sup>21</sup>

The dissent endorsed a more literal reading of the statute, particularly in the absence of legislative history for § 554(a). Because the petitioners had not challenged on appeal the bankruptcy court’s finding that the property was burdensome and of inconsequential value to the estate, the Code’s criteria for abandonment had been satisfied.<sup>22</sup> The precedent cited by the majority was far from dispositive, because it had been handed down before § 554 had allowed trustees to abandon burdensome property.<sup>23</sup> Moreover, unlike the automatic stay of § 362, the Code’s abandonment provision as written contains no exception prohibiting abandonment in cases of public interest.<sup>24</sup>

---

obtained in an action or proceeding by a governmental unit to enforce such governmental unit’s police or regulatory power.”

<sup>20</sup> As the court in *Quanta Resources Corp.* noted:

Except as provided in section 1166 [concerning reorganization of railroads], a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

*Quanta Resources Corp.*, 739 F.2d at 919 (quoting 28 U.S.C. § 959(b)).

Unlike the trustee, the Third Circuit found this provision applicable to liquidation proceedings:

[I]t would be an overly literal reading that would dismiss wholly the import of the provision on the ground that “abandonment” of property is distinguishable from “management” of property. The interests at stake are not so different; in each case the creditors have an interest in preserving the debtor’s estate so as to maximize their proportionate recovery . . . .

*Id.* at 920.

<sup>21</sup> 11 U.S.C. § 105 (1988).

<sup>22</sup> *Quanta Resources Corp.*, 739 F.2d at 923.

<sup>23</sup> *Id.* at 923-24.

<sup>24</sup> *Id.* at 924. Judge Gibbons explained:

[T]he plain language of [section 554] permits abandonment in this case; moreover, there is no legislative history to that section providing any exceptions to the statute or expressing any intent contrary to abandonment by a trustee of property found to be burdensome or of inconsequential value. A fair reading of section 554 permits abandonment in this case and thus avoids the constitutional question presented by the taking clause.

*Id.* at 925 (Gibbons, J., dissenting).



## 2. Honoring a Pre-Code Exception

Affirming the Third Circuit's decision, the Supreme Court inferred that the congressional enactment of § 554 incorporated the pre-Code judicial requirement of compliance with the restrictions of state and federal law.<sup>25</sup>

Justice Powell's majority opinion, like that of the Third Circuit, cited not only the existing exceptions from the automatic stay for government actions, but also the requirement that the trustee comply with state laws, as evidence that the Code's provisions for the trustee to abandon estate property did not preempt state environmental law.<sup>26</sup> Responding to the argument that Congress could have provided similarly explicit limitations on the abandonment power, the Court observed that the specific restrictions to the automatic stay power had been a congressional reaction to judicial interpretations between 1973 and 1978 that had greatly expanded the scope of the automatic stay; by contrast, precedent had "firmly established" at the time of the Code's enactment the exceptions to abandonment.<sup>27</sup> Finally, the post-Code enactment of the Resource Conservation and Recovery Act ("RCRA")<sup>28</sup> and the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA")<sup>29</sup> indicated a clear congressional intent to prevent, restrict and remedy the disposal of hazardous materials.<sup>30</sup>

The bankruptcy court, before authorizing abandonment, was therefore required to

formulat[e] conditions that will adequately protect the public's health and safety. Accordingly, without reaching the question whether certain state laws imposing conditions on abandonment may be so onerous as to interfere with the bankruptcy adjudication itself, we hold that a trustee may not abandon

---

<sup>25</sup> *Midlantic*, 474 U.S. at 500-01. The Court observed that "[t]he 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. . . . The Court has followed this rule with particular care in construing the scope of bankruptcy codifications." *Id.* at 501 (citing *Swarts v. Hammer*, 194 U.S. 441, 444 (1904) (extraordinary exemptions from nonbankruptcy law are accorded trustee only where Congress "clearly expressed" them); and *Palmer v. Massachusetts*, 308 U.S. 79, 85 (1939) (in absence of congressional "language fitting for so drastic a change," states' longstanding power over local railroad service was not withdrawn by grant to district courts of bankruptcy powers over railroads)).

<sup>26</sup> *Id.* at 502-05.

<sup>27</sup> *Id.* at 504.

<sup>28</sup> 42 U.S.C. §§ 6901-6992k (1988).

<sup>29</sup> 42 U.S.C. § 9601-9675 (1988).

<sup>30</sup> *Midlantic*, 474 U.S. at 505-06.

property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards.<sup>31</sup>

In a footnote, however, the Court characterized this environmental exception as "narrow":

[i]t does not encompass a speculative or indeterminate future violation of such laws that may stem from abandonment. The abandonment power is not to be fettered by laws or regulations not reasonably calculated to protect the public health or safety from imminent and identifiable harm.<sup>32</sup>

Although the parameters of this exception have been addressed by many different courts, the trustee's obligation to comply with state environmental laws in the context of abandonment remains open to interpretation.<sup>33</sup>

---

<sup>31</sup> *Id.* at 507 (footnote omitted).

<sup>32</sup> *Id.* n.9.

<sup>33</sup> Several courts have required strict compliance. *See, e.g.,* Lancaster v. State of Tennessee (*In re* Wall Tube & Metal Products Company), 831 F.2d 118, 122 (6th Cir. 1987) (whether trustee is liquidating, managing, or reorganizing debtor's estate, environmental hazard on estate's property is within his control and must be remedied); *In re* Microfab, Inc., 105 B.R. 161, 167-69 (Bankr. D. Mass.1989) (trustee must comply fully with state environmental laws, unless he does not have financial resources to satisfy their obligations); *In re* Peerless Plating Company, 70 B.R. 943, 947 (Bankr. W.D. Mich. 1987) (generally requiring full observance of state regulations); *In re* Stevens, 68 B.R. 774, 782 n.7 (D. Me. 1987) (*Midlantic* does not entitle bankruptcy court to make what is a quintessential legislative determination — that is, what set of conditions of hazardous waste storage will "adequately protect the public's health and safety"; such conditions are conditions that will provide for compliance with relevant state and local laws).

Other courts have found the trustee obligated only to prevent imminent harm. *See, e.g.,* *In re* Smith-Douglass, Inc., 856 F.2d 12, 16 (4th Cir. 1988) (before authorizing abandonment, bankruptcy court must determine whether risk of imminent harm exists in reference to design of state law or regulation alleged to have been violated; court must then impose conditions that will adequately protect public's health and safety under this law); *Leavell v. Karnes*, 143 B.R. 212, 218 (S.D. Ill. 1990) (bankruptcy court must first determine whether property poses immediate and identifiable threat to public health or safety; if so, court may allow abandonment only after proper steps taken to protect public); *In re* Shore Company, Inc., 134 B.R. 572, 578 (Bank. E.D. Tex. 1991) (trustee's right to abandon environmentally impacted estate property is limited only by precondition that trustee remediate any imminent and identifiable danger present on property proposed to be abandoned); *In re* FCX, Inc., 96 B.R. 49, 54 (Bankr. E.D.N.C. 1989) (full compliance with all environmental laws is not required prior to abandonment, but abandonment is not authorized when there is immediate threat to the public health and safety and imminent danger of death or illness); *White v. Coon (In re* Purco, Inc.), 76 B.R. 523, 533 (Bankr. W.D. Pa. 1987) (permitting abandonment when conditions are such that abandonment will not render public health and safety inadequately protected); *In re* Oklahoma Refining Company, 63 B.R. 562, 565 (Bankr. W.D. Okl. 1986) (allowing trustee who "has done what is reasonable under the circumstances" to abandon property where: (1) pollution at debtor's refinery does

Justice Rehnquist's dissent, which Chief Justice Burger and Justices White and O'Connor joined, relied first on a literal reading of § 554(a). The dissent asserted:

This language, absolute in its terms, suggests that a trustee's power to abandon is limited only by considerations of the property's value to the estate. It makes no mention of other factors to be balanced or weighed and permits no easy inference that Congress was concerned about state environmental regulations.<sup>34</sup>

Yet the majority had construed the very absence of a specific restriction, along with the lack of relevant legislative history for this provision, as an indication that Congress had tacitly incorporated judicial precedent into the Code.

Not only did the dissent distinguish the three pre-Code cases cited by the majority,<sup>35</sup> but it noted that even if those decisions were seen as directly relevant, "three rather isolated cases do not constitute the sort of settled law that we can fairly assume Congress intended to codify absent some expression of its intent to do so."<sup>36</sup> Nor could the majority rely on a leading bankruptcy treatise to support the proposition that the environmental exception to abandonment had been "well settled" before the Code's enactment.<sup>37</sup> Had

---

not present immediate and menacing harm to public health and safety; (2) abandonment will not aggravate existing situation, create a genuine emergency or increase the likelihood of disaster or intensification of polluting agents; and (3) whether abandonment is denied or approved, estate has no funds to finance closure plan or post-closure monitoring).

See NEW JERSEY BANKRUPTCY MANUAL (1993), at 3-158 to 3-160.

<sup>34</sup> *Midlantic*, 474 U.S. at 509 (Rehnquist, J., dissenting) (footnote omitted). The dissent suggested that it might be amenable to "a far narrower condition on the abandonment power than that announced by the Court today, such as where abandonment by the trustee itself might create a genuine emergency that the trustee would be uniquely able to guard against." *Id.* at 515 (Rehnquist, J., dissenting).

<sup>35</sup> The dissent pointed out that *Ottenheimer* did not seek to reconcile the Bankruptcy Code with state environmental law, but instead with another federal statute, which concerned preharbor blockage. *Midlantic*, 474 U.S. at 511-12 (Rehnquist, J., dissenting). Moreover, because *Chicago Rapid Transit* did not address prerequisites for abandonment, it should be regarded as dictum with respect to this aspect of the *Midlantic* analysis. *Id.*

Although acknowledging that *Lewis Jones*, 1 B.R. 277 (Bankr. E.D. Pa. 1974), "admittedly comes closer to supporting the Court's position than does *Ottenheimer*," the dissent nonetheless found that "it too turns on the judge-made nature of the abandonment power. Moreover, I do not believe that the isolated decision of a single Bankruptcy Court rises to the level of 'established law' that we can fairly assume Congress intended to incorporate." *Midlantic*, 474 U.S. at 512 (Rehnquist, J., dissenting).

<sup>36</sup> *Id.* at 512 (Rehnquist, J., dissenting).

<sup>37</sup> *Id.* Justice Rehnquist criticized the majority's apparent acceptance of the states' argument, which relied heavily upon a classic pre-Code bankruptcy treatise,

Congress been so inclined, it could have included in § 554 a restriction analogous to that of § 1170(a)(2), which specifically requires that the abandonment of railroad lines be "consistent with the public interest."<sup>38</sup>

Moreover, § 959(b) applies only to the trustee's management or operation of the property, and not to a debtor's application to abandon: the majority's construction of this provision to incorporate into § 554(a) the restrictions of state environmental laws "would create an exception to the abandonment power without a shred of evidence that Congress intended one."<sup>39</sup> Finally, to graft public interest restrictions onto § 554 under the equitable powers granted to the bankruptcy court by § 105 "would plainly be contrary to the purposes of the Code,"<sup>40</sup> because the estate's assets, and therefore future distributions to creditors, would be diverted towards cleanup of the property.

*Midlantic*, though avoiding ramifications of the Takings and Supremacy Clauses, alerted the bankruptcy community that a Code provision's "plain language" could be augmented by considerations of the pre-Code precedent that Congress, in enacting the Code, had not explicitly opposed. In addition, the policies expressed in other Code sections, as well as those endorsed by Congress in more recent statutes, could be used to justify judicially-created amendments, whose precise contours it could be left to the lower courts to develop.

---

COLLIER ON BANKRUPTCY (14th ed. 1978). *Id.* (quoting 4A COLLIER ON BANKRUPTCY 502-04) (14th ed. 1978), to the effect that "[r]ecent cases illustrate . . . that the trustee in the exercise of the power to abandon is subject to the application of general regulations of a police nature."'). *See also* *Quanta v. City of N.Y.*, 739 F.2d at 916 (same section of treatise).

Despite the Third Circuit's and majority's reliance on this treatise, Justice Rehnquist found the source insufficient "legislative history" on which to ground an interpretation of the Code. Indeed,

the proposition for which the section in Collier is cited is not the view that authority for abandonment is qualified by state police power, but instead the much less remarkable position that "[t]he concept of abandonment is well recognized in the case law. See 4A Collier P70.42[3]." In order to divine that the statutory power to abandon in the proposed Code was to be conditioned on compliance with state police power regulations, therefore, a Senator or Congressman would not merely have had to look at the legislative history of the precursor to the Code, but also would have had to read the several-page treatise section cited in that earlier legislative history.

*Midlantic*, 474 U.S. at 512-13 (Rehnquist, J., dissenting).

<sup>38</sup> *Id.* at 513 (Rehnquist, J. dissenting) (quoting 11 U.S.C. § 1170(a)(2) (1988)).

<sup>39</sup> *Id.* at 514 (Rehnquist, J., dissenting).

<sup>40</sup> *Id.* at 515 (Rehnquist, J., dissenting).

B. Kelly v. Robinson<sup>41</sup>

*Kelly*, decided the term after *Midlantic*, similarly concerned the interaction of the bankruptcy process with state laws—in this case, with statutes concerning the administration of Connecticut's criminal justice system. Unlike *Midlantic*, which had relied on pre-Code precedent to create an exception to the literal language of a Code provision, *Kelly* involved the interpretation of an existing Code exception, which concerned the dischargeability of an individual debtor's debts. In concluding that restitution obligations imposed by state criminal authorities as conditions of probation are not dischargeable in Chapter 7 proceedings, the Court not only adopted an uncharacteristically restrictive definition of "debt," but endorsed pre-Code precedent that actually *contradicted* explicit provisions of the Bankruptcy Act.

1. Background

As a condition of a five-year term of probation for her conviction of larceny in the second degree, Carolyn Robinson was required to make restitution for \$9932.95 of public assistance benefits that she had wrongfully received from the Connecticut Department of Income Maintenance ("CDIM"). In November 1980, the Connecticut Superior Court ordered Robinson to make monthly payments of \$100 to the Connecticut Office of Adult Probation ("COAP"), beginning in January, 1981.<sup>42</sup>

In early February 1981, Robinson filed a Chapter 7 petition. Upon obtaining her discharge three months later, she sought a determination that the restitution obligation was a debt dischargeable under § 727.<sup>43</sup> The bankruptcy court, adopting the

---

<sup>41</sup> 479 U.S. 36 (1986).

<sup>42</sup> Robinson v. Director, Office of Adult Probation (*In re Robinson*), 45 B.R. 423-24 (Bankr. D. Conn. 1984). The Supreme Court acknowledged "some uncertainty about the total amount Robinson was ordered to pay," because five years of monthly \$100 payments would account for only \$6000 of the \$9932.95 owed by the debtor. *Kelly*, 479 U.S. at 39 n.2.

<sup>43</sup> See generally 11 U.S.C. § 727(a) (1988). Under § 727(a), to further the debtor's "fresh start" the court is to grant a Chapter 7 individual debtor a discharge unless the debtor has: fraudulently transferred or destroyed estate property or records; committed perjury or made a false claim; refused to obey a lawful order of the court, or, in certain cases, to answer material questions; or has been previously granted a discharge under certain conditions. *Id.*; see also 11 U.S.C. § 524(a) (1988) (setting forth the effect of a bankruptcy discharge). Section 524 explains that a discharge

(1) voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any *debt* discharged under § 727 . . . ; [and]

analysis of a recent decision on similar facts,<sup>44</sup> held that, because COAP and CDIM had no statutory power to enforce their right to receive restitution payments,<sup>45</sup> they had no "right to payment" of restitution and therefore neither a "claim" nor a dischargeable "debt" as those terms are defined by the Code.<sup>46</sup> Moreover, the court noted, it would be an unsound policy choice to allow criminals to avoid their restitution obligations by instituting bankruptcy proceedings.<sup>47</sup> In fact, even if the restitution obligation could be construed as a "debt" within the meaning of the Bankruptcy Code, it would constitute a "penalty" that would be excepted from discharge under § 523(a)(7).<sup>48</sup>

---

(2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover, or offset any such *debt* as a personal liability of the debtor, whether or not discharge of such debt is waived . . . .

*Id.* (emphasis added).

<sup>44</sup> *In re Pellegrino*, 42 B.R. 129 (Bankr. D. Conn. 1984) (Pellegrinos' obligation to make restitution for food stamps that Mrs. Pellegrino had fraudulently received did not constitute dischargeable "debt" under the Code), *cited by Robinson*, 45 B.R. at 424.

<sup>45</sup> The penal code of Connecticut, under which restitution was one of nine possible conditions of probation, provides for the criminal defendant to make payments to COAP, which then forwards funds to the victim. This statute does not, however, furnish a private victim with any means of enforcing the restitution order against a recalcitrant defendant; nor could the State, in the absence of a direct individual victim of Mrs. Pellegrino's fraud, claim greater rights against her. *Pellegrino*, 42 B.R. at 132-34.

<sup>46</sup> *Robinson*, 45 B.R. at 424-25. See 11 U.S.C. § 101(12) (1988) (defining "debt" for bankruptcy purposes as "liability on a claim") and 11 U.S.C. § 101(5) (defining "debt" for bankruptcy purposes). Under § 101(5), "claim" means

(A) *right to payment*, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or

(B) right to an equitable remedy for breach of performance if such breach gives rise to a right for payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured[.]

11 U.S.C. § 101(5) (1958) (emphasis added.)

<sup>47</sup> *Pellegrino*, 42 B.R. at 134.

<sup>48</sup> *Robinson*, 45 B.R. at 425. Under § 523(a)(7), an individual debtor is generally not discharged from a debt "to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss."

*Pellegrino* held that

[i]t is a distortion of bankruptcy law and policy to view Code § 523(a)(7) as a shield to restitution obligations in the context of this proceeding. . . . The bankruptcy laws were not enacted and must not be interpreted to provide a refuge to criminals. The plaintiffs bargained in state court for Pellegrino's freedom [on the condition that

Although the district court, in an unpublished opinion, upheld the bankruptcy court's proposed order, the Second Circuit reversed.<sup>49</sup> "First, the literal terms of [the Code's definition of "claim"] are sufficiently broad — apparently by congressional design — to define as a debt a restitution obligation as to which *any* person or entity, not just the crime victim, has a right to payment"<sup>50</sup>; and, unlike a private victim, COAP had the right to enforce the restitution obligation. Second, policy grounds supported the inclusion of the right of restitution in the definition of "claim." Although contradicting the great weight of precedent,<sup>51</sup> this conclusion avoided "the anomalous result that no holder of a right to restitution could participate in the bankruptcy proceeding or receive any distributions of the debtor's assets in liquidation. There is no evidence that Congress intended such a result."<sup>52</sup>

The Second Circuit also rejected the argument that the dischargeability of restitution obligations would provide "a haven for criminal offenders."<sup>53</sup> The court of appeals observed that this threat had been addressed by the automatic stay for criminal

---

restitution would be made]. This court will not permit them to escape the full obligations of that bargain.

*Pellegrino*, 42 B.R. at 138-39.

<sup>49</sup> *Robinson v. McGuigan (In re Robinson)*, 776 F.2d 30 (2d Cir. 1985).

<sup>50</sup> *Id.* at 34. The Second Circuit cited various congressional reports indicating that "claim" was to be construed as broadly as possible. *Id.* at 34-35 (quoting H.R. REP. NO. 595, 95th Cong., 2d Sess. 309, reprinted in 1978 U.S.C.C.A.N. 5963, 6266 (new definition of "claim" in § 101(4) is the "broadest possible definition," under which "all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the bankruptcy case. It permits the broadest possible relief in the bankruptcy court."); and citing the Senate report that accompanied S.2266, reprinted in BANKRUPTCY REFORM ACT OF 1978: HEARINGS ON S.2266 AND H.R. 8200 BEFORE THE SUBCOMM. ON IMPROVEMENT IN JUDICIAL MACHINERY OF THE SENATE COMM. ON THE JUDICIARY, 95th Cong., 1st Sess. 3 (1977) (containing identical language to that of § 104(A), and explanation similar to that included in House Report)).

<sup>51</sup> The appeals court found only one reported decision supporting its view that an obligation to make criminal restitution constituted a debt. In *In re Brown*, 39 B.R. 820 (Bankr. M.D. Tenn. 1984), the bankruptcy court characterized as a "debt" the debtor's obligation, as a condition of his probation, to pay restitution to an individual whose property he had damaged while driving "under the influence": the court reasoned that an equivalent judgment for the victim's compensation would itself be a dischargeable "debt."

<sup>52</sup> *Id.* at 36. The Second Circuit noted that the Bankruptcy Act of 1898 recognized as a provable claim a judgment ordering restitution of a fixed sum. "Since Congress intended its definition of 'claim' in the Code to expand the class of obligations that would be dischargeable, it is hardly conceivable that it thought that a right to restitution provable under the 1898 Act would now be construed as outside of the Code's broad definition of claim." *Id.*

<sup>53</sup> *Id.* at 37 (quoting H.R. REP. NO. 595, 95th Cong., 2d Sess. 342, reprinted in

actions or proceedings against the debtor.<sup>54</sup> In fact, the very existence of that exception, as well as the explicitly nondischargeable status of debts to or for the benefit of governmental units for fines, penalties, and forfeiture under § 523(a)(7), supported the view that Congress had not intended to exclude criminals entirely from the protection of the Code's provisions. In the context of this careful statutory balance of interests, "it is inappropriate for a court, based on its own view as to the relative importance of [any] policy, to create judicial exceptions to the clear language of the statute that are warranted neither by that language nor by the legislative history."<sup>55</sup>

Unlike the bankruptcy court, the Second Circuit held that COAP had an enforceable right to receive restitution payments from the debtor, even though the amount of the payments had been fixed by the Connecticut sentencing court and even though the debtor stood to lose her freedom, rather than her property, as a penalty for noncompliance.<sup>56</sup> Therefore, the debtor's obligation qualified as a "debt" within the meaning of the Code.<sup>57</sup>

On the issue of dischargeability, the appeals court found "no question" but that the first two criteria for dischargeability under § 523(a)(7) had been met: Robinson's debt was to some extent a "penalty" for her crime, and it was payable "to and for the benefit of a governmental unit."<sup>58</sup> The debt did not fall within the scope of this section,<sup>59</sup> however, because the debtor's obligation was actually compensatory. First, the state statute involved allowed the state court to order a criminal to "make restitution of the fruits of his offense or make restitution, in an amount he can afford to pay or provide in a suitable manner, *for the loss or damage caused thereby*."<sup>60</sup> Second, notwithstanding any compensatory

---

1978 U.S.C.C.A.N. 5963, 6299; and S. REP. No. 989, 95th Cong., 2d Sess. 51, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5837).

<sup>54</sup> Under § 362(b)(1), the automatic stay does not apply to "the commencement or continuation of a criminal action or proceeding against the debtor[.]" 11 U.S.C. § 362(b)(1) (1988).

<sup>55</sup> *Robinson*, 776 F.2d at 38 (citations omitted).

<sup>56</sup> *Id.* at 38-39.

<sup>57</sup> *See supra* note 46.

<sup>58</sup> *Robinson*, 776 F.2d at 40.

<sup>59</sup> *Id.* at 40-41. Because the relevant Connecticut agencies had not timely objected to the discharge, as required by § 523(c), the debt might have been nondischargeable under § 523(a)(2) (concerning debts "for obtaining money, property [or] services" by false pretenses, fraud, or a fraudulent writing) or § 523(a)(4) (concerning debts "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny"). *Robinson*, 776 F.2d at 39.

<sup>60</sup> *Id.* at 40 (quoting CONN. GEN. STAT. ANN. § 53a-30(a)(4) (West 1985 & Supp. 1993)) (emphasis added).



conditions of probation, the "actual pecuniary loss" involved was in the exact amount of the loss suffered by the CDIM. Third, though the restitution payments were made by the debtor to COAP, they were forwarded to CDIM.<sup>61</sup>

The Second Circuit thus reversed the district court's order and remanded the matter to that court for an order declaring the debtor's restitution obligation discharged, as well as an order enjoining COAP and CDIM from taking steps to recover further restitution payments.<sup>62</sup> In a concurring opinion, one judge suggested that Congress amend § 523(a)(7) to prevent "the unfortunate result compelled by the [literal] language of the relevant provisions of the Bankruptcy Code."<sup>63</sup> To preclude convicted criminals from declaring bankruptcy as a means of discharging their restitution obligations, Judge Mansfield asserted, courts would be forced to impose punishments in the form of fines, penalties, or forfeitures, which would not qualify as nondischargeable under that subsection.<sup>64</sup>

## 2. Adopting Precedent Contradicting the Bankruptcy Act

The Supreme Court's majority opinion, delivered by Justice Powell, reversed the Second Circuit. As opposed to that court of appeals, the high Court began from the position that "the [statutory] text is only the starting point [to be considered] in light of the history of bankruptcy court deference to criminal judgments and in light of the interests of the States in unfettered administration of their criminal justice systems."<sup>65</sup>

Before the enactment of the Code, courts had generally agreed that a bankruptcy discharge would not affect state criminal judgments that had been rendered against the debtor.<sup>66</sup> Indeed, the Court could locate only one federal decision in which a criminal court sentence had been affected by the criminal's discharge under the Bankruptcy Act.<sup>67</sup> This common policy choice had diverged, however, from the plain intent of § 57(j), § 63 and § 17 of the Bankruptcy Act, which respectively: rendered unallowable debts owed to government entities; enunciated the scope

---

<sup>61</sup> *Id.* at 40-41.

<sup>62</sup> *Id.* at 41.

<sup>63</sup> *Id.* at 41-42 (Mansfield, J., concurring).

<sup>64</sup> *Id.* at 41 (Mansfield, J., concurring).

<sup>65</sup> *Kelly v. Robinson*, 479 U.S. 36, 43-44 (citations omitted).

<sup>66</sup> *Id.* at 45-47.

<sup>67</sup> *Id.* at 45 n.6 (citing *In re Alderson*, 98 F. 588 (W. Va. 1899) (discharge releases debtor from judgments assessed against him prepetition in connection with misdemeanor of unlawful retailing)).

of debts to be released upon discharge (*without* exception for criminal penalties); and exempted four specific groups of debts (*not including* criminal penalties) from discharge.<sup>68</sup> The majority attributed the reluctance of prior courts to follow the terms of the Act to "a deep conviction that federal bankruptcy courts should not invalidate the results of state criminal proceedings,"<sup>69</sup> or "limit the rehabilitative and deterrent options available to state criminal judges."<sup>70</sup>

In what might be called an instance of judicial jiu-jitsu, the Supreme Court cited the Bankruptcy Act's own depth and detail as evidence that *contrary* judicial precedent should be incorporated into the Code.<sup>71</sup> After briefly reviewing the *Midlantic* decision, in which "we declined to hold that the new Bankruptcy Code silently abrogated another exception created by courts construing the old Act,"<sup>72</sup> the *Kelly* Court insisted that the Code's literal terms were "subject to interpretation,"<sup>73</sup> and that the legislative history of § 523(a)(7) did not support the conclusion "that this language should be read so intrusively" as to discharge a debtor's state-ordered obligation of restitution.<sup>74</sup> Indeed, controversy would have marked the legislative history had such a significant change in existing practice been intended.<sup>75</sup>

Similarly, despite the language and legislative history that would justify a broad construction of dischargeable "debts" as defined by § 101(4), the Court's examination of the "state of the law"<sup>76</sup> before the enactment of the Code raised "serious doubts" that Congress had intended to include criminal penalties within this definition.<sup>77</sup> Finally, although three members of the *Kelly* majority had not been satisfied in *Midlantic* by a leading bankruptcy treatise's summary of pre-Code law,<sup>78</sup> here that same commentary was cited with approval for the proposition that "fines

---

<sup>68</sup> *Id.* at 44-45.

<sup>69</sup> *Id.* at 47.

<sup>70</sup> *Id.* at 49.

<sup>71</sup> See *id.* at 46 ("Congress enacted the Code in 1978 against the background of an established judicial exception to discharge for criminal sentences, including restitution orders, an exception created in the face of a statute drafted with considerable care and specificity.").

<sup>72</sup> *Id.* at 47.

<sup>73</sup> *Id.* at 50.

<sup>74</sup> *Id.* at 50.

<sup>75</sup> *Id.* at 51.

<sup>76</sup> *Id.* at 50 n.12.

<sup>77</sup> *Id.* at 50.

<sup>78</sup> See *supra* note 37 and accompanying text for a discussion of the *Midlantic* court's treatment of *Collier on Bankruptcy*.

and penalties are not affected by a discharge."<sup>79</sup>

In analyzing § 523(a)(7), the Court agreed with the Second Circuit that Robinson's restitution obligations were for the benefit of the state.<sup>80</sup> Unlike the court of appeals, however, the majority found that these obligations were not intended to compensate the victim, but rather to further the state's "penal and rehabilitative interests."<sup>81</sup> The noncompensatory character of these payments was supported by the victim's failure to control either the decision to award restitution (which generally hinged on the state's penal goals and the defendant's situation, rather than on the harm caused) or the amount awarded.<sup>82</sup> The majority also observed that the Connecticut statute at issue afforded eight possible alternatives, as well as a catchall provision, for probation arrangements. As one of these alternatives, the restitution option called for the court to fix the amount and manner of the defendant's restitution "in an amount he can afford to pay or provide in a suitable manner, for the loss or damage caused thereby."<sup>83</sup>

In holding that the debtor's restitution obligations were not dischargeable, the Court cast itself as preserving the integrity of criminal proceedings in state court.<sup>84</sup> By contrast, it observed, the Second Circuit's holding would inevitably have compelled state prosecutors to defend state criminal judgments in federal bankruptcy court, and would have affected the state criminal judges' choice of alternatives among imprisonment, fines and restitution.<sup>85</sup>

Justice Marshall's dissent, which was joined by Justice Stevens, suggested that the majority had adopted an unnatural construction of § 523(a)(7) and of Connecticut's probation statute in order to nullify the State's failure to object timely to the dis-

---

<sup>79</sup> *Kelly*, 479 U.S. at 46 (quoting 1A COLLIER ON BANKRUPTCY 1609-10 & n.10 (14th ed. 1978)). The Court found that the inability of a discharge in bankruptcy to modify a criminal judgment against the debtor "was so widely accepted by the time Congress enacted the new Code that a leading commentator could state flatly that 'fines and penalties are not affected by a discharge.'" *Id.*

<sup>80</sup> *Id.* at 53. The Court reached this conclusion "[b]ecause criminal proceedings focus on the State's interest in rehabilitation and punishment, rather than the victim's desire for compensation." *Id.*

<sup>81</sup> *Id.* (footnote omitted).

<sup>82</sup> *Id.* at 52-53.

<sup>83</sup> *Id.* at 52 (quoting CONN. GEN. STAT. § 53a-30(a)(4) (West 1985 & Supp. 1993)).

<sup>84</sup> *Id.* at 47.

<sup>85</sup> *Id.* at 48 (footnote omitted).

charge of the debtor's restitution obligations.<sup>86</sup> On a more theoretical level, the dissent understood that "[w]hile restitution imposed as a condition of probation under the Connecticut statute is in part a penal sanction, it is also intended to compensate victims for their injuries," as evidenced by the statute's explicitly linking the amount of restitution to "the loss or damage caused" by the defendant.<sup>87</sup> In this connection, it was irrelevant that the victim could not control either the imposition of an obligation of restitution or its amount.<sup>88</sup> Moreover, instead of abrogating the pre-Code precedent that held fines and penalties nondischargeable, Congress had in the Code both "codified that law *and* added the requirements of section 532(a)(7)."<sup>89</sup>

The majority's characterization of the debtor's restitution payments as "to and for the benefit of a governmental unit" had been satisfied in the present situation because the debtor had defrauded a state agency. In cases where the victim was not itself a governmental unit, however, the majority's conclusion could be sustained only on the more general principle that *all* restitution payments benefit the government, and thereby all governmental units, by preserving order. Yet "if the requirement is to be read so broadly . . . *any* fine, penalty, or forfeiture would be for the benefit of a governmental unit, making this qualification in section 523(a)(7) superfluous."<sup>90</sup> In addition, the restitution obligation could hardly avoid being characterized as a "debt" under the Code's sweeping definitions of "debt" and "claim."<sup>91</sup> As the Second Circuit had concluded, the "right of payment" held by COAP should be no less effective if Robinson's nonpayment of restitution obligations would be grounds for her incarceration, rather than for levy and execution upon her property.<sup>92</sup>

Finally, the majority's considerations of the relative authorities of state and federal courts could be seen as more properly within the jurisdiction of Congress. Like the Second Circuit's concurrence, the Supreme Court's dissent suggested that Con-

---

<sup>86</sup> *Id.* at 53-54 (Marshall, J., dissenting).

<sup>87</sup> *Id.* at 55 (Marshall, J., dissenting).

<sup>88</sup> *Id.* at 56 (Marshall, J., dissenting) (footnote omitted).

<sup>89</sup> *Id.* at 55 n.2 (Marshall, J., dissenting) (emphasis added).

<sup>90</sup> *Id.* at 56 n.3 (Marshall, J., dissenting).

<sup>91</sup> *Id.* at 56 (Marshall, J., dissenting) (citing H.R. REP. NO. 595, 95th Cong., 2d Sess. 309 (1977); S. REP. NO. 989, 95th Cong., 2d Sess. 22 (1978), *reprinted in* 1978 U.S.C.A.N. 5808, 6266 ("claim" to be given "broadest possible definition"); and *Ohio v. Kovacs*, 105 S. Ct. 705, 708 (1985) (Congress desired broad definition of "claim")).

<sup>92</sup> *Id.* at 57 (Marshall, J., dissenting).

gress could, "if it were so inclined, . . . amend the Bankruptcy Code specifically to make criminal restitution obligations nondischargeable in bankruptcy."<sup>93</sup>

The dissent's arguments would soon win the day in a case strikingly similar on its facts.

3. Sounding the Retreat? *Pennsylvania Dept. of Public Welfare v. Davenport*<sup>94</sup>

Four terms after handing down *Kelly*, the Court adopted a closer reading of the Code in declaring that restitution payments imposed as conditions of probation in state criminal actions *were* dischargeable in chapter 13 proceedings. Deferring not to pre-Code policy, as it had in *Kelly*, but instead to the literal language of the statute, the Court found itself "guided by the fundamental canon that statutory interpretation begins with the language of the statute itself."<sup>95</sup> Justice Marshall's majority opinion salvaged a key argument of his *Kelly* dissent: that the Code's broad definitions of "debt" as "liability on a claim," and of "claim" as a "right to payment," included those restitution claims enforced by the state's threat of incarceration for nonpayment.<sup>96</sup>

The United States, as *amicus* on behalf of the Department of Public Welfare, argued that restitution obligations could be pursued by an exemption provided under § 362(b)(1) from the automatic stay of "the commencement or continuation of a criminal action or proceeding against the debtor."<sup>97</sup> However, the Court concluded that "the language [and] the structure of the Code as a whole" undercut this reasoning: not only did that section not specifically exempt actions to collect restitution obligations, but "Congress could well have concluded that . . . in the context of Chapter 13, a debtor's interest in full and complete release of his obligations outweighs society's interest in collecting or enforcing a restitution obligation outside the agreement reached in the Chapter 13 plan."<sup>98</sup>

The United States also argued that the parity between the treatment of claims in chapters 7 and 13 restricted to *civil* fines

---

<sup>93</sup> *Id.* at 58-59 (Marshall, J., dissenting) (footnote omitted).

<sup>94</sup> 495 U.S. 552 (1990).

<sup>95</sup> *Id.* at 557-58.

<sup>96</sup> *Id.* at 557-58 (quoting §§ 101(11) and 101(4)(A)).

<sup>97</sup> *Id.* at 560 (quoting § 362(b)(1)).

<sup>98</sup> *Id.* at 560-61.

and penalties the exception to discharge. Section 1325(a)(4)<sup>99</sup> mandates that a chapter 13 plan leave creditors at least as well off as they would have been in chapter 7; yet § 726(a)(4) provides only a fourth priority to allowed claims for “any fine, penalty or forfeiture . . . to the extent that such *fine, penalty, or forfeiture*, or damages are not compensation for actual pecuniary loss suffered by the holder of such claim.”<sup>100</sup> Surely, Congress could not have intended to accord such a low priority to criminal fines and penalties!<sup>101</sup>

The Court disposed of this contention by observing that *Kelly*'s analysis of § 523(a)(7) had construed “fine, penalty, or forfeiture” as including criminal fines and penalties.<sup>102</sup> Indeed, if “debt” were read to exclude criminal restitution orders, § 523(a)(7)'s “codification of the judicial exception for criminal restitution orders” would be rendered superfluous.<sup>103</sup> Finally, Congress had deliberately balanced the attractiveness of chapters 7 and 13 by granting chapter 13 debtors a wider range of discharge: some of § 523(a)'s exceptions to discharge, including § 523(a)(7)'s exception for debts arising from a “fine, penalty, or forfeiture,” are not applicable to chapter 13 proceedings.<sup>104</sup>

The majority distinguished *Kelly* by the very principle of statutory interpretation that *Midlantic*, and *Kelly* itself, had endorsed: “We will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure.”<sup>105</sup> Although *Kelly*'s examination of “past bankruptcy practice” had revealed a pre-Code aversion to disturbing state criminal judgments through bankruptcy proceedings, such an investigation would not be warranted in *Davenport*, where “the statutory language [of § 1328] plainly reveals Congress's intent not

---

<sup>99</sup> Section 1325(a)(4) imposes as a condition of confirmation that a chapter 13 plan ensure that

the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date.

<sup>100</sup> 11 U.S.C. § 726(a)(4) (1988) (emphasis added).

<sup>101</sup> *Kelly*, 495 U.S. at 561.

<sup>102</sup> *Id.* at 561-62. Although in *Davenport* “[t]he United States acknowledge[d] that the phrase ‘fine, penalty, or forfeiture’ as it appears in § 726(a)(4) must have the same meaning as in § 523(a)(7),” *id.*, the Court would later find much more troublesome the principle that a phrase retains the same meaning in different sections of the Code. See *infra* notes 597-602 and accompanying discussion.

<sup>103</sup> *Id.* at 562.

<sup>104</sup> *Id.* at 563.

<sup>105</sup> *Id.* at 563 (citing *Kelly*, 479 U.S. at 47 (in turn citing *Midlantic*)).

to except restitution orders from discharge in certain Chapter 13 proceedings."<sup>106</sup>

Justice Blackmun's *Davenport* dissent, which was joined by Justice O'Connor, looked beyond the literal language of the Code to conclude that the majority's interpretation produced "a result demonstrably at odds with the intention of [the Code's] drafters."<sup>107</sup> First, neither the statutory definition nor its legislative history indicated that obligations resulting from criminal restitution orders constituted "rights to payment," or claims, that gave rise to debts that could in turn be discharged in chapter 13 proceedings.<sup>108</sup> Second, to allow such obligations to be discharged would contradict the pre-Code precedent, examined at length in *Kelly*, of respecting both the "history of bankruptcy court deference to criminal judgments and . . . the interests of the States in unfettered administration of their criminal justice systems."<sup>109</sup> The dissent's own analysis revealed that "under the 1898 Act . . . criminal monetary sanctions were not 'debts' for the purpose of pre-Code bankruptcy proceedings."<sup>110</sup>

Nor did the Code's broad definition of "debt" provide a clear indication that in enacting the Code Congress had intended to change this practice. Indeed, *Kelly* itself had explicitly rejected such an argument, holding that "nothing in the legislative history of these sections compels the conclusion that Congress intended to change the state of the law with respect to criminal judgments."<sup>111</sup> Moreover, the legislative history indicated that "[t]he bankruptcy laws are not a haven for criminal offenders."<sup>112</sup>

The enactment of § 523(a)(7), observed the dissent,

---

<sup>106</sup> *Id.* At the time of the *Davenport* decision, § 1328(a), which specifies the types of debts that are not dischargeable after the debtor has completed all payments under his chapter 13 plan, did not mention restitution obligations. However, Congress subsequently amended this section to include as nondischargeable "debts for restitution included in a sentence on the debtor's conviction of a crime." 11 U.S.C. § 1328(a)(3) (1990), added by the Crime Control Act of 1990, Pub. L. No. 101-647, § 3103, 101 Stat. 4789, 4916, and Criminal Victims Protection Act of 1990, Pub. L. No. 101-581, § 3, 104 Stat. 2865, 2865 (providing identical language).

<sup>107</sup> *Davenport*, 495 U.S. at 565 (Blackmun, J., dissenting) (quoting *Ron Pair*, 489 U.S. at 242 (Blackmun, J., dissenting)).

<sup>108</sup> *Id.* "The statute, on its face, is not self-defining and surely does not compel the result that criminal restitution orders constitute 'debts.' " *Id.* at 567 (Blackmun, J., dissenting).

<sup>109</sup> *Id.* at 567 (Blackmun, J., dissenting) (quoting *Kelly*, 479 U.S. at 44).

<sup>110</sup> *Id.* at 569 (Blackmun, J., dissenting).

<sup>111</sup> *Id.* at 570 (Blackmun, J., dissenting) (quoting *Kelly*, 479 U.S. at 50 n.12).

<sup>112</sup> *Id.* (quoting H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 342, codified at 1978 U.S.C.A.N. 6299 (reviewing extent of automatic stay)).

does little to demonstrate clear congressional intent to change traditional pre-Code practice. Even if [that section] can be interpreted as making criminal restitution orders not dischargeable, this does not mean that Congress intended to make criminal restitution orders debts. Under pre-Code practice, nondischargeability of a criminal restitution order would be evidence that it was not a debt at all. Congress gave no indication that it intended to break with this pre-Code conception of dischargeability when it enacted § 523(a)(7).<sup>113</sup>

Justice Blackmun thus maintained that *Davenport* precisely the spectre that *Kelly* had sought to dispel: that sentencing courts would be encouraged to impose prison sentences rather than restitution obligations, because convicted criminals could evade the latter but not the former by seeking the protection of chapter 13. Observed the dissent, "Congress surely would not have enacted legislation with such an extraordinary result without at least some discussion of its consequences."<sup>114</sup>

Although called into question by the *Davenport* decision, the logic of *Kelly*, like that of *Midlantic*, undermined any reliance on a literal approach to the Bankruptcy Code. Yet if *Midlantic* and *Kelly* clearly illustrated the use of legislative history to overcome the Code's "plain meaning," the Court would soon refine its approach. The next major decision on the interpretation of the Code would find the Justices split over the criteria for resorting to an examination of legislative history. It would also mark the Court's rejection of a specific set of precedent as insufficient to establish a pre-Code practice that Congress could tacitly have imported into the Code.

C. U.S. v. Ron Pair Enterprises, Inc.<sup>115</sup>

In *Ron Pair*, the Court rejected the presumption of *Midlantic* and *Kelly* that, in enacting the Code, Congress had adopted those existing judicial constructions that it did not explicitly reject. Under the new test, the legislative history of a provision would be relevant to its interpretation only if the provision itself was sus-

---

<sup>113</sup> *Id.* at 572 (Blackmun, J., dissenting).

<sup>114</sup> *Id.* at 573 (Blackmun, J., dissenting). *Cf.* *Grogan v. Garner*, 498 U.S. 279, 290-91 (1990) (standard of proof for dischargeability exceptions in § 523(a) is ordinary "preponderance of the evidence" standard; because, at the time of Code's enactment, courts continued to be nearly evenly split over appropriate standard of proof, it would not be reasonable to conclude that in enacting this section Congress silently endorsed background rule that "clear and convincing" evidence is required to establish exemptions from discharge).

<sup>115</sup> 489 U.S. 235 (1989).



ceptible to a reasonable interpretation that clearly conflicted with important state or federal legislation.

Analyzing the effect of a strategically-placed comma so as to endorse the "plain meaning" of the provision in question, the Court nonetheless considered precedent to the contrary, if only to dismiss these decisions as mere guides for the exercise of the court's equitable powers.

### 1. Background

*Ron Pair* addressed whether the federal government was entitled to postpetition interest on its oversecured claim for unpaid withholding and social security taxes, which claim had been perfected through a tax lien on the chapter 11 debtor's property. Central to the analysis was the degree to which the Code should recognize the pre-Code distinction between voluntary and involuntary secured claims.

If a creditor's claim against an estate is secured by a lien on property in which the estate has an interest, Bankruptcy Code § 506(a) divides the claim into a secured claim, to the extent of the value of the creditor's interest in the estate's interest in the property, and an unsecured claim, in the value of the remainder of the allowed claim.<sup>116</sup> Section 506(b) entitles the creditor to postpetition interest on the secured claim, provided that the claim is still oversecured after the value of the benefit to the holder of the trustee's preserving and disposing of the property is deducted from the value of the property:

To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges

---

<sup>116</sup> Section 506(a) provides that

An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

11 U.S.C. § 506(a) (1988).

*provided for under the agreement under which such claim arose.*<sup>117</sup>

In asserting diametrically opposed interpretations of this provision, the parties advanced arguments both grammatical and historical. The debtor read the emphasized clause to modify both "interest on such claim" and "any reasonable fees, costs, or charges," and so to incorporate pre-Code precedent restricting postpetition interest to oversecured consensual (i.e., contractual) claims. The Justice Department, however, saw the clause as modifying only "reasonable fees, costs or charges," and asserted that Congress had intended to provide for postpetition interest on oversecured *nonconsensual* claims as well.

The district court, relying on the "plain meaning" of the statutory section, reversed the bankruptcy court's judgment for the debtor.<sup>118</sup> In turn reversing the district court, the Sixth Circuit began its own analysis by finding that the ambiguity of the statute rendered pre-Code precedent relevant.<sup>119</sup> The court of appeals observed that a "well-established general rule" had once prohibited postpetition interest on both secured and unsecured claims, on the grounds that the allowance of such interest would have penalized those creditors to whose claims low interest rates applied, and would correspondingly have benefited those creditors whose claims involved higher interest rates.<sup>120</sup> Among the judicial exceptions that had arisen, however, was the allowance, to creditors with oversecured claims, of postpetition interest, to the extent that the value of the collateral would support the payment of such interest.<sup>121</sup>

---

<sup>117</sup> *Id.* § 506(b) (emphasis added).

<sup>118</sup> *United States v. Ron Pair Enterprises, Inc.* (*In re Ron Pair Enterprises, Inc.*), 59 A.F.T.R. 2d 87-386, 86-2 U.S.T.C. P 9642, 1986 WL 10091 (E.D. Mich. 1986). The court's two-paragraph opinion relied on *In re Colegrove*, 771 F.2d 119 (6th Cir. 1985) and *In re Best Repair Company, Inc.*, 86-1 U.S.T.C. P 9408, No. 85-1907 (4th Cir. 1986) to support its conclusion that the plain language of Section 506(b) entitled the United States to post-petition interest on its over-secured pre-petition tax claim.

<sup>119</sup> *United States v. Ron Pair Enterprises*, 828 F.2d 367 (6th Cir. 1987). The appeals court cited *Midlantic* and *Kelly* to the effect that "pre-Code law should be reviewed in order to better understand the context in which the provision was drafted and therefore the language itself." *Id.* at 370. The court also rejected the government's contention that this rule applied only if the pre-Code law involved overriding considerations of public policy: under a "well-established principle in bankruptcy law," the court could presume, in the absence of explicit indications to the contrary, that Congress had not intended "to deviate from the judicially created rule." *Id.* at 370 n.4.

<sup>120</sup> *Id.* at 370.

<sup>121</sup> *Id.* at 370. The other two exceptions arose where (1) the debtor was proven to be solvent and (2) where the property in which the creditor has a security interest produced income postpetition. *Id.*

This principle would give the benefit of the bargain to the oversecured creditor that had been able to extract beneficial contract terms and valuable collateral from the debtor prepetition. But because this analysis did not apply to tax liens or to other nonconsensual liens, postpetition interest would not be allowed on such claims, even if they were oversecured.<sup>122</sup>

The Sixth Circuit agreed with the debtor that § 506(b) should be read as codifying this judicially-created pre-Code exception.<sup>123</sup> This court of appeals dismissed the Fourth Circuit's own "plain meaning" approach to the provision,<sup>124</sup> reasoning that the Fourth

---

<sup>122</sup> *Id.* at 371 (citing *In re Kerber Packing Company*, 276 F.2d 245, 247 (7th Cir. 1960) (finding "a very clear distinction" between lien at issue, which was "a general lien perfected pursuant to the provisions of the Internal Revenue Code and [that] attaches upon all property and right to property, whether real or personal" and liens involved in cases allowing postpetition interest on oversecured creditor's claim, because each lien of the latter type addressed "a voluntary transaction between the debtor and creditor [in which] the payment of interest was contemplated by the parties"); *United States v. Highell*, 273 F.2d 682, 684 (10th Cir. 1959) (observing that no assertion made that government's claim for postpetition interest on income tax penalties fell within exceptions to general rule prohibiting postpetition interest); *United States v. Bass*, 271 F.2d 129, 131-32 (9th Cir. 1959) (noting in this context "a meaningful distinction . . . between statutory and contractual liens"); and *United States v. Harrington*, 269 F.2d 719, 721-24 (4th Cir. 1959) (questioning relevance of precedent allowing postpetition interest on "liens upon specific property of the bankrupt growing out of a contract between him and the creditor," because with one exception "no case found by us [on postpetition interest] involves a statutory lien upon all of the assets of the bankrupt."))

Two additional considerations distinguish tax liens from consensual liens. First, as opposed to contractual liens, tax liens often encumber all of the debtor's property, instead of a specific asset. *Id.* Moreover, because other creditors have no means to compel the debtor to pay its taxes in full, and thus to prevent the accrual of postpetition interest, "[t]o penalize these creditors for the bankrupt's inability to pay its taxes on time violates all notions of equity." *Id.* at 371 n.6.

Yet, as the Supreme Court would note in rejecting the Sixth Circuit's analysis, "modern commercial lending practices have changed, and it is not unusual for commercial lenders to obtain a lien on almost all of the debtor's property." *Ron Pair*, 489 U.S. at 247 n.9.

<sup>123</sup> *Id.* at 371-72. The Court of Appeals for the Sixth Circuit cited as support for this interpretation the opinions of "[s]everal bankruptcy courts, and at least one district court and one commentator [i.e., *Collier on Bankruptcy*]." *Id.* at 371. That treatise construed the placement of the comma after "interest on such claim," in § 506(b) to reflect the drafters' intent that interest was to be allowed only on the claim, and not on any other amount. *Id.* "This commentator notes, however, that a logical explanation for the comma is to allow for postpetition interest on nonconsensual lien claims, although [it] admittedly is not of that view." *Id.* (citing 3 COLIER ON BANKRUPTCY 506-43 & n.10 (15th ed. 1987)).

<sup>124</sup> In *In re Best Repair Co.*, the court observed that in § 506(b) [t]he phrase "interest on such claim" is set off by commas, and the following phrase is introduced by "and any." The effect of this usage is to make "interest on such claim" a separate and distinct clause to which "provided for under the agreement" does not apply. If Con-

Circuit had improperly dismissed considerations of pre-Code law.<sup>125</sup> There had been no explicit indication in the legislative history of the Code that Congress had abandoned the pre-Code exception; nor would the insertion of a comma and the words "and any" before the final phrase of § 506(b) suffice to express this intent.<sup>126</sup>

## 2. Reinterpreting *Midlantic* and *Kelly*

Reversing the Sixth Circuit's decision,<sup>127</sup> the Supreme Court

---

gress had wanted the agreement proviso to limit "interest on such claim" to consensual claims, it could easily have done so by listing seriatim and in parallel form the different items an over-secured creditor can recover subject to an agreement. Though Congress could have more clearly separated the interest clause from the agreement clause, we think that the natural meaning of its chosen words is to permit post-petition interest on nonconsensual oversecured claims.

789 F.2d 1080, 1082 (4th Cir. 1986) (footnotes omitted). The Fourth Circuit offered two alternate constructions that Congress could have employed had it intended to effect the opposite result, *id.* n.2, which result "strains the plain meaning of the language and grammar of the provision" as enacted. *Id.* at 1082.

<sup>125</sup> The Sixth Circuit indicated that

[i]n our view, the Fourth Circuit's conclusion in *Best Repair* is weakened by its subsequent acknowledgment that "§ 506(b) is not so clear that we would not consider its legislative history to aid our interpretation," and because it reaches its conclusion without a thorough discussion of pre-Code law, perhaps concluding that pre-Code law is only relevant if the language is ambiguous. In light of *Midlantic* and *Kelly*, we believe such an approach is flawed. Rather, where it is claimed that the Code has significantly altered an existing judicially created concept, courts should review pre-Code law since it may be discovered that the language, when viewed in the proper historical context, is not unambiguous but is actually subject to more than one reasonable interpretation.

*Ron Pair*, 828 F.2d at 372-73 (quoting *Best Repair*, 789 F.2d at 1082).

<sup>126</sup> *Id.* at 373.

<sup>127</sup> The Sixth Circuit had been joined by the First Circuit, in *In re Newbury Cafe, Inc.*, 841 F.2d 20,22 (1st Cir. 1988) (legislative history of postpetition interest awards "wholly inconclusive," and does not rebut initial inference, under *Midlantic*, that enactment of § 506(b) was not intended to change existing law). Indeed, *Newbury Cafe* noted that the two other exemptions to the rule prohibiting postpetition interest had been "preserved intact" in the Code. *Id.* Section 552(b) generally allows, where provided for by the terms of a security agreement and by applicable nonbankruptcy law, the application of prepetition security interest to postpetition proceeds, products, offspring, rent or products of the collateral. 11 U.S.C. § 552(b) (1988). Section 726(a)(5) authorizes payment of postpetition interest on priority claims, allowed unsecured claims, and

any allowed claim, whether secured on unsecured, for any fine, penalty, or forfeiture, or for multiple, exemplary or punitive damages, arising before the earlier of the order for relief or the appointment of a trustee, to the extent that such fine, penalty, forfeiture or damages are not compensation for actual pecuniary loss suffered by the holder of such claims.

11 U.S.C. § 726(a)(5).

exhibited a reluctance to look beyond the "plain language" of the Code, which Congress had labored over "for nearly a decade" before its enactment.<sup>128</sup> In a direct repudiation of *Midland*'s and *Kelly*'s principle of tacit congressional acceptance of pre-Code precedent, the Court in *Ron Pair* held that Congress, in effecting "a substantial overhaul of the [bankruptcy] system," could hardly have been expected "to have explained with particularity each step it took."<sup>129</sup> Because the legislative history would not necessarily supply indications of congressional intent, there would be no need to penetrate beyond the Code's plain language unless a party's interpretation of that language threatened the statute's coherence or consistency.<sup>130</sup> Indeed, the literal reading of the Code should control, unless it would "produce a result demonstrably at odds with the intentions of its drafters."<sup>131</sup>

Justice Blackmun's majority opinion quickly concluded that "[t]he language before us expresses Congress' intent — that postpetition interest be available — with sufficient precision so that reference to legislative history and to pre-Code practice is hardly necessary."<sup>132</sup> The presence of commas around the interest phrase in the statute, which allows "to the holder of such claim, *interest on such [oversecured] claim*, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose,"<sup>133</sup> indicated that such postpetition interest is independent of the presence or absence of an agreement relating to a consensual lien. Bluntly, the Court held that "[t]he language and punctuation Congress used cannot be read in any other way."<sup>134</sup> Thus, "[b]y the plain language of the statute, the two types of recovery [for consensual and nonconsensual liens] are distinct."<sup>135</sup> This construction of the statute's plain language did not conflict with "any other section of the Code, or with any im-

---

Agreeing with the Sixth Circuit, the First Circuit concluded that "[a] comma, often a matter of personal style, is a very small hook on which to hang a change in the law of substantial proportions." *Newbury Cafe*, 841 F.2d at 22.

<sup>128</sup> *Ron Pair*, 489 U.S. at 240.

<sup>129</sup> *Id.* at 241. On the other hand, it could be inferred from the lengthy drafting period of the Code not only that substantial revisions had been made to the Act, but that sufficient time had been available for Congress to have documented at least the major changes that the Code effected.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* at 242 (quoting *Griffin v. Oceanic Contractors, Inc.*, 458 U.S. 564, 571 (1982)).

<sup>132</sup> *Id.* at 241.

<sup>133</sup> *Id.* (quoting 11 U.S.C. § 506(b) (1988)) (emphasis added).

<sup>134</sup> *Id.* at 242 (footnote omitted).

<sup>135</sup> *Id.* (footnote omitted).

portant state or federal interest; nor is a contrary view suggested by the legislative history."<sup>136</sup>

The Court also found that the Sixth Circuit's interpretation of § 506(b) as preventing postpetition interest on oversecured nonconsensual liens would conflict with the other subsections of § 506, which themselves did not distinguish between consensual and nonconsensual liens.<sup>137</sup> The application of § 506(b) only to consensual liens could have been rendered explicit by the use of the phrase, "security interest," which the Code defines, and elsewhere uses, for this purpose.<sup>138</sup>

Promulgating a new test, the Court held that the examination of legislative history should be limited to those situations in which both (1) the "statutory language which, at least to some degree, [is] open to interpretation"<sup>139</sup> and (2) "under the proposed interpretation, [the Code provision is] in clear conflict with

---

<sup>136</sup> *Id.* at 243 (footnote omitted). Although its own standard thus rendered an examination of pre-Code precedent unnecessary, the Court nonetheless observed that the pre-Code practice of allowing postpetition interest to holders of consensual liens but not of nonconsensual liens

was an exception to an exception, recognized by only a few courts and often dependent on particular circumstances. It was certainly not the type of "rule" that we assume Congress was aware of when enacting the Code; nor was it of such significance that Congress would have taken steps other than enacting statutory language to the contrary.

....

... More importantly, this "rule," in the few cases where it was recognized, was only a guide to the trustee's exercise of his powers in the particular circumstances of the case. . . . [T]he doctrine does [not do] anything more than provide a bankruptcy court with guidance in the exercise of its equitable powers.

*Id.* at 246, 248.

<sup>137</sup> *Id.* at 242 n.5.

<sup>138</sup> *Id.* (citing 11 U.S.C. § 101(45) (1982 & Supp. IV) [now § 101(50)] (defining "security agreement" as an "agreement that creates or provides for a security interest"; 11 U.S.C. § 362(b)(12),(13) (1982 & Supp. IV) (automatic stay not applicable to certain actions to foreclose security interest in or relating to vessel or vessel under construction, or fishing facilities); 11 U.S.C. § 363(a) (1982 & Supp. IV) (defining "cash collateral" with reference to property subject to security interest under § 552(b)); 11 U.S.C. § 547(c)(3)-(5) (1982 & Supp. IV) (new value and other exceptions to trustee's avoidance power); 11 U.S.C. § 552 (1982 & Supp. IV) (postpetition effect of security interest); 11 U.S.C. § 752(c) (1982 & Supp. IV) (disposition of cash or security remaining after liquidation of customer interest); 11 U.S.C. § 1110(a) (1982 & Supp. IV) (right of secured party with purchase-money security interest in aircraft equipment and vessels to take possession of such equipment); 11 U.S.C. § 1168(a) (1982 & Supp. IV) (concerning same right with respect to rolling stock equipment); and 11 U.S.C. § 1322(b)(2) (1982 & Supp. IV) (restricting ability of plan to modify rights of holders of certain security interests)).

<sup>139</sup> *Ron Pair*, 489 U.S. at 245.

state or federal laws of great importance.”<sup>140</sup> The Court explained that neither of those conditions had been met in *Ron Pair*, which involved a statute that clearly directed that postpetition interest be paid on all oversecured claims. The “natural” interpretation of the provision in question “does not conflict with any significant state or federal interest, nor with any other aspect of the Code.”<sup>141</sup>

Justice O'Connor's dissent, which was joined by Justices Brennan, Marshall and Stevens, found that the comma appearing at the end of the phrase, “interest on such claim,” did not diminish the relevance, to the allowance of postpetition interest, of the consensual or nonconsensual nature of the oversecured claim. Were the comma to be removed, the provision at issue would allow to the holder of an oversecured claim “interest on such claims and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose.”<sup>142</sup> By this reading, unless such interest were the subject of a provision in a consensual agreement, it could not be awarded to the claimant.<sup>143</sup> The statute's inclusion of the words “and any” would not affect this

---

<sup>140</sup> *Id.* (emphasis added). The Court distinguished *Midlantic* as an instance in which “we looked to pre-Code practice for interpretive assistance” because a literal construction of the Code provision at issue would apparently have contradicted the intention of the Code's drafters. The Court found evidence of that intention expressed in: “other provisions of the Code itself,” in lack of congressional indication that nonbankruptcy law was being overturned, and in federal environmental statutes. *Id.* at 244.

*Kelly*, the Court observed, concerned a Code provision that was similarly “subject to interpretation,” and for which, “as in *Midlantic*, pre-Code practice was significant because it reflected policy considerations of great longevity and importance.” *Id.* at 244-45 (footnote omitted).

<sup>141</sup> *Id.* at 245.

Although the payment of postpetition interest is arguably somewhat in tension with the desirability of paying all creditors as uniformly as practicable, Congress expressly chose to create that alleged tension. There is no reason to suspect that Congress did not mean what the language of the statute says.

*Id.* at 245-46.

<sup>142</sup> 11 U.S.C. § 506(b) (1988) (emphasis added).

<sup>143</sup> *Ron Pair*, 489 U.S. at 250 (O'Connor, J., dissenting) (citation omitted). The dissent drew support from the Court's own precedent to the effect that punctuation is not dispositive in the construction of a statute. *Id.* (citing *Simpson v. United States*, 435 U.S. 6, 11-12 n.6 (1978) (disregarding punctuation in construing statute); *Barrett v. Van Pelt*, 268 U.S. 85, 91 (1925) (punctuation not controlling element in interpretation); *Costanzo v. Tillinghast*, 287 U.S. 341 (1932) (punctuation not decisive); *Stephens v. Cherokee Nation*, 174 U.S. 445, 479-80 (1899) (ignoring punctuation); *Ewing v. Burnet*, 11 U.S. (1 Pet.) 41, 43-44 (1837) (analysis of punctuation to be employed only as last resort)).

analysis.<sup>144</sup>

The dissent rejected the majority's conclusion that the remainder of § 506(b) did not distinguish between consensual and nonconsensual liens. Because § 506(b) itself refers to charges "provided for under the agreement under which such claim arose," the provision *could* be said to recognize consensual liens, and the "reasonable fees, costs, or charges" could only be the result of a consensual lien.<sup>145</sup> Contrary to the majority's suggestion, Congress would have had no need to refer to "security interests" in this section to establish such a distinction.<sup>146</sup>

The dissent also disagreed with the majority's holding that the statutory language addressed by *Midlantic* had not been "open to interpretation." Indeed, Justice Rehnquist's dissent in *Midlantic* had acknowledged as much.<sup>147</sup> The majority in *Ron Pair* had misconstrued *Midlantic* and *Kelly* to prohibit consideration of legislative history unless the statute itself was ambiguous and the interpretation at issue conflicted with the Code or with other laws. In fact, though, "[t]he rule of *Midlantic* is that bankruptcy statutes will not be deemed to have changed pre-Code law unless there is some indication that Congress thought that it was effecting such a change."<sup>148</sup>

Rather than identifying an ambiguity and then determining whether the interpretation advanced was hostile to existing statutes, the dissent derived its own two-step test from *Midlantic*'s analysis. "[T]he first step . . . is to ascertain whether there was an established pre-Code bankruptcy practice"<sup>149</sup>; the second step is "to look for some indicia that Congress knew it was changing pre-Code law."<sup>150</sup> Yet the unpredictability inherent in this approach would concern precisely the issues addressed in *Midlantic* and *Kelly*: could Congress be presumed to have documented every change of policy? Moreover, is judicial precedent (or a treatise's commentary on the same) the only indication of pre-Code bankruptcy practice? And what degree of support or docu-

---

<sup>144</sup> *Id.*

<sup>145</sup> *Id.* at 251 (O'Connor, J., dissenting).

<sup>146</sup> *Id.*

<sup>147</sup> *Id.* at 252 (O'Connor, J., dissenting). Justice O'Connor compared the majority's assertion that "*Midlantic* 'concerned statutory language which . . . was open to interpretation,'" *id.* at 245, with Justice Rehnquist's *Midlantic* dissent, to the effect that the language of § 554(a) is "absolute in its terms," *Ron Pair*, 474 U.S. at 509 (Rehnquist, J., dissenting). *Id.* at 252.

<sup>148</sup> *Id.* (citations omitted).

<sup>149</sup> *Id.* at 253 (O'Connor, J., dissenting).

<sup>150</sup> *Id.* at 253, 254 (O'Connor, J., dissenting) (citations omitted).



mentation will be sufficient to demonstrate that a pre-Code practice had been "established?"

Under the dissent's test, Justice O'Connor argued, the Code should be seen as incorporating prior practice on postpetition interest, for several reasons. First, the pre-Code practice of refusing to allow postpetition interest on nonconsensual liens "was more widespread and more well established than the practice in *Midlantic*." Second, knowledge of this practice could be imputed to Congress at the time of the Code's enactment. Finally, the legislative history of § 506(b) did not indicate Congress's intention to change this policy.<sup>151</sup>

*Ron Pair*'s standard for the relevance of legislative history remains indeterminate in several respects. First, the "degree" to which a provision is "open to interpretation" is itself subject to question. Indeed, it is within the Court's power, as in *Ron Pair*, to declare flatly that a disputed provision is *not* amenable to any other than a "plain meaning" interpretation, and thus that no ambiguity exists.<sup>152</sup> Indeed, though the disagreement of circuit courts of appeal on the interpretation of a given Code provision would strongly suggest that the provision was "open to interpretation," Justice Scalia has on at least two occasions reproved the "legal culture" for advancing arguments that might have been disposed of by a literal reading of the Code.<sup>153</sup>

Second, even an ambiguity of sufficient stature to be deemed "open to interpretation" might not merit legislative history analysis if the interpretation advanced is found not to present a "clear" conflict with existing statutes. As in *Midlantic*, which bowed to the environmental goals enunciated by Congress, and *Kelly*, which deferred to the states' power to administer their criminal justice systems, courts could explicitly subordinate the interpretation of Code provisions to the aims of other statutes. Alternatively, the Code's own goal could trump those of other statutes. In either situation, however, the court in question would be examining the legislative history, if any, not of the particular Code section at issue, but of the Code and/or other stat-

---

<sup>151</sup> *Id.*

<sup>152</sup> Under the strictest reading of *Ron Pair*, a court could refuse to consider any interpretation other than a literal construction of a Code provision unless that "plain meaning" itself led to "a result demonstrably at odds with the intentions of its drafters." *Ron Pair*, 489 U.S. at 242-43. Of course, this begs the question of whether the provision is "open to interpretation," by assuming that there is only one literal interpretation of the statute.

<sup>153</sup> See *infra* notes 203, 425.

utes as a whole. Nor did *Ron Pair* indicate what would constitute a "clear conflict."

Finally, the Court provided no indication of which state or federal laws were to be considered "of great importance." Presumably, the hierarchy of statutes could vary with the context of the issues and interests at stake. In fact, for a given context, newly enacted legislation could alter the order of priorities. Thus, the *Ron Pair* test for the relevance of legislative history would, if anything, make the interpretation of the Code less predictable.<sup>154</sup>

In precluding alternate interpretations of the Code, *Ron Pair* left unsettled the outlines of *Midlantic's* test for the relevance of the Code's legislative history. Nor did the *Ron Pair* opinion enunciate any general tests or standards for determining whether Congress had been aware of a given pre-Code practice or precedent, and, if so, whether Congress had sought to eliminate it in enacting the Code. Finally, *Ron Pair* demonstrated the Court's increasing tendency to review an ambiguous section of the Code in the context of other Code provisions, and, in particular, to correlate the terms of one subsection with those of neighboring subsections. The degree to which this last technique could be applied effectively would be a significant focus of later "plain meaning" decisions.<sup>155</sup>

D. *Toibb v. Radloff*<sup>156</sup>

Endorsing a literal reading of the Code, the Court in *Toibb*,

---

<sup>154</sup> Complicating this entire analysis is the fact that the Code itself, which surely constitutes a statute "of great importance" for purposes of the *Ron Pair* analysis, embraces conflicting policies: the "equity policy" of "distribut[ing] a troubled company's assets through the equal sharing of losses by creditors of equal rank is often at odds with the "reorganization policy" of "restructuring a business to preserve jobs, to pay creditors, [and] to produce a return for owners." MARTIN J. BIENSTOCK, *BANKRUPTCY REORGANIZATION* 1-2 (1988).

In consumer bankruptcy proceedings, the counterpart to the "reorganization policy" is commonly known as the "fresh start" policy, but gives rise to many of the same conflicts. Thus, "[t]he fresh start for debtors, a chance for a person in financial collapse to begin anew, is an appealing idea, until one confronts the inevitable fact that it permits people to walk away from their obligations and to break their promises." TERESA A. SULLIVAN, ELIZABETH WARREN & JAY L. WESTBROOK, *AS WE FORGIVE OUR DEBTORS: BANKRUPTCY AND CONSUMER CREDIT IN AMERICA* 20 (1989) (noting also that policy of protecting each creditor from other creditors to achieve fairest collective result actually bars "creditors from taking action to protect themselves, a right that the rest of the law enshrines and vindicates.").

<sup>155</sup> See *infra* notes 597-602 and accompanying text.

<sup>156</sup> 111 S. Ct. 2197 (1991).

reversing a decision of the Eighth Circuit in holding that chapter 11 reorganizations are available to individual nonbusiness debtors.<sup>157</sup> Indeed, Justice Blackmun's majority opinion began with the observation that, "[i]n our view, the plain language of the Bankruptcy Code disposes of the question before us."<sup>158</sup> Underlying the certainty of this analysis may have been the neat interlocking of Code provisions to produce a syllogistic conclusion. Nevertheless, the dissent managed to detect an ambiguity that would allow the introduction of legislative history to support a contrary interpretation. Perhaps because the issue did not turn on the meaning of only one section of the Code, neither the majority nor the dissent referred to the statutory approach of *Midlantic*, *Kelly* and *Ron Pair*.

### 1. Following the Logic

The interconnection of the relevant Code provisions was not difficult to perceive. First, the Code limits eligibility for Chapter 11 relief to "a person that may be a debtor under chapter 7 of this title, except a stockbroker or a commodity broker, and a railroad."<sup>159</sup> Second, Chapter 7 relief itself is deemed available to all "persons" except for railroads and certain financial institutions.<sup>160</sup> Finally, the Code defines "person" to include individuals.<sup>161</sup> Therefore, the statutory provisions on their face would render an individual eligible for chapter 11 protection. Moreover, the specific exclusions of certain classes of debtors from the

---

<sup>157</sup> *Id.* at 2202. Eleven months after filing a chapter 7 petition in November 1986, Sheldon Baruch Toibb filed a motion to convert the case to a chapter 11 proceeding. *Id.* at 2198. The bankruptcy court granted the motion, but subsequently issued an order to show cause why Toibb's case should not be dismissed for failure to qualify as a chapter 11 debtor. *Id.* After a hearing, Toibb was found not to be engaged in an ongoing business; the court, under the authority of *Wamsganz v. Boatmen's Bank of DeSoto*, 804 F.2d 503 (8th Cir. 1986) (predicating individuals' eligibility for chapter 11 protection on their involvement in an ongoing business), ordered that the proceeding be dismissed if Toibb did not, within ten days, convert his case back to a chapter 7 proceeding. *Id.* at 2198-99. The district court affirmed this order. *Id.* at 2199. Neither the bankruptcy court's nor the district court's decision was reported. *In re Toibb*, 902 F.2d 14, 14 (8th Cir. 1990).

On appeal, the Eighth Circuit affirmed, without elaboration, both "the Bankruptcy Court's finding that Mr. Toibb did not qualify as a business entitled to Chapter 11 protection" and the dispositive effect of *Wamsganz* on the bankruptcy court's legal analysis. *Id.*

<sup>158</sup> *Toibb*, 111 S. Ct. at 2199.

<sup>159</sup> 11 U.S.C. § 109(d) (1988).

<sup>160</sup> *Id.* § 109(b).

<sup>161</sup> 11 U.S.C. § 101(41) (1988). This definition appeared at § 101(35) (1988) at the time of the *Toibb* decision.

coverage of chapters 7 and 11 indicated to the Court that although "Congress knew how to restrict recourse to the avenues of bankruptcy relief; it did not place Chapter 11 reorganization beyond the reach of a nonbusiness individual debtor."<sup>162</sup>

The Court firmly rejected any inference from the Code's legislative history and structure that these debtors were excluded from chapter 11 protection. Not only was the legislative history irrelevant unless the statutory language was unclear,<sup>163</sup> but it was in fact ambiguous at best on the possibility of such chapter 11 proceedings.<sup>164</sup> The presence of chapter 11 provisions explicitly referring to business debtors<sup>165</sup> demonstrated no more than the "understandable expectation that chapter 11 would be used primarily by debtors with ongoing businesses[,] and certainly did not constitute "an additional prerequisite for chapter 11 eligibility."<sup>166</sup>

Justice Stevens's lone dissent adopted a more holistic view of the Code. Although chapter 11 relief is statutorily available "only to [a] person that may be a debtor under Chapter 7,"<sup>167</sup> this Justice observed, it was not necessarily intended to be available to every such debtor.<sup>168</sup> This ambiguity justified an examination of the Code's legislative history, which satisfied Justice Stevens that chapter 11 relief was not applicable to individual nonbusiness debtors.<sup>169</sup> The dissent emphasized several considerations, including: (1) the "repeated references" to the business and management of the debtor, both in chapter 11 itself and in the Senate

---

<sup>162</sup> *Toibb*, 111 S. Ct. at 2199.

<sup>163</sup> *Id.* at 2200. Curiously, the Court referred here not to *Midlantic*, *Kelly*, or *Ron Pair*, but to an earlier, nonbankruptcy decision for the general proposition that "[w]here, as here, the resolution of a question of federal law turns on a statute and the intention of Congress, we look first to the statutory language and then to the legislative history if the statutory language is unclear." *Id.* at 2200 (quoting *Blum v. Stenson*, 465 U.S. 886, 896 (1984)).

<sup>164</sup> *Id.* (citing H.R. REP. NO. 596, 95th Cong., 2d Sess. 125 (1977), reprinted in 1978 U.S.C.C.A.N. 5787 (offering "consumer debtors" the choice only between chapter 13 and "straight bankruptcy" (presumably chapter 7)); and S. REP. NO. 989, 95th Cong., 2d Sess. 3 (1978), reprinted in 1978 U.S.C.C.A.N. 5789 (chapter 11 relief applicable to individuals, but its procedures are too complex to be used in "consumer context"))).

<sup>165</sup> *Id.* (citing 11 U.S.C. § 1102 (1988) (authorizing appointment of equity security holders' committee) and 11 U.S.C. § 1104(a)(1) (1988) (authorizing appointment of trustee where debtor's "current management" deficient or dishonest)).

<sup>166</sup> *Id.*

<sup>167</sup> 11 U.S.C. § 109(d) (1988) (emphasis added).

<sup>168</sup> *Toibb*, 111 S. Ct. at 2202 (Stevens, J., dissenting).

<sup>169</sup> *Id.* at 2203-04 (Stevens, J., dissenting).

Report's analysis of that chapter<sup>170</sup>; (2) the House Report's limitation of consumer relief to chapters 7 and 13<sup>171</sup>; (3) the description of chapter 11 merely as "Reorganization," as opposed to the titling of chapter 13 as "Adjustment of Debts of an Individual With Regular Income,"<sup>172</sup>; (4) the absence in chapter 11, but not in chapter 13, of upper limits for the secured and unsecured debts of individual debtors<sup>173</sup>; and (5) the ability of a creditor, under the majority's analysis, to institute an involuntary chapter 11 proceeding against nonbusiness individuals, although the Code explicitly prohibits such proceedings in chapter 13 matters.<sup>174</sup>

*Toibb*, then, indicates that even a seemingly ironclad chain of logic might be snipped by a creative approach to the ambiguities inherent in the language of the Code.<sup>175</sup> Once the gate had been

<sup>170</sup> *Id.* at 2202-03 (Stevens, J., dissenting).

<sup>171</sup> *Id.* (citing H.R. REP. NO. 595, 95th Cong., 2d Sess. 125 (1977)).

<sup>172</sup> *Id.* at 2202 (Stevens, J. dissenting). *Cf.* LOOKING-GLASS, *supra* note 1, at 253 ("'Must a name mean something?' Alice asked doubtfully. 'Of course it must,' Humpty Dumpty said with a short laugh.'").

<sup>173</sup> *Toibb*, 111 S. Ct. at 2203-04 (Stevens, J., dissenting).

<sup>174</sup> *Id.* at 2204 (Stevens, J., dissenting) (citing 11 U.S.C. § 303(a) (1988) (involuntary cases may be commenced only under chapter 7 or chapter 11)).

<sup>175</sup> Justice Stevens's appreciation of statutory ambiguity and of the corresponding importance of an examination of legislative history were similarly in evidence in *Connecticut National Bank v. Germain*, 112 S. Ct. 1146 (1992). In reversing the Second Circuit by holding that an interlocutory order issued by a district court sitting as a court of appeals in bankruptcy is appealable, Justice Thomas's majority opinion adopted a literal approach to the statutes at issue: 28 U.S.C. § 1292 provides that courts of appeals have jurisdiction over "[i]nterlocutory orders of the district courts of the United States," and 28 U.S.C. § 158(d) grants courts of appeals jurisdiction over appeals from all final decisions, judgments, orders and decrees entered by district courts of bankruptcy appellate panels hearing appeals from final and interlocutory orders of bankruptcy courts.

Citing *Ron Pair*, the Court observed that "[w]e have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there . . . when the words of a statute are unambiguous, then, this first canon is also the last. . . ." *Id.* at 1149 (citations omitted). Because 28 U.S.C. § 1292 did not distinguish between review of orders issued by district courts sitting as trial courts in bankruptcy from those issued as appellate courts, and because no section of title 28 appeared to limit review to the former, "[t]here is no reason to infer from either § 1292 or § 158(d) that Congress meant to limit appellate review of interlocutory orders in bankruptcy proceedings." *Id.* at 1150.

In a three-paragraph concurrence, which did *not* cite *Ron Pair*, Justice Stevens reminded the Court that "[w]hen there is some uncertainty about the meaning of a statute, it is prudent to examine its legislative history." *Id.* If, in enacting the current system of bankruptcy appeals through the Bankruptcy Amendments and Federal Judgeship Act of 1984 ("BAJFA"), Pub. L. No. 98-353, 98 Stat. 333, "Congress had intended such a significant change in the scheme of appellate jurisdiction [as excluding review by the courts of appeals of certain interlocutory bankruptcy

opened to the domain of legislative history, the arguments in favor of a "non-literal" reading of the statute grow even stronger.

*E. Union Bank v. Wolas*<sup>176</sup>

It was Justice Stevens, the sole dissenter in *Toibb*, who six months later delivered a majority opinion that applied the "plain meaning" approach to eliminate any distinction between "short term" and "long term" loans in the context of the "ordinary course of business" exception to the preference rule. Though the Court explicitly restricted the scope of its inquiry to examining "short term" versus "long term" loans. Justice Scalia's brief concurrence suggested that, given the plain language of the provision in question, the question should never have arisen. Apparently abandoning the conclusion of *Ron Pair* that considerations of legislative history had no place in the interpretation of a sufficiently straightforward statutory provision, the Court in *Wolas* championed the plain meaning of a provision completely rewritten by Congress in the enactment of the Code.

By emphasizing that Congress has no duty to indicate or to elaborate on all of the changes that the Code had been *intended* to effect in existing practice, *Ron Pair* had dramatically enhanced the Court's power to preclude considerations of legislative history. Now, by announcing that it would uphold the logical consequences of a rewritten provision of the Code, even if these implications were *unintended* by Congress, the Court hewed even more closely to the literal language of the Code.

### 1. Background

Generally, the Code allows bankruptcy trustees expansive power to "avoid," or reverse, any transaction that was made: (1) within ninety days before the debtor's bankruptcy; (2) when the debtor was insolvent; (3) to benefit a creditor; (4) on account of antecedent debt; and (5) to enable the creditor to receive more than it would have in a liquidation of the debtor.<sup>177</sup> One of the

---

orders], some indication of this purpose would almost certainly have found its way into the legislative history. The legislative record, however, contains no mention of an intent to limit the scope of § 1292(b). This silence tends to support the conclusion that no such change was intended." *Id.*

<sup>176</sup> 112 S. Ct. 527 (1991).

<sup>177</sup> Under § 547(b), the trustee may generally avoid any transfer of an interest of the debtor in property—  
(1) to or for the benefit of a creditor;

seven exceptions to the trustee's avoidance power involves transfers that were "made in the ordinary course of business and financial affairs of the debtor and the transferee."<sup>178</sup>

Herbert Wolas, the chapter 7 trustee for ZZZZ Best, Inc., attempted to recover, as preferential transfers, several interest payments and loan commitment fees that the debtor had made on an eight-month revolving credit agreement during the six months before it filed for bankruptcy.<sup>179</sup> In an unreported opinion, the bankruptcy court found the "ordinary course" exception applicable to these payments. It rejected Wolas's argument that ZZZZ Best, as the operator of a "Ponzi," or pyramid, scheme, *had* no ordinary course of business.<sup>180</sup> The district court affirmed.<sup>181</sup>

On appeal, however, the Ninth Circuit reversed on different grounds, citing its prior decision that the ordinary course of business exception did not extend to sheltering interest payments on *long-term* debt.<sup>182</sup> Although the lender attempted to distinguish the loan to ZZZZ Best as prepayable at any time and as having

- 
- (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
  - (3) made while the debtor was insolvent;
  - (4) made—
    - (A) on or within 90 days before the date of the filing of the petition; or
    - (B) between 90 days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
  - (5) that enables such creditor to receive more than such creditor would receive if—
    - (A) the case were a case under chapter 7 of this title;
    - (B) the transfer had not been made; and
    - (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

11 U.S.C. § 547(b) (1988).

<sup>178</sup> Under section 547(c)(2), the trustee may not avoid as a preference a transfer to the extent that such transfer was

- (A) in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee;
- (B) made in the ordinary course of business or financial affairs of the debtor and the transferee; and
- (C) made according to ordinary business terms.

11 U.S.C. § 547(c)(2) (1988).

<sup>179</sup> *Wolas v. Union Bank (In re ZZZZ Best Co., Inc.)*, 921 F.2d 968, 969 (9th Cir. 1990).

<sup>180</sup> *Id.* For an illuminating profile of the debtor's pre-bankruptcy operations, see JOE DOMANICK, *FAKING IT IN AMERICA: BARRY MINKOW AND THE GREAT ZZZZ BEST SCAM* (Knightsbridge, New York 1989).

<sup>181</sup> 1989 WL 263387 (C.D. Cal. 1989).

<sup>182</sup> *Wolas*, 921 F.2d at 969 (citing *In re CHG International, Inc.*, 897 F.2d 1479 (9th Cir. 1990)).

conditioned the debtor's access to funds on the debtor's keeping current with interest payments, the court "fail[ed] to see any significant difference between a revolving line of credit and an ordinary loan for purposes of § 547(c)(2)."<sup>183</sup> Nor did the eight-month term of the revolving loan exclude it from the category of "long-term loans" — this court of appeals had previously characterized as long-term a loan for only seven months.<sup>184</sup>

## 2. Upholding Implications, Even if Unintended

Because the text of the exception did not address the term of the debt for which the allegedly preferential repayment had been made,<sup>185</sup> and because the Code did not in fact distinguish between long-term and short-term debt,<sup>186</sup> the Court declined to restrict to short-term debt the application of the "ordinary course" exception.<sup>187</sup>

Although *Ron Pair* had declared that the analysis of sufficiently unambiguous language would not address considerations of legislative history, Justice Stevens interpreted that decision to imply that "[g]iven the clarity of the statutory text, respondent's burden of persuading us that Congress intended to create or preserve a special rule for long-term debt is exceptionally heavy."<sup>188</sup> This Justice therefore embarked on an extended examination of the legislative history of § 547.

The version of the statute originally enacted in 1978 as part of the Code specified that the ordinary course of business exception applied only to payments made within forty-five days after the debt had been incurred.<sup>189</sup> This qualification had been repealed by the Bankruptcy Amendments and Federal Judgeship

---

<sup>183</sup> *Id.*

<sup>184</sup> *Id.* (citation omitted).

<sup>185</sup> *Wolas*, 112 S. Ct. at 530.

<sup>186</sup> *Id.* n.7.

<sup>187</sup> *Id.* at 530 (citing *U.S. v. Ron Pair Enterprises*, 489 U.S. 235, 241-42 (1989)).

<sup>188</sup> *Id.* (citing *Ron Pair*, 489 U.S. at 1030-31).

<sup>189</sup> The original version of § 547(c)(2) excepted a transfer from the trustee's avoidance powers

(2) to the extent that such transfer was—

(A) in payment of a debt incurred in the ordinary course of business or financial affairs of the debtor and the transferee;

(B) *made not later than 45 days after such debt was incurred*;

(C) made in the ordinary course of business or financial affairs of the debtor and the transferee; and

(D) made according to ordinary business terms.

*Wolas*, 112 S. Ct. at 530 n.8 (quoting 92 Stat. 2549, 2598 (1978)) (emphasis added).



Act of 1984.<sup>190</sup> The Court declined to speculate on Congress's intentions in deleting this language, since "[t]he fact that Congress may not have foreseen all of the consequences of a statutory enactment is not a sufficient reason for refusing to give effect to its plain meaning."<sup>191</sup>

Nor did the Court accept the argument that § 547(c)(2) had originally been enacted to codify a judicially-created "current expense" exception to the preference rule, which had allowed the debtor to pay its (presumably short-term) trade creditors and other suppliers even as bankruptcy approached. Indeed, § 547 provided other exceptions to address this concern.<sup>192</sup> Moreover, there was no "extrinsic evidence" that Congress had intended to codify the current expense rule<sup>193</sup>; that rule had apparently not even been mentioned in the legislative history.<sup>194</sup> In short, "the fact that Congress carefully examined and entirely rewrote the preference provision in 1978 supports the conclusion that the text of section 547(c)(2) as enacted reflects the deliberate choice of Congress."<sup>195</sup>

On a policy level, the Court identified two separate goals of the Code's preference provision, § 547: to prevent creditors eager to recover their assets from a failing business from "racing to the courthouse," and to distribute the debtor's assets equally among the creditors.<sup>196</sup> Although the "ordinary course of business" exception to the trustee's avoidance power would favor the

---

<sup>190</sup> PUB. L. NO. 98-353, § 462(c), 98 Stat. 333, 378.

<sup>191</sup> *Wolas*, 112 S. Ct. at 531 (citing *Toibb v. Radloff*, 111 S. Ct. 2197 (1991)).

<sup>192</sup> As the Court observed, *id.* at 532 n.13, under § 547(c)(1), a trustee may not avoid a transfer to the extent that the transfer was "(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and (B) in fact a substantially contemporaneous exchange." 11 U.S.C. § 547(c)(1) (1988).

Similarly, under § 547(c)(4), transfers are exempted from the trustee's avoidance powers to the extent that they are

(4) to or for the benefit of a creditor, to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor—

(A) not secured by an otherwise unavoidable security interest; and

(B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor.

11 U.S.C. § 547(c)(4) (1988).

<sup>193</sup> *Wolas*, 112 S. Ct. at 532.

<sup>194</sup> *Id.* n.14.

<sup>195</sup> *Id.*

<sup>196</sup> *Id.* at 532-33 (citing H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 177-78, reprinted in 1978 U.S.C.C.A.N. 6137, 6138).

recipients of the transfers in question at the expense of other creditors, it would discourage these recipients from starting, or joining in, the feeding frenzy that would pull a drowning debtor under for the third time. Noting that “the statutory text — which makes no distinction between short-term debt and long-term debt— precludes an analysis that divorces” the two policies,<sup>197</sup> the Court held that “[w]hether Congress has wisely balanced the sometimes conflicting policies underlying § 547 is not a question that we are authorized to decide.”<sup>198</sup> Nor did it determine whether the \$7 million revolving credit agreement that the debtor had entered into seven months before filing a chapter 7 petition was a long- or short-term debt<sup>199</sup>; whether the payments of interest and the loan commitment fee, made during the 90 days before bankruptcy in the approximate aggregate amount of \$102,500, qualified for the ordinary course of business exception<sup>200</sup>; whether the loan in question had been incurred in the ordinary course of business of both parties<sup>201</sup>; or whether the payments had been made in the ordinary course of business and according to ordinary business terms.<sup>202</sup>

In a one-paragraph concurrence, Justice Scalia chided:

It is regrettable that we have a legal culture in which such arguments have to be addressed (and are indeed credited by a Court of Appeals), with respect to a statute utterly devoid of language that could remotely be thought to distinguish between long-term and short-term debt. Since there was here no contention of a “scrivener’s error” producing an absurd result, the plain text of the statute should have made this litigation unnecessary and unmaintainable.<sup>203</sup>

In the Court’s next “plain meaning” case, this Justice’s expres-

---

<sup>197</sup> *Id.* at 533.

<sup>198</sup> *Id.*

<sup>199</sup> *Id.* at 529 n.5. The Court explained: “Because we hold that the ordinary course of business exception applies to payments on long-term as well as short-term debt, we need not decide whether the revolving line of credit was a ‘long-term’ debt.” *Id.*

<sup>200</sup> *Id.* at 533.

<sup>201</sup> *Id.*

<sup>202</sup> *Id.* at 533-34.

<sup>203</sup> *Id.* at 534 (Scalia, J., concurring). Justice Scalia did not indicate, however, that the *Ron Pair* test would specifically have ruled out an inquiry into the legislative history of the preference provisions. Nor did this Justice address the means by which a “scrivener’s error” could be distinguished from a statutory section that permitted unintended consequences.

sion of disappointment with bankruptcy's "legal culture" would be not only more detailed but also much more impassioned.

F. *Dewsnup v. Timm*<sup>204</sup>

Where *Wolas* had found the Court unwilling to accept non-literal interpretations of a Code provision specifically rewritten by Congress, *Dewsnup*, like *Midlantic* and *Kelly*, conversely demonstrated the Court's reluctance "to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history."<sup>205</sup> Accordingly, in affirming Tenth Circuit precedent that denied chapter 7 debtors the ability to "strip down" the liens of undersecured creditors, the Court held that such debtors have no statutory right to redeem overencumbered property by tendering to creditors its market value. However, an extended and unusually caustic dissent by Justice Scalia suggested that the "plain meaning" approach espoused by the Court's recent bankruptcy decisions had been carried to such an extreme that each separate subsection of the Code was now being interpreted in isolation, thereby jeopardizing not only the integrity of the Court's methodology but the collective coherence of its decisions.<sup>206</sup>

1. Background

In 1978, to collateralize a loan of \$119,000, Aletha Dewsnup and her husband granted a lien on two parcels of farmland. Three years later, after Mr. Dewsnup had died and Mrs. Dewsnup had defaulted on the loan, the secured creditors filed a notice of default. However, Mrs. Dewsnup averted foreclosure proceedings by petitioning for liquidation under chapter 7.<sup>207</sup> By 1987, the outstanding loan balance had reached \$120,000. At this point, Dewsnup brought an adversary proceeding before the bankruptcy court to "strip down" the value of the lien to the property's fair market value of \$39,000.<sup>208</sup> If this relief had been granted, she would have been able to recover title to the property, free and clear of liens, simply by paying the fair market

---

<sup>204</sup> 112 S. Ct. 773 (1992). The following discussion has been adapted with permission from that presented in Walter A. Effross, *Debtors Stripped of 3d Cir. Right to Strip Liens*, 130 N.J.L.J. 707 (1992).

<sup>205</sup> *Dewsnup*, 112 S. Ct. at 779.

<sup>206</sup> *Id.* at 779-89 (Scalia, J., dissenting).

<sup>207</sup> *Id.* at 776. Originally, Mrs. Dewsnup had filed two chapter 11 petitions, but both were dismissed. *Id.*

<sup>208</sup> *Id.*

value to the lienholders. However, the bankruptcy court,<sup>209</sup> the district court (in an unreported opinion) and the United States Court of Appeals for the Tenth Circuit<sup>210</sup> refused to allow the lien to be stripped down. Noting that the Tenth Circuit and the Third Circuit had disagreed on the relevant legal issues, the Supreme Court granted certiorari.

In bankruptcy proceedings, each claim filed against the debtor is automatically deemed "allowed," and thus qualified for repayment, unless an objection to the claim is filed by the trustee or debtor-in-possession, or by another creditor.<sup>211</sup> However, the allowed claim of a creditor who is undersecured "by a lien on property in which the estate has an interest" is bifurcated by § 506(a): the undersecured creditor is deemed to hold a secured claim in the amount of his interest in the collateral, and an unsecured claim for the deficiency.<sup>212</sup> In Dewsnap's case, the creditors' allowed claim of \$120,000 was thus divided into an allowed secured claim of \$39,000 (the court-determined value of the property) and an allowed unsecured claim of \$91,000, the remainder of the claimed amount.

Since overencumbered property can provide satisfaction only to those creditors who hold a secured interest in this collateral, under § 554 the trustee may abandon this property as "of inconsequential value and benefit to the estate [*i.e.*, to all other creditors]." <sup>213</sup> Exempted from the bankruptcy estate and returned to the debtor, abandoned property is no longer protected by the automatic stay and other bankruptcy provisions, but is immediately vulnerable to the secured creditors' state law remedies of foreclosure.

Dewsnap attempted to deter such foreclosure by citing § 506(d), which provides in relevant part that "[t]o the extent that a lien secures a claim against the debtor that is not an allowed *secured* claim, such lien is void."<sup>214</sup> Arguing that this provision voided the \$91,000 *unsecured* claim that had been created by § 506(a), the debtor asserted that she could thus redeem the

---

<sup>209</sup> Dewsnap v. Timm (*In re Dewsnap*), 87 B.R. 676 (Bankr. D. Utah. 1988).

<sup>210</sup> 908 F.2d 588 (10th Cir. 1990).

<sup>211</sup> Section 502(a) provides that "[a] claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest . . . objects." 11 U.S.C. § 502(a) (1988).

<sup>212</sup> See *supra* note 116 for the full text of § 506(a).

<sup>213</sup> See *supra* notes 16-17 and accompanying text for a discussion of § 554.

<sup>214</sup> 11 U.S.C. § 506(d) (1988) (emphasis added).

abandoned property merely by retiring the \$39,000 allowed secured claim.

Before the bankruptcy court, the secured creditors noted that the form of relief sought by Dewsnap is provided for by § 722.<sup>215</sup> However, while that section allows a debtor to redeem abandoned property by paying to lienholders the amount of the allowed secured claim, such redemption is available not for real property but only for "tangible personal property intended for personal, family or household use."<sup>216</sup> Thus, Dewsnap's attempt to construe § 506(a) to redeem real property would contradict the specific provisions of § 722, and, by implication, the intention of Congress.

Though this statutory argument would persuade the Tenth Circuit, the bankruptcy court held that the rejection of the debtor's claim was not "compelled by the language of the Code."<sup>217</sup> Instead, the court saw § 506 as intended to limit, to the amount of estate property securing a creditor's lien, the creditor's abilities to: reject a plan; avoid cramdown; realize the equivalent of his secured claim; make a § 1111(b) election; or receive the first distributions in a liquidation.<sup>218</sup>

Since abandoned property is not part of the estate, and since rights to such property are unaffected by the bankruptcy process, the court found it "inconceivable" that Congress would have intended to permit chapter 7 debtors to avoid creditors' liens on abandoned property.<sup>219</sup> Such an unauthorized expansion of the debtor's rights would deprive the creditors of their entitlement to foreclose against the property, and thus of their ability not only to set a minimum sale price (by bidding the amount of the debt) but to benefit from any appreciation in the value of the property (by waiting to sell into a rising market). The bankruptcy court

---

<sup>215</sup> Under § 722,

An individual debtor may, whether or not the debtor has waived the right to redeem under this section, redeem tangible personal property intended primarily for personal, family or household use, from a lien securing a dischargeable consumer debt, if such property is exempted under section 522 of this title or has been abandoned under section 554 of this title, by paying the holder of such lien the amount of the allowed secured claim of such holder that is secured by such lien.

<sup>11</sup> U.S.C. § 722 (1988).

<sup>216</sup> *Id.*

<sup>217</sup> *Dewsnap*, 87 B.R. at 680.

<sup>218</sup> *Id.* at 682.

<sup>219</sup> *Id.* at 683.

dismissed Dewsnap's complaint with prejudice. The district court affirmed summarily, without appending an opinion.

a. *Split Between the Tenth and Third Circuits*

In affirming the district court's opinion and observing that "[t]he estate has no interest in, and does not administer, abandoned property,"<sup>220</sup> the Tenth Circuit specifically distinguished its approach from that of the Third Circuit in *Gaglia v. First Federal Savings & Loan Association*.<sup>221</sup> There, the residence of individual chapter 7 debtors, which had an alleged value of \$34,000, was encumbered with a first mortgage in the amount of \$29,000 and a second mortgage for more than \$200,000. The Third Circuit voided the junior mortgage to the extent that it exceeded the \$5,000 of available equity in the property.

The *Gaglia* creditors, like the Tenth Circuit, read § 506(d) in conjunction with § 506(a). In their analysis, because abandoned property such as overencumbered real estate is no longer subject to the operation of the Code, such property does not qualify under § 506(a) as "property in which the estate has an interest." Section 506(a), therefore, could not be applied to claims secured by liens on overencumbered property, and thus could not separate from such claims unsecured portions to be avoided by the debtor under § 506(d).

But the Third Circuit held that this reading of § 506(a) "would seem to conflict with the plain meaning" of § 506(d).<sup>222</sup> In addition, whether or not the debtor had any equity in the property, the estate had an "interest" in the debtor's legal title to property secured by a mortgage.<sup>223</sup> Finally, *Gaglia* noted that a creditor whose lien was secured by abandoned property could more efficiently assert his claim through the bankruptcy process than foreclose on the property, and that the creditor's participation in the bankruptcy proceeding "would aid the overall administration of the estate."<sup>224</sup>

Among the subsidiary issues over which the Third and Tenth Circuits clashed were:

---

<sup>220</sup> *Dewsnap*, 908 F.2d at 590-91.

<sup>221</sup> 889 F.2d 1304 (3d Cir. 1989).

<sup>222</sup> *Id.* at 1308.

<sup>223</sup> *Id.* In *Dewsnap*, the Tenth Circuit ruled that the debtor's interest in legal title to the property was disposed of when the property was abandoned. *Dewsnap*, 908 F.2d at 591.

<sup>224</sup> *Gaglia*, 889 F.2d at 1308 n.5.

*Import of § 722.* The Third Circuit held that § 722 does not render redundant § 506, which "is not a redemption provision."<sup>225</sup> Even after the unsecured claim created by § 506(a) was avoided under § 506(d), the debtors would remain subject to the first mortgage on the property and would be liable to the junior mortgagee for the remaining equity in the property.

Though agreeing that § 506 is not a redemption provision, the Tenth Circuit concluded that "the rationale of [*Gaglia*] mandates that it become one."<sup>226</sup> The Tenth Circuit read § 722's inapplicability to the redemption of real property as indicating that Congress did not intend to provide such relief to a chapter 7 debtor. However, unlike the *Gaglias*, *Dewsnup* was apparently prepared to tender to lienholders her property's market value in cash, and would, under the Third Circuit's analysis, then own the property free and clear of any liens. To the Tenth Circuit, "[t]his result [was] both inequitable and unfair and would constitute an expansion of debtors' rights far beyond what is contemplated in the Code."<sup>227</sup>

*Appreciation of the Property.* The Third Circuit noted that "stripping down" a creditor's lien to the value of his secured interest would not only diminish the amount that the debtor would have to repay in order to recover clear title but might also enable the debtor to negotiate a more favorable repayment schedule. If the junior mortgagee's lien were not stripped down, the debtor might have little motivation to build equity in the property, since this creditor could foreclose on their equity at any time.<sup>228</sup>

Even after the *Gaglias* had been discharged, a creditor not involved in the bankruptcy proceedings could foreclose to obtain a deficiency judgment. The court concluded that "applying § 506 here is called for not only by the language of that section, but will further the Code's policy of providing the debtor with a fresh start."<sup>229</sup> Moreover, the Third Circuit found that the application of this section would not harm the second mortgagee, whose total recovery — either through the bankruptcy process or through foreclosure on the abandoned property — would be limited to the excess of the fair market value of the property over the balance outstanding on the first mortgage.<sup>230</sup>

---

<sup>225</sup> *Id.* at 1310.

<sup>226</sup> *Dewsnup*, 908 F.2d at 542.

<sup>227</sup> *Id.* at 592.

<sup>228</sup> *Gaglia*, 889 F.2d at 1308.

<sup>229</sup> *Id.* at 1309.

<sup>230</sup> *Id.* at 1308.

The Tenth Circuit disagreed, noting that only at a foreclosure sale, and not within the bankruptcy process, could a lienholder itself purchase the property as an investment, hoping that its value would rise. The Third Circuit's analysis, by assuming that an outside party would acquire the property at a forced sale, would deprive the creditors of the chance to benefit from any appreciation on the property, thus giving debtors "much more than the 'fresh start' to which they are entitled. We do not believe Congress intended such a result when it enacted these Code provisions."<sup>231</sup>

*Effect of Relief from Stay.* The *Gaglia* bankruptcy court held that stripping down liens under § 506 would nullify the creditor's right to "whatever benefit he might receive" by lifting the automatic stay under § 362(d)(2).<sup>232</sup> That provision directs the court to grant relief from the automatic stay if the debtor does not have equity in the property in question and the property is not necessary for an effective reorganization, both of which conditions would be met in a chapter 7 liquidation involving overencumbered property.

However, by equating the benefits to the undersecured creditor of proceeding within the bankruptcy process or by foreclosure, the Third Circuit rejected this analysis. Adopting the same argument opposed by the Tenth Circuit in *Dewsnup*, the *Gaglia* Court held that, whether or not the debtor opposed a motion to lift stay with his own motion to strip down the lien, "the creditor receives exactly the same thing — the fair market value of the property less the value of any more senior obligations."<sup>233</sup> The motion to lift the stay, under this logic, merely allows a secured creditor to obtain his satisfaction quickly; it indicates neither Congressional intent to allow foreclosure on the chapter 7

---

<sup>231</sup> *Dewsnup*, 908 F.2d at 593.

<sup>232</sup> *In re Gaglia*, 76 B.R. 81, 84 (Bankr. W.D. Pa. 1987). Section 362(d)(2) provides:

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the [automatic] stay provided under [§ 362(a)], such as by terminating, annulling, modifying, or conditioning such stay . . . .

(2) with respect to a stay of an act against property under subsection (a) of this section, if—

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization.

11 U.S.C. § 362(d)(2) (1988).

<sup>233</sup> *Gaglia*, 889 F.2d at 1310 n.9.



debtor's overencumbered property nor an intent that the entire claim remain secured if the property is not liquidated.

*Skewing Incentives for Forms of Relief.* Finally, the Third and Tenth Circuits diverged over whether allowing the liquidating debtor to strip down liens would lead debtors to prefer liquidation under chapter 7 to reorganization under chapters 11, 12 or 13. The Tenth Circuit found that, rather than being intended to allow liquidating debtors to strip down liens on abandoned real property, § 506 was "intended to facilitate valuation and disposition of property in the reorganization chapters of the Code."<sup>234</sup>

By contrast, the Third Circuit noted that, though the strip-down application of § 506 was clearly foreseeable, Congress had not explicitly prohibited such an application of this provision. Moreover, a liquidating debtor seeking this relief against a reticent unsecured creditor could itself file a proof of claim on behalf of that creditor to subject that creditor's claim to being stripped down. Thus, the section "was intended not only to protect creditors, but is also available as a debtor's remedy."<sup>235</sup>

In this context, the two courts of appeals construed differently the policy implications of various reorganization provisions of the Code. The Third Circuit noted that its interpretation of § 506 did not give an individual debtor a reason to prefer a chapter 7 liquidation to a chapter 13 reorganization. Because § 1322(b)(2) prevents chapter 13 plans from modifying the rights of creditors that hold claims secured only by an interest in the debtor's principal residence, and since § 506 determines the extent to which such claims are secured, the result would be the same.<sup>236</sup> However, the Tenth Circuit interpreted this specific protection of chapter 13 as indicating Congress's "strong preference for reorganization rather than liquidation in the bankruptcy setting."<sup>237</sup> Stripping down liens to allow the debtor to redeem his abandoned property would be "inconsistent with this preference [since it would] allow debtors more in a liquidation than they would receive in a reorganization."<sup>238</sup>

Similarly, the Tenth Circuit noted that, rather than allowing liens to be stripped down, § 1111(b)(1) permits undersecured chapter 11 creditors to elect to hold a secured lien on the prop-

---

<sup>234</sup> *Dewsnup*, 908 F.2d at 591.

<sup>235</sup> *Gaglia*, 889 F.2d at 1309.

<sup>236</sup> *Id.* at 1311.

<sup>237</sup> *Dewsnup*, 908 F.2d at 592.

<sup>238</sup> *Id.*

erty to the full extent of the original obligation.<sup>239</sup> Yet the Third Circuit observed that this section "is carefully drawn and uses specific, precise language": while Congress could exempt certain creditors from the operation of § 506, it had not chosen to so exempt chapter 7 creditors holding undersecured liens on abandoned property.<sup>240</sup> The Third Circuit also indicated that "the availability of lien avoidance is but one factor that a debtor will consider in choosing between Chapter 7 and Chapter 11."<sup>241</sup>

## 2. Resorting to a Subsection-by-Subsection Analysis?

In a brief majority opinion written by Justice Blackmun, the Supreme Court, restricting its decision to the case before it and not to "all possible fact situations,"<sup>242</sup> refused to allow the debtor to "strip down" liens to the value of the collateral. In affirming the decision of the Tenth Circuit, the Court was reluctant to alter the bargain that it perceived to have been made among the debtor/mortgagor and the creditors/mortgagees, under which the liens on the property were intended to remain in effect until foreclosure and the creditors were expected to receive the benefit of any appreciation in the value of the property during the bankruptcy process.<sup>243</sup> Thus, the Court declined to penalize undersecured creditors merely for asserting a claim against abandoned property, or for being drawn into the bankruptcy process by the debtor's or another party's filing proofs of claim on their behalf.<sup>244</sup>

In two ways, the Court effectively ignored *Ron Pair's* standard for the relevance of legislative history. First, without addressing the test enunciated by that decision, the Court found that the legislative history of § 506 supported the preservation of

---

<sup>239</sup> *Id.*

<sup>240</sup> *Gaglia*, 889 F.2d at 1311.

<sup>241</sup> *Id.*

<sup>242</sup> *Dewsnup v. Timm*, 112 S. Ct. 773, 778 (1992). The Court decided to "focus upon the case before us and allow other facts to await their legal resolution on another day." *Id.*

<sup>243</sup> *Id.* Although the Court has more recently, on other grounds, held that chapter 13 debtors cannot strip liens on their primary residences, see *Nobelman v. American Savings Bank*, 113 S. Ct. 2106 (1993), *infra* note 486, it has yet to address the effect of *Dewsnup* on lien-stripping in chapter 11 cases. See William R. Baldiga and Theodore Orson, *The Effect of Dewsnup v. Timm on Chapter 11 Cases*, 110 BANKING L.J. 130, 142 (1993) (unlike chapter 7 debtor in *Dewsnup*, chapter 11 debtor is not eligible for "windfall" from appreciation in value of property; therefore, "it is reasonable to assume that the Supreme Court will . . . refuse to extend its prohibition of 'lienstripping' to the reorganization arena.").

<sup>244</sup> *Id.*

the full amount of the undersecured creditors' lien. Liens on real property had not been affected by bankruptcy proceedings under the Bankruptcy Act of 1898; nor had that Act reduced a creditor's lien on an asset of a liquidating debtor except through payment of the debt.<sup>245</sup> Second, ascribing "a full understanding of this practice" to the legislators who enacted the Code,<sup>246</sup> the Court cited *Ron Pair* as support for the proposition that:

Given the ambiguity here, to attribute to Congress the intention to grant a debtor the broad new remedy against allowed claims to the extent that they become 'unsecured' for purposes of § 506(a) without the new remedy's being mentioned somewhere in the Code itself or in the annals of Congress is not plausible, in our view, and is contrary to basic bankruptcy principles.<sup>247</sup>

(This subversion of *Ron Pair* did not escape the notice of Justice Scalia, whose dissent assailed the majority's opinion as "[a]lmost point for point . . . the methodological antithesis of *Ron Pair*."<sup>248</sup>)

Thus, the Court declined to interpret § 506(d)'s "allowed secured claims" as an "indivisible term of art defined by reference to § 506(a)," which splits undersecured allowed claims into allowed secured claims and allowed undersecured claims; rather, the Court read the phrase "term-by-term to refer to any claim that is, first, allowed, and, second, secured."<sup>249</sup> This construction would in-

---

<sup>245</sup> *Id.* at 778-79.

<sup>246</sup> *Id.* at 779.

<sup>247</sup> *Id.* (citing *Davenport*, 110 S. Ct. at 2138; and *Ron Pair*, 109 S. Ct. at 1032-33). Earlier, the Court had noted that

Were we writing on a clean slate, we might be inclined to agree with [the debtor] that the words "allowed secured claim" must take the same meaning in § 506(d) as in § 506(a). But, given the ambiguity in the text, we are not convinced that Congress intended to depart from the pre-Code rule that liens pass through bankruptcy unaffected.

*Id.* at 778 (footnote omitted).

It was apparently this "ambiguity" that rendered the Code "open to interpretation" under the standard enunciated in *Ron Pair*. However, there was no indication of a "clear conflict" with "any other aspect of the Code."

The Court made a similar end run around the *Ron Pair* test in *Farrey v. Sanderfoot*, 111 S. Ct. 1825, 1829 (1991) (debtor cannot avoid fixing of lien on property under § 522(f)(1) unless he held interest in that property prior to attachment of lien). The parties had agreed on the meaning of the words of the Code section in question, and Justice White's majority opinion identified neither an ambiguity, nor a threat to the purposes of the Code. Nonetheless, the Court cited *Ron Pair* in concluding that a literal reading of § 522(f)(1) "fully comports with the provision's purpose and history," *id.*, even though that decision could have been read to restrict the relevance of legislative history in precisely such situations as *Farrey*'s. *Id.*

<sup>248</sup> *Id.* at 787 (Scalia, J., dissenting).

<sup>249</sup> *Id.* at 777.

clude claims such as those of the *Dewsnup* lienholders, so long as the claims were *allowed in full* and *secured even in part*.

In a dissenting opinion joined by Justice Souter, Justice Scalia protested that the majority “replaces what Congress said with what it thinks Congress ought to have said — and in the process disregards, and hence impairs for future use, well-established principles of statutory construction.”<sup>250</sup> In light of the “ ‘ ‘normal rule of statutory construction that ‘ ‘identical words used in different parts of the same act are intended to have the same meaning,’ ’ ’ ’ ”<sup>251</sup> Justice Scalia criticized the majority for engaging in “what might be called the one-subsection-at-a-time approach to statutory exegesis.”<sup>252</sup>

The majority, noting the textual ambiguity<sup>253</sup> in the interpretation of § 506(d), had specifically declined to express an opinion regarding the construction of the term, “allowed secured claim” elsewhere in the Code.<sup>254</sup> But the dissent noted that the phrase, “allowed secured claim” in § 506(d) “can only be referring to that allowed ‘secured claim’ so carefully described two brief subsections earlier,”<sup>255</sup> and concluded that the majority’s interpretation of this phrase would unavoidably insert redundancies into § 506(d).<sup>256</sup>

---

<sup>250</sup> *Id.* at 780 (Scalia, J., dissenting).

<sup>251</sup> *Id.* (citations omitted). The dissent insisted that “[t]hat rule must surely apply, *a fortiori*, to use of identical words in the same section of the same enactment.” *Id.*

<sup>252</sup> *Id.* at 781 (Scalia, J., dissenting) *Cf.* United States Savings Ass’n of Texas v. Timbers of Inwood Forest, 484 U.S. 365, 371 (1988) (Justice Scalia’s majority opinion notes that statutory terms are often “clarified by the remainder of the statutory scheme—because the same terminology is used elsewhere in a context that makes [their] meaning clear, or because only one of their permissible meanings produces a substantive effect that is compatible with the rest of the law.”).

<sup>253</sup> Justice Scalia criticized the majority for defining as ambiguous any Code provision that was “the subject of disagreement between self-interested litigants,” *id.*, without first applying its own “textual and structural analysis.” *Id.* at 788 (Scalia, J., dissenting).

<sup>254</sup> *Id.* at 778 n.3 (Scalia, J., dissenting).

<sup>255</sup> *Id.* at 780 (Scalia, J., dissenting).

<sup>256</sup> *Id.* at 782 (Scalia, J., dissenting). Section 506(d) provides generally that “[t]o the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void . . . .” 11 U.S.C. § 506(d) (1988) (emphasis added). If the emphasized phrase referred, as the creditors argued, only to the degree by which an undersecured claim is actually secured by the value of the collateral, there would be no need to refer again in this subsection to a “secured” claim. *Dewsnup*, 112 S. Ct. at 782. On the other hand, if, as the debtors asserted, the “secured claim” of § 506(d) connoted any claim, whether fully- or under-secured, for which a lien had been given as security, the second occurrence of “secured” would still be redundant. *Id.* at 783 (Scalia, J., dissenting).

The dissent suggested instead that the emphasized phrase be given its “natural meaning,” *i.e.*, that it signify both the secured and unsecured portions of an under-

As for the majority's "benefit of the bargain" analysis, Justice Scalia observed that, though the Court's analysis of "gaps in the express coverage of the Code, or genuinely ambiguous provisions," had often been informed by pre-Code practice, "we have *never* held pre-Code practice to be determinative in the face of what we have here: contradictory statutory text."<sup>257</sup>

The dissent also addressed several of the disagreements between the Third and Tenth Circuits that had not been discussed by the majority. Like the Third Circuit, Justice Scalia read § 506(d) not as allowing the debtor to redeem the property, but merely as reducing the lienholder's interest in the property to the property's liquidation value.<sup>258</sup> The dissent similarly agreed with *Gaglia* that § 1322(b)(2) would not render chapter 7 more attractive than chapter 13, and noted that the debtor's construction of § 506(d) could equally be applied to chapters 11, 12 and 13.<sup>259</sup>

In addition, Justice Scalia observed that appreciation in the value of the collateral could be denied to creditors not only by stripping down liens in chapter 7 but by applying the "cram-down" provisions of chapter 11 or chapter 13.<sup>260</sup> In fact, far from being disfavored, reorganization (as opposed to liquidation) would continue to have the advantages of allowing the debtor to remain in control of his business and personal assets, and of offering him a discharge from more prepetition *in personam* liabilities.<sup>261</sup> Finally, the dissent faulted the Tenth Circuit for concluding that § 506(a), and therefore § 506(d), does not apply to abandoned property: "[s]ection 506 automatically operates upon all property in which the estate has an interest at the time the bankruptcy petition is filed."<sup>262</sup>

This Justice, insisting that the Code's revised "text means precisely what it says,"<sup>263</sup> saw the majority's approach to the interpretation of § 506(a) as diverging widely from the Court's previous methods of analyzing the Code. For example, two months previously, the Court had in *Wolas* construed § 547(c)(2)'s ordinary course of business exception to the avoidance of preferences as equally applicable to "long-term debt" and "short-term debt." In

---

secured claim, and that the subsequent reference to "an allowed secured claim" be given its "previously established statutory meaning," *i.e.*, that this phrase indicate only the secured portion of the allowed undersecured claim. *Id.*

<sup>257</sup> *Id.* at 786 (Scalia, J., dissenting).

<sup>258</sup> *Id.* at 784 (Scalia, J., dissenting).

<sup>259</sup> *Id.* at 784-785 (Scalia, J., dissenting).

<sup>260</sup> *Id.* at 785 (Scalia, J., dissenting).

<sup>261</sup> *Id.* at 784 (Scalia, J., dissenting).

<sup>262</sup> *Id.* at 785 (Scalia, J., dissenting).

<sup>263</sup> *Id.* at 787 (Scalia, J., dissenting).

*Wolas* as in *Dewsnup*, the Court had confronted ambiguities that would appear to allow significant deviations from prior practice. *Wolas* had championed the statute's "plain meaning" even where Congress had arguably not evaluated all of the implications of the rewritten text, since "the fact that Congress carefully reexamined and entirely rewrote the [section] supports the conclusion that the text . . . as enacted reflects [its] deliberate choice."<sup>264</sup> However, in *Dewsnup* the Court had abandoned the plain meaning of a similarly rewritten section, to revert to the majority's conception of "pre-Code law."<sup>265</sup> Moreover, the majority had seemingly rejected *Ron Pair*'s emphasis on the irrelevance of the legislative history of, and of the pre-Code practice relating to, a Code provision which expressed Congress's intent "with sufficient precision."<sup>266</sup>

Though Justice Scalia's dissent in *Dewsnup* anticipated a disastrous "destruction of predictability" in interpretations of the Code,<sup>267</sup> this characterization might well have been exaggerated. First, it is far from clear that the "plain meaning" approach to the Code has itself fostered a significant degree of predictability.<sup>268</sup> Second, the Court's explicit restriction to § 506(d) of its construction of "allowed secured claim" may actually evidence its continued pursuit of predictability. In interpreting an intricately constructed statute that is rife with interconnections and cross-references, and that, as Justice Scalia himself recognized, "has little to do with natural justice,"<sup>269</sup> the Court's inclination to limit its holdings to the circumstances before it can be seen as an attempt not to create more ambiguities than it resolves. Third, Justice Scalia had himself discerned in *Wolas* that the Code was "utterly devoid of language that could remotely be thought to distinguish between long-term and

---

<sup>264</sup> *Id.* (quoting *Wolas*, 112 S. Ct. at 532 (Scalia, J., concurring)).

<sup>265</sup> *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting). Indeed, the dissent found "[n]o provision of the former Bankruptcy Act, nor any pre-Code doctrine, [that] purported to invalidate — across the board — liens securing claims disallowed in bankruptcy." *Id.*

<sup>266</sup> *Ron Pair*, 489 U.S. at 241 (O'Connor, J., dissenting).

Yet even when Justice Scalia concurred in the plurality's interpretation of a notably ambiguous statute, he would find occasion to deride "that last hope of lost interpretive causes, that St. Jude of the hagiology of statutory construction, legislative history." *U.S. v. Thompson/Center Arms Company*, 112 S. Ct. 2102, 2111 (1992) (Scalia, J., concurring) (National Firearms Act may not be construed to require manufacturer of pistol sold with accompanying conversion kit to pay tax for "making" a "firearm.")

<sup>267</sup> *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting).

<sup>268</sup> See *infra* notes 589-90 and accompanying text.

<sup>269</sup> *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting).

short-term debt," the question there at issue.<sup>270</sup> By contrast, *Dewsnup* addressed the interpretation of the much more complex term, "allowed secured claim." Indeed, the majority in that opinion twice noted the "ambiguity" of this phrase, and resorted to reviewing the section's legislative history. Although the Court did not cite *Ron Pair*, its review of the legislative history suggests that it considers § 506(a) "open to interpretation."<sup>271</sup>

In addition, while *Ron Pair* had dismissed as irrelevant a pre-Code practice that "would be of little assistance," because it "was an exception to an exception, recognized by only a few courts and often dependent upon particular circumstances,"<sup>272</sup> the *Dewsnup* majority cited legislative history and Court precedent as evidence that Congress was fully aware when enacting the Code that existing practice discouraged the stripping down of liens.<sup>273</sup>

Where ambiguities in the Code have not expressed Congress's intent with "sufficient precision" under *Ron Pair*, the Court may still rely on such legislative history or pre-Code practice as is sufficiently developed to have been considered when Congress enacted or amended the Code. This reading would limit the hermeneutic threat that Justices Scalia and Souter perceived in the Court's investigation beyond the plain language of § 506 and in the constriction of the Court's holding to the meaning of one phrase in one subsection of the Code. To the extent that the creditors and the debtor had anticipated these practices, the Court was prepared to give the parties the benefit of their bargain. In this sense, *Dewsnup* indicates that, despite *Ron Pair*'s apparently stringent standard for the relevance of legislative history, extra-statutory considerations will remain relevant to the interpretation of the Code.

#### G. *Taylor v. Freeland & Kronz*<sup>274</sup>

Extending to the Federal Rules of Bankruptcy Procedure its literal interpretation of the Bankruptcy Code, the Court held that all objections to a debtor's claimed exemptions must be filed within the statutorily prescribed period, whether or not the exemptions are justified by the Code or even asserted in good faith by the debtor. The assignment of the *Taylor* opinion to the most

---

<sup>270</sup> *Wolas*, 112 S. Ct. at 534 (Scalia, J., dissenting).

<sup>271</sup> See *supra* note 139 and accompanying text.

<sup>272</sup> *Ron Pair*, 489 U.S. at 246.

<sup>273</sup> *Dewsnup*, 112 S. Ct. at 778-79.

<sup>274</sup> 112 S. Ct. 1644 (1992). The following discussion has been adapted with permission from that presented in Walter A. Effross, *Trustee's Right To Object: Use It or Lose It!*, 131 N.J.L.J. 335 (1992).

junior Justice, and the Court's near-unanimity, imply that, as in Justice Thomas's two prior bankruptcy opinions,<sup>275</sup> the issue may have been seen as relatively straightforward.<sup>276</sup> Yet Justice Stevens's lone dissent, by suggesting that the Court might have abandoned its strict adherence to the words of the statute had the debtor's conduct indicated actual fraud, highlights the potential of the Code's catch-all equitable provision to reconcile the stringent literalism of the "plain meaning" approach with the equitable nature of the Code itself.

### 1. Background

Under § 541(a) of the Code, the commencement of a bankruptcy case creates a "bankruptcy estate," which is broadly defined to include "all legal or equitable interests of the debtor in property" as of that time.<sup>277</sup> Generally, the assets of the bankruptcy estate are distributable to creditors. Section 522(l), however, allows an individual debtor in any of these proceedings to

---

<sup>275</sup> *Connecticut National Bank v. Germain*, 112 S. Ct. 1146 (1992) (regarding appeals of interlocutory orders; five-Justice majority concurred in by remaining Justices); *Holywell Corp. v. Smith*, 112 S. Ct. 1021 (1992) (trustee required to pay taxes for gains realized from sale of liquidated real estate; unanimous decision).

<sup>276</sup> In the wake of *Taylor*, trustees and creditors would do well to observe scrupulously the time limits for filing objections to: a debtor's discharge (under Code § 727(c) and Bankruptcy Rule 4004(a)); the dischargeability of a debt (Code § 523(c) and Bankruptcy Rule 4007(c)); the use, sale or lease of property (Code § 363 and Bankruptcy Rule 6004(b)); and the abandonment of property (Code § 554 and Bankruptcy Rule 6007(a)).

Under Bankruptcy Rule 9006(b)(3), the time limits for filing the first of these two objections may be extended only after a hearing on notice, requested by motion made before the original time limit has expired. The court may extend the latter two time limits with or without motion or notice if request is made before the original, or a previously extended, period expires, or, if the period has expired, on motion "where the failure to act was the result of excusable neglect."

<sup>277</sup> Section 541(a) provides:

The commencement of a [voluntary, joint, or involuntary] case creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

11 U.S.C. § 541(a) (1988).

Section 541(b) excludes from the estate: "any power that the debtor may exercise solely for the benefit of an entity other than the debtor"; certain interests of the debtor as lessee of nonresidential real property; any eligibility of the debtor to participate in certain education programs; and any accreditation status or state licensure of the debtor as an educational institution. *Id.* § 541(b). In addition, § 542(c)(2) provides that "[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under [Title 11]." *Id.* § 541(c)(2).



file a list of property that should, under § 522(b), be "exempted" from the estate: *i.e.*, returned to the debtor.<sup>278</sup> Section 522(b)(1)<sup>279</sup> provides that, in those states that have not precluded the "federal exemptions" of § 522(d),<sup>280</sup> debtors may avail themselves of any or all of those eleven specific categories of exemptions (*e.g.*, a debtor can exempt his interest, not to exceed \$1200, in one motor vehicle).

As an alternative to the federal exemptions, § 522(b)(2)(A) allows individual debtors to claim as exempt in federal bankruptcy proceedings any property that is exempt from attachment by creditors under applicable state or local law (*e.g.*, the debtor's interest in certain spendthrift trusts) or under any federal law other than the federal exemptions (*e.g.*, civil service retirement

<sup>278</sup> Section 522(l) provides:

The debtor shall file a list of property that the debtor claims as exempt under [§ 522(b)]. If the debtor does not file such a list, a dependent of the debtor may file such a list, or may claim property as exempt from property of the estate on behalf of the debtor. Unless a party in interest objects, the property claimed as exempt on such list is exempt.

11 U.S.C. § 522(l) (1988).

<sup>279</sup> Section 522(b) provides:

Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (1), or, in the alternative, paragraph (2) of this subsection . . . .

(1) property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor under paragraph (2)(A) of this subsection specifically does not so authorize; . . . .

(2)(A) any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer period of such 180-day period than in any other place; and

(B) any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law.

11 U.S.C. § 522(b) (1988).

<sup>280</sup> Section 522(d) identifies eleven separate classes of property that may be exempted under § 522(b)(1), including: a specified dollar value of the debtor's interest in certain real property, in one motor vehicle, in certain personal, family, or household possessions, and in tools of the trade of the debtor or of a dependent of the debtor; certain unmaturing life insurance contracts; professionally prescribed health aids for the debtor or for a dependent of the debtor; and the debtor's right to receive certain benefits or payments under federal, state or local law. *See generally* 11 U.S.C. § 522(d) (1988).

benefits).<sup>281</sup>

Section 522(l) provides that "Unless a party in interest objects, the property claimed as exempt on [the debtor's] list is exempt." Under Bankruptcy Rule 4003(b), such objections may be filed by the trustee, or by any creditor, within thirty days after the conclusion of the creditors' meeting or of the filing of any amendment to the list or supplemental schedules, unless the time for objection has been previously extended by the court.<sup>282</sup> Bankruptcy Rule 4003(c) provides that the objecting party shall bear the burden of proof at a hearing before the court.<sup>283</sup>

In October 1984, when Emily Davis filed a chapter 7 bankruptcy petition, a sex and age discrimination judgment rendered in her favor by the Pennsylvania Commonwealth Court was being appealed to the Pennsylvania Supreme Court by her former employer. On the schedules to her petition, Davis, noting that the potential proceeds from the judgment were "unknown," listed them as an asset that should be exempted from her bankruptcy estate.<sup>284</sup>

At the required meeting of Davis's creditors, in January 1985, her counsel advised the trustee that the judgment might ultimately result in a payment to the debtor of approximately \$90,000. The trustee wrote to the debtor's counsel several days later, advising that any proceeds of the lawsuit would be property of the bankruptcy estate. In response to the trustee's request for further information about the action, Davis's counsel informed him that a settlement might be reached for \$110,000.<sup>285</sup>

However, the trustee did not file a formal objection to the debtor's exemption of these funds from her bankruptcy estate.

---

<sup>281</sup> See *infra* note 279 and accompanying text.

<sup>282</sup> Rule 4003(b) provides:

The trustee or any creditor may file objections to the list of property claimed as exempt within 30 days after the conclusion of the meeting of creditors held pursuant to Rule 2003(a), or the filing of any amendment to the list or supplemental schedules unless, within such period, further time is granted by the court. Copies of the objections shall be delivered or mailed to the trustee and to the person filing the list and the attorney for such person.

FED. R. BANKR. P.4003(b).

<sup>283</sup> Rule 4003(c) provides that "[i]n any hearing under this rule, the objecting party has the burden of proving that the exemptions are not properly claimed. After hearing on notice, the court shall determine the issues presented by the objections." FED. R. BANKR. P. 4003(c).

<sup>284</sup> Taylor v. Freeland & Kronz (*In re Davis*), 105 B.R. 288, 290-91 (Bankr. W.D. Pa. 1989).

<sup>285</sup> Taylor v. Freeland & Kronz, 112 S. Ct. 1644, 1646-47 (1992).

Rather, he stated on the record that, in his experience, debtors were likely to settle pending suits for amounts well within the exemption limits.<sup>286</sup> The trustee also opined that the discrimination claim might be "a nullity."<sup>287</sup>

In October 1986, the Pennsylvania Supreme Court affirmed the debtor's judgment against her former employer. Davis subsequently settled the matter for \$110,000 (which included her attorneys' fees). Of this amount, \$23,483.75 was to be paid "as and for back pay or front pay"; another \$23,483.75, "as and for all alleged tort claims or any other tort claims not represent[ing] asserted wage losses"; and the remaining \$63,032.50, for legal fees and costs.<sup>288</sup> The trustee filed a complaint against the debtor and her attorneys in bankruptcy court, asserting that the settlement payments were property of the estate. Noting that the trustee had not timely filed an objection to the debtor's claim of exemption, the debtor and her counsel refused to relinquish these funds.

The bankruptcy court read into § 522(l) a requirement that the debtor assert all exemption claims in good faith. Otherwise, the court observed, an unscrupulous debtor could achieve "exemption by declaration": her broad assertion that *all* of the estate's property was exempt would force her creditors and the already-overburdened trustee to evaluate the status of each asset.<sup>289</sup> If this tactic were widely adopted, "[o]rderly administration of such debtors' estates would be difficult, if not impossible, and uncertainty and constant litigation, if not outright chaos, would result."<sup>290</sup> Moreover, this type of blanket exemption would contradict § 522(b)'s explicit limitation of exemptions to property already exempted by federal, state or local law.<sup>291</sup>

The court noted that Davis's claim of exemption appeared to be predicated on the federal exemption for loss of future earnings under § 522(d)(11)(E).<sup>292</sup> It did not disturb that component

---

<sup>286</sup> *Id.* at 1647. The exemption for payments for loss of future earnings, while not limited by an absolute dollar value, is restricted by § 522(d)(11)(E) to payment "to the extent reasonably necessary for the support of the debtor and any [of her] dependent[s]." 11 U.S.C. § 522(d)(11)(E) (1988).

<sup>287</sup> *Taylor*, 112 S. Ct. at 1646-47.

<sup>288</sup> *Taylor*, 105 B.R. at 291.

<sup>289</sup> *Id.* at 292-93.

<sup>290</sup> *Id.*

<sup>291</sup> *Id.* at 292-93.

<sup>292</sup> *Id.* at 293. Section 522(d)(11)(E) exempts from the bankruptcy estate [t]he debtor's right to receive, or property that is traceable to—

(E) a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to

of the settlement identified as for "back pay or front pay," even though no specific federal exemption provides for "back pay." However, since no federal exemption applied to tort claims, the court allowed the trustee to recover for the benefit of the bankruptcy estate the \$23,483.75 that had been allocated for such claims.<sup>293</sup> Indeed, because the debtor had admitted mischaracterizing that portion of the settlement in order to avoid tax liability, the court held that she was now estopped from redefining the "tort claim" proceeds as payment for lost wages.<sup>294</sup>

The recovered funds would satisfy not only all creditors' claims, with interest, but also the trustee's counsel fees for bringing the recovery action. Thus, the court declined to determine whether the remainder of the settlement amount was due to the trustee, who would merely have returned such funds to the debtor. Given his "dereliction of duty and/or ignorance of bankruptcy law,"<sup>295</sup> the court was unwilling to allow the trustee to deduct additional fees for his administration of any such funds. The district court affirmed, since "[a]llowing the debtor to recover proceeds for which there was no statutory basis [for exemption] would render § 522(b) negatory."<sup>296</sup>

However, the Third Circuit reversed the decision of the district court, finding the result below "unwarranted under the clear language of the Bankruptcy Code and Bankruptcy Rules,"<sup>297</sup> whose "import is clear and [who] admit of no exception."<sup>298</sup> Citing the legislative history of the Code and Rules, the appeals court insisted that objections be timely made, even if the debtor's claimed exemption was invalid or lacked a good-faith statutory basis.

Indeed, before the enactment of the Code, former Bankruptcy Rule 403 had required the trustee to file a report deeming each exemption claim allowable or non-allowable, subject to objections by the debtor and creditors within fifteen days. As the Advisory Committee on Bankruptcy Rules' Note to current Bank-

---

the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

11 U.S.C. § 522(d)(11)(E) (1988).

<sup>293</sup> *Taylor*, 105 B.R. at 293. The trustee was also authorized to recover from Freeland & Kronz, the initial transferee, "interest at the prevailing legal rate, from the date of the initial transfer on September 17, 1987." *Id.*

<sup>294</sup> *Id.* at 294.

<sup>295</sup> *Id.*

<sup>296</sup> 118 B.R. 272, 275 (W.D. Pa. 1990).

<sup>297</sup> *Taylor v. Freeland & Kronz*, 938 F.2d 420, 421 (3d Cir. 1991).

<sup>298</sup> *Id.* at 423.

ruptcy Rule 4003 observes, the Code shifted that burden by allowing the debtor to claim exemptions to which the creditors and the trustee could object within thirty days.<sup>299</sup> To the Third Circuit panel, "[n]othing in the legislative materials suggest[ed] that any exceptions to this bright-line rule were intended."<sup>300</sup> The court of appeals also cited as support another Note of the Advisory Committee, which indicated that, "[i]n the interest of prompt administration of bankruptcy cases certain time periods may not be extended."<sup>301</sup>

The Third Circuit concluded that the finality and certainty created by strict deadlines outweighed any threat that unscrupulous debtors would incapacitate the bankruptcy system, or receive windfalls, by declaring all of their assets exempt. Not only does Bankruptcy Rule 9011 (a counterpart to Federal Rule of Civil Procedure 11) provide for sanctions for bad faith claims of exemption, but vigilant trustees and creditors should generally be able to detect and challenge unfounded claims for exemption. "Thus, in the vast majority of cases, overzealous claims of exemptions by a debtor will serve only to induce the enmity of the other parties and of the court."<sup>302</sup>

Nor would a bankruptcy court's failure to reject unchallenged claims of exemption, even if they were unjustified or brought in bad faith, circumvent the restrictions of § 522(b). That section does not become operative, the Court of Appeals held, until the trustee or a creditor files an objection to the claimed exemption under § 522(l).<sup>303</sup> By contrast, the lower courts would first have scrutinized controversial claims under § 522(b), whether or not an objection had been timely filed. This regime, the Third Circuit noted, "would render [S]ection 522(l) meaningless."<sup>304</sup>

---

<sup>299</sup> *Id.* at 425 (citing FED. R. BANKR. P. 4003 (advisory committee note)).

<sup>300</sup> *Id.* at 425.

<sup>301</sup> *Id.* (quoting FED. R. BANKR. P. 9006 (advisory committee note)). Curiously, while Bankruptcy Rule 9006(b)(2)—to which this Note is appended—does prohibit the enlargement of certain time periods in which action may be taken, this prohibition is not applicable to the time period, set forth in Rule 4003(b), for filing objections. Indeed, Rule 9006(b)(2) specifically provides that "the court may enlarge the time for taking action [under Rule 4003(b)] only to the extent and under the conditions stated in [that Rule]." FED. R. BANKR. P. 9006(b)(2).

<sup>302</sup> *Id.* at 426.

<sup>303</sup> *Id.*

<sup>304</sup> *Id.*

## 2. Inviting Equitable Elaboration of Plain Meaning?

In his third Supreme Court opinion on creditors' rights, Justice Thomas affirmed the Third Circuit's decision, on the grounds that "[d]eadlines may lead to unwelcome results, but they prompt parties to act and they produce finality."<sup>305</sup> The high court thus rejected opposing precedent in the Fifth, Sixth, and Eighth Circuits.<sup>306</sup>

The Court observed that, in addition to Rule 9011, § 727(a)(4)(B) (denying discharge for fraudulent claims), Rule 1008 (mandating verified filings) and 18 U.S.C. § 152 (criminalizing bankruptcy fraud) provide disincentives for a debtor and her counsel to attempt "exemption by declaration."<sup>307</sup> Congress remained free to supplement these protections if it found them inadequate.<sup>308</sup>

Significantly, the Court declined on procedural grounds<sup>309</sup> to authorize the lower courts to invalidate the claimed exemption under § 105(a) of the Code, which provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Code]," despite any Code provision "providing for the raising of an issue by a party in interest."<sup>310</sup> However, the length and tone of this dismissal appeared unusually defensive. From the Court's six-sentence justification, which cited four Supreme Court decisions and two Supreme Court Rules, it might be inferred that the Justices had recognized the importance of this issue and were awaiting — perhaps even inviting — a suitable case in which to address it.

---

<sup>305</sup> *Taylor v. Freeland & Kronz*, 112 S. Ct. 1644, 1648 (1992).

<sup>306</sup> *In re Peterson*, 920 F.2d 1389, 1393-95 (8th Cir. 1990) (appropriate standard for analysis of late objections to claimed exemptions is "middle-ground" of determining whether debtor had good-faith statutory basis for claimed exemption); *In re Dembs*, 757 F.2d 777, 780 (6th Cir. 1985) (requiring good-faith statutory basis for exemption); *In re Sherk*, 918 F.2d 1170, 1174 (5th Cir. 1990) (inferring requirement of statutory basis for claimed exemption).

<sup>307</sup> *Taylor*, 112 S. Ct. at 1648.

<sup>308</sup> *Id.* at 1648-49.

<sup>309</sup> *Id.* at 1649. The issue had been raised by the trustee for the first time in his opening brief on the merits, in contravention of the Court's Rule 14.1(a) and 24.1, which restrict the Court's examination to the questions set forth in the petition for certiorari.

Nonetheless, this intriguing resolution to the problem of the delinquent trustee had been accepted by the Fourth Circuit and by district courts in Wisconsin and Pennsylvania. *Id.* (citing *Ragsdale v. Genesco, Inc.*, 674 F.2d 277, 278 (4th Cir. 1982); *In re Stainforth*, 116 B.R. 127, 131 (W.D. Wis. 1990); *In re Budinsky*, No. 90-01099, 1991 WL 105640 (W.D. Pa. June 10, 1990).

<sup>310</sup> 11 U.S.C. § 105 (1988).

The application of § 105 might well have resolved Justice Stevens's argument in dissent that, given the equitable nature of bankruptcy, a literal reading of the Code and Rules should be supplanted by the doctrine of equitable tolling. Traditionally, that doctrine has allowed statutes of limitation to be extended where the guilty party affirmatively concealed the fraud or where the defrauded party's unawareness of the fraud was not due to its own lack of care.<sup>311</sup> Yet the dissent seemed to be stretching to fit the facts of *Taylor* to those conditions.

First, Justice Stevens observed that the debtor's claims for exemption of the entire settlement amount were, even if not fraudulent, at least unjustified by the Code and Rules.<sup>312</sup> As the Third Circuit had recognized, the bankruptcy and district courts initially resolved whether a claim for exemption that had drawn an objection satisfied § 522(b); if it did not, these courts then addressed whether the claim had been filed in good faith. The dissent went so far as to propose that since Davis's exemption claim did not meet the requirements of § 522(b), the 30-day objection period had never begun to run.<sup>313</sup>

But the claim of exemption filed with Davis's petition (as opposed to her deliberate postpetition representation regarding tort claims) would not so clearly qualify as affirmative fraud. To begin with, it could be argued that the debtor and her counsel had in good faith mistakenly filled out the schedule, or misread the Code. Even if the claim *had* been fraudulently made, no effort had been made to conceal such fraud. Indeed, Davis and her counsel had apparently been candid in representing to the trustee the potential amount of settlement.

Second, although the trustee had been aware of an objectionable claim, and it was his own "lack of care" in failing to file a timely objection that had created his present difficulties, the dissent noted that strict operation of the thirty-day objection period would harm "innocent creditors."<sup>314</sup> However, many creditors would have been on notice of the bankruptcy filing, and would have had the opportunity to examine the schedules with their counsel, and to object to the claimed exemption, within the thirty-day period.

Finally, Justice Stevens suggested that the debtor would not

---

<sup>311</sup> *Taylor*, 112 S. Ct. at 1650 (Stevens, J., dissenting) (citing *Bailey v. Glover*, 21 U.S. (1 Wall.) 342, 347-50 (1875)).

<sup>312</sup> *Id.*

<sup>313</sup> *Id.* at 1652 (Stevens, J., dissenting).

<sup>314</sup> *Id.* at 1650 (Stevens, J., dissenting).

be prejudiced by the trustee's failure to object promptly.<sup>315</sup> But the dissent's *de facto* extension of the objection period would prejudice other participants in the bankruptcy process by reducing its efficiency and by undermining its certainty and finality. As the dissent itself recognized, the trustee's counsel, warning of the potential systemic burden of "exemption by declaration," had noted that the 880,000 bankruptcy cases filed in 1991 had been divided among only 291 bankruptcy judges.<sup>316</sup>

The dissent concluded by speculating that "if the debtor or the trustee were guilty of fraud, the Court would readily ignore what it now treats as the insurmountable barrier of 'plain meaning.' . . . In my view, it is a mistake to adopt a 'strict letter' approach . . . when justice requires a more searching inquiry."<sup>317</sup>

It remains to be seen whether, in light of the equitable nature of the bankruptcy court, the sweeping language of § 105(a) will foster a "searching inquiry" to overcome the new literalism of such decisions as *Ron Pair*, *Wolas*, and *Toibb*. The Court's subsequent decision to construe expansively the "excusable neglect" standard for failure to file documents timely,<sup>318</sup> although not directly addressing § 105, indicates that the "plain meaning" doctrine may yet be amenable to considerations of equity.

#### H. *Barnhill v. Johnson*<sup>319</sup>

In *Barnhill*, the Court held that funds transferred by a

---

<sup>315</sup> *Id.* According to Justice Stevens, "[u]nder these circumstances, unless the debtor could establish some prejudice caused by the trustee's failure to object promptly, I would hold that the filing of a frivolous claim for an exemption is tantamount to fraud for purposes of deciding when the 30-day period begins to run." *Id.*

The time limits with respect to the right to file an objection to the abandonment of property may be among the most significant in today's bankruptcy practice, given the attempts of many trustees or debtors-in-possession to abandon environmentally troubled properties for which the bankruptcy estates cannot afford cleanup costs. See, e.g., *State of New Jersey Department of Environmental Protection v. North American Products Acquisition Corp.*, 137 B.R. 8, 10 (D.N.J. 1992) (construing Supreme Court's *Midlantic* decision as requiring pre-abandonment hearing to determine threat posed to public and property by abandonment of contaminated facility). An extended discussion of this opinion appears in Walter A. Effross, *The Toxic Risk and "the Public Fisc,"* 1 N.J.L. 945 (1992).

<sup>316</sup> *Id.* at 1651 n.4 (Stevens, J., dissenting).

<sup>317</sup> *Id.* at 1652 (Stevens, J., dissenting).

<sup>318</sup> See *infra* notes 430-85 and accompanying text for a discussion of *Pioneer Investment Services Company v. Brunswick Associates Limited Partnership*.

<sup>319</sup> 112 S. Ct. 1386 (1992). The following discussion has been adapted with permission from that presented in Walter A. Effross, *Supremes Endorse "Date of Honor" Check Rule*, 131 N.J.L.J. 6 (1992).



debtor's check are recoverable for the benefit of creditors if the check is *honored* within ninety days before the debtor's bankruptcy. In rejecting an alternative approach — that recovery is possible only if the check is *delivered* within this "preference period" — the Court closely analyzed the definition of "transfers," both under the Code and under the Uniform Commercial Code (the "U.C.C."), and distinguished between the legislative histories of two related subsections of the Code. In absence of support from statute or precedent, the Court declined to construe broadly the phrase, "conditional transfer," thereby signalling an informal limit to the "plain meaning" theory.

### 1. Background

Under § 101(54) of the Code, a "transfer" includes any "mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing or parting with property or with an interest in property. . . ." <sup>320</sup> In turn, transfers are a key element of § 547's definition of "preferences," presumptively partial transfers made by the debtor before entering bankruptcy. <sup>321</sup> Preferential transfers may be reversed by the trustee or debtor-in-possession to recoup the transferred property for more equitable distribution to creditors.

Section 547(b) defines a preference as "any transfer of an interest of the debtor in property. . . made on or within 90 days before the filing of the petition" to or for the benefit of a creditor, that enables the creditor to receive more than the creditor would in the debtor's liquidation under the Code. <sup>322</sup> However, neither the Code nor its legislative history explicitly indicates the time at which transfers by check are deemed to have occurred for purposes of § 547(b).

In *Barnhill*, the debtor's check, which a creditor received ninety-two days before the bankruptcy filing, was dated and deposited the next day, and was honored the following day by the

---

<sup>320</sup> 11 U.S.C. § 101(54) (1988).

<sup>321</sup> See *supra* note 177 and accompanying text.

<sup>322</sup> See *id.*

The 90-day "preference period" is extended to one year where the transfer is made to or for the benefit of an "insider" such as a controlling person of, or an entity affiliated with, the debtor. 11 U.S.C. § 547(b)(4)(B) (1988). A literal reading of § 547 in conjunction with § 550(a), which relates to the recovery of preferential transfers, has given rise to the so-called *Deprizio* problem: a one-year preference period applicable to the lender who takes the guaranty of an insider of the debtor. See, e.g., Walter A. Effross, *Deprizio's Honor: Lenders, Insider Guarantors and the Prisoners' Dilemma*, 21 SETON HALL L. REV. 774 (1991).

drawee bank.<sup>323</sup> At issue was whether the transfer was recoverable as falling within the ninety-day "preference period." The creditor argued that the transfer had occurred when it had received the check, two days before the preference period had begun. The bankruptcy trustee countered that the transfer had taken place when the check had been honored, on the first day of the preference period. The bankruptcy court<sup>324</sup> and the district court<sup>325</sup> supported the creditor's "date of delivery" approach, but the United States Court of Appeals for the Tenth Circuit reversed, favoring the trustee's "date of honor" rule.<sup>326</sup> Because of the conflict among the circuits on this issue, the Supreme Court granted certiorari.

a. Conflict Among the Circuits

i. Background

In dating transfers by check for purposes of preference avoidance, several circuits had found relevant the legislative his-

---

<sup>323</sup> Johnson v. Barnhill (*In re Antweil*), 111 B.R. 337, 339 (D.N.M. 1990).

<sup>324</sup> Johnson v. Barnhill (*In re Antweil*), 97 B.R. 69 (Bankr. D.N.M. 1989). The bankruptcy court, following the Tenth Circuit's decision in Bernstein v. RJL Leasing (*In re White River Corporation*), 799 F.2d 631 (10th Cir. 1986), held that the "date of delivery" rule not only would allow the debtor (rather than the bank) to determine the date of transfer, but would also "comport with the state law treatment of post-dated checks." *Johnson*, 97 B.R. at 70. The relevant state law determined the time at which an antedated or postdated check is payable by reference to "the stated date if the instrument is payable on demand or at a fixed period after [that] date." *Id.* (citation omitted). The bankruptcy court therefore defined "delivery" as "the later of the date a check is received or dated." *Id.*

The court found the "date of delivery" rule equally applicable to § 547(b) preference actions and to § 547(c) defenses, because there appeared to be "no good reason to view a single transaction differently depending on which subsection of the statute is being read." *Id.* Moreover, because in this situation both the date of the check at issue and the date of its delivery were outside the 90-day preference period, a "date of honor" rule would not aid the plaintiff. *Id.*

<sup>325</sup> The district court affirmed the bankruptcy court's conclusion that the "date of delivery" rule was "in accord with much of the legislative history and policy objectives" identified by *White River*, *supra* note 312. *Johnson*, 111 B.R. at 340.

Because both the date written on the check and the date of the check's receipt fell outside the ninety-day preference period, the district court declined to adopt or to reject the lower court's definition of the date of delivery as the later of the dates on which a check is received and dated. *Id.* at 342. Moreover, because only one-day intervals elapsed between the check's delivery, date and deposit, and honoring, the court found the postdating relevant not to the anticipated time of honor but instead to the time of presentment to the drawee bank, and held that the check was "intended as a cash payment." *Id.* (citing *Global International Airways Corp. v. Evergreen Air Center, Inc. (In re Global International Airways Corp.)*, 80 B.R. 990, 995 (Bankr. W.D. Mo. 1987) (applying "date of delivery" rule to postdated checks if transfer of check constitutes substantially contemporaneous payment)).

<sup>326</sup> Johnson v. Barnhill, 931 F.2d 689 (10th Cir. 1991).

tory of § 547(c). That section exempts certain arms'-length transactions from § 547(b)'s definition of preferences.<sup>327</sup> For example, to encourage trade creditors not to desert a troubled business, the bankruptcy courts will not reverse payments made or security interests given by the debtor in exchange for new goods and services supplied to it, or for debts incurred by the debtor in the ordinary course of its business, before the bankruptcy filing.

The legislative history of § 547(c) contains statements by Senator DeConcini and Representative Edwards that "payment of a debt by means of a check is equivalent to a cash payment, unless the check is dishonored" and that "for these purposes, payment is considered to be made when the check is delivered."<sup>328</sup> As the Supreme Court noted, the "date of delivery" rule for § 547(c) transfers had been unanimously supported by the five Circuits that had addressed the issue.<sup>329</sup>

Only one of these decisions, however, had explicitly concerned whether the date of "delivery" occurs when the check is mailed by the debtor, versus when it is received by the payee. The Fourth Circuit had found delivery to take place on "the date that the creditor receives the check."<sup>330</sup> Less definitively, the Ninth Circuit had held, in the context of § 547(c), that a check was delivered at "the time the debtor gave the check to the creditor."<sup>331</sup> Yet all five of the Circuits adopting the "date of delivery" rule required for the operation of that rule that the check be presented within the thirty-day period set by U.C.C. § 3-503(2)(a) as "a reasonable time for presentment."<sup>332</sup>

---

<sup>327</sup> 11 U.S.C. § 547(c)(1), (2) (1988).

<sup>328</sup> 124 CONG. REC. at 34000 and 34200 (1978).

<sup>329</sup> *Johnson*, 112 S. Ct. at 1391 n.9 (citation omitted).

<sup>330</sup> *In re Continental Commodities, Inc.*, 841 F.2d 527, 530 (4th Cir. 1988), *following* *O'Neill v. Nestle Libbys P.R., Inc.*, 729 F.2d 35, 38 (1st Cir. 1984) (§ 547(e)(1)(B) deals with perfection of security interests in debtor's property and does not apply to § 547(c) cases in which creditor has not taken debtor's check as security) and *In re White River Corp.*, 799 F.2d at 633-34 (*O'Neill* is supported by legislative history, policy considerations and pragmatic concerns; "delivery date" rule comports with commercial practice, encourages trade creditors to continue dealing with troubled businesses, and allows debtor to determine precise date of transfer).

<sup>331</sup> *Robert K. Morrow, Inc. v. Agri-Beef Co. (In re Kenitra, Inc.)*, 797 F.2d 790, 791 (9th Cir. 1983), *cert. denied*, 479 U.S. 1054 (1987). *Agri-Beef* held that the enactment of the Code had instituted "no changes . . . that suggest a reason to depart from the rule in *Shamrock Golf*." *Morrow*, 797 F.2d at 791 n.1 (citing *Shamrock Golf v. Richcraft, Inc.*, 680 F.2d 645 (9th Cir. 1982) (adopting date of discovery rule, in context of Bankruptcy Act)).

<sup>332</sup> *Braniff Airways, Inc. v. Midwest Corp.*, 873 F.2d 805, 808 (5th Cir. 1989);

ii. *Sixth Circuit Precedent*

After examining the legislative history of § 547(c), the Sixth Circuit applied the “date of delivery” rule to § 547(b) as well, since “[t]o give the word ‘transfer’ a different meaning in these complementary subparts seems inconsistent, unworkable, and confusing.”<sup>333</sup> Moreover, a “date of delivery” approach would have the virtues of “consistency, clarity, and simplicity,” and would fulfill the expectations both of debtors and of creditors.<sup>334</sup> Although the relevant legislative history made no reference to § 547(b), the court of appeals attributed this omission to the process of assembling committee reports rather than to a specific Congressional intent to distinguish the timing of preferences under the two sections.<sup>335</sup>

Under the Sixth Circuit’s analysis, “delivery” occurred when the payee received the check rather than when the debtor mailed the check. The court of appeals observed that this rule not only avoided inquiry into which party insisted on payment by check, or confusion over when a check was mailed, but placed the burden of documentation on the recipient (to post the check) rather than on the debtor (to retain proof of mailing).<sup>336</sup> Like the circuit courts that had approached the question in the context of § 547(b), the Sixth Circuit required as a condition of this timing

---

*Continental Commodities*, 841 F.2d at 530; *In re Wolf & Vine*, 825 F.2d 197, 201-02 (9th Cir. 1987); *White River*, 99 F.2d at 634; *O'Neill*, 829 F.2d at 38.

U.C.C. § 3-503(2)(a) provides:

(2) A reasonable time for presentment is determined by the nature of the instrument, any usage of banking or trade and the facts of the particular case. In the case of an uncertified check which is drawn and payable within the United States and which is not a draft drawn by a bank the following are presumed to be reasonable periods within which to present for payment or to initiate bank collection:

(a) with respect to the liability of the drawer, thirty days after date or issue whichever is later.

*Id.*

<sup>333</sup> Official Unsecured Creditors’ Comm. of Belknap, Inc. v. Shaler Corp. (*In re Belknap, Inc.*), 909 F.2d 879, 883 (6th Cir. 1990).

<sup>334</sup> *Id.*

<sup>335</sup> *Id.*

<sup>336</sup> *Id.* at 884. Similarly, the Fourth Circuit applied the “date of delivery” rule after drawing analogies to § 547(c) and § 549(a) and observing that “in the commercial arena, for most purposes, payment by check is the end of a commercial transaction.” *In re Virginia Information Systems Corp.*, 932 F.2d 338, 341 (4th Cir. 1991) (citing *In re Continental Commodities*, 841 F.2d 527 (4th Cir. 1988); *Quinn Wholesale, Inc. v. Northern*, 873 F.2d 77 (4th Cir.), *cert. denied*, 493 U.S. 851 (1989) (under *Continental* analysis, transfer was effective on date of delivery, in context of avoidance of postpetition transaction under § 549(a))).

that the check be presented within thirty days of delivery, and honored upon presentment.

However, the Tenth Circuit's opinion in *Barnhill*, noting the divergent policies of the two provisions, specifically rejected the application of § 547(c)'s legislative history to § 547(b). Section 547(c), the court observed, encourages creditors to transact with a troubled debtor, by fulfilling, despite the threat of the debtor's bankruptcy, the creditors' ordinary commercial expectations of payment. By contrast, § 547(b) is intended to recover preferential transfers for distribution to creditors, whether or not the transferees envisioned the debtor's bankruptcy.<sup>337</sup>

The Tenth Circuit also disagreed with the Sixth Circuit about the most efficient manner in which to document transactions made by check. While the date of honor could be evidenced by the bank statement, there would not necessarily be a clear record of the date of delivery. Indeed, under U.C.C. § 3-409(1),<sup>338</sup> the debtor's check is not effective when provided to the recipient, but only when accepted by the drawee bank. Since the debtor's bank account could be garnished by another creditor, and thus the check recipient's right to the account funds nullified, at any time before the check is honored, the transfer could occur only when the check is actually honored. The same conclusion had earlier been reached by the Eleventh Circuit and Seventh Circuit<sup>339</sup> in their analyses of § 96(a)(2) of the Bankruptcy Act.<sup>340</sup>

Concepts similar to those of the Bankruptcy Act's § 96(a)(2) are embodied in Code's § 547(e), which has itself been seen as a statutory source for determining the preferential timing of transfers by check under § 547(b). Section 547(e)(1) provides that for the purposes of § 547's preference analysis, transfers of fixtures or property other than real property are perfected when "a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee."<sup>341</sup> Under § 547(e)(2), if a transfer is perfected within ten days of its taking effect, the

---

<sup>337</sup> *Johnson v. Barnhill*, 931 F.2d 689, 692-93 (1991).

<sup>338</sup> U.C.C. § 3-409(1) provides that "[a] check or other draft does not of itself operate as an assignment of any funds in the hands of the drawee available for its payment, and the drawee is not liable on the instrument until he accepts it."

<sup>339</sup> *Nicholson v. First Investment Co.*, 705 F.2d 410, 413 (11th Cir. 1983); *Fitzpatrick v. Philco Finance Corp.*, 491 F.2d 1288, 1293 (7th Cir. 1974).

<sup>340</sup> 11 U.S.C. § 96(a)(2) provided that a transfer was made when the transferee's rights in the property were superior to those of any subsequent judicial lien-holder whose rights stemmed from a simple contract.

<sup>341</sup> 11 U.S.C. § 547(e)(1) (1988).

transfer will be regarded as having been made when it took effect; otherwise, the transfer will be deemed to have been made at the time of perfection.<sup>342</sup> If the transfer is not perfected before the commencement of the debtor's bankruptcy proceedings, the transfer will be deemed to have been made at the later of the commencement of the case or ten days after the transfer took effect.<sup>343</sup>

As the Tenth Circuit noted, however, the language of perfection, which refers to the attachment of security interests, is not directly appropriate to the honoring of a check, which involves the direct transfer of the debtor's assets, unless the check has been taken as security. "It is unnecessary and incorrect to analogize to security interests and to U.C.C. Article 9 perfection rules when U.C.C. Article 3 squarely covers commercial paper such as checks."<sup>344</sup>

### iii. *Seventh Circuit Precedent*

Contradicting the Tenth Circuit, the Seventh Circuit championed the "date of delivery" rule, with "delivery" defined as the date on which the creditor received the debtor's check. This court of appeals advanced a more subtle analysis, based on the inclusion in § 101(54)'s definition of "transfer" of both "absolute [and] conditional" transfers.<sup>345</sup> The delivery of the debtor's check to the creditor was seen as a conditional transfer, since the drawee bank could refuse to honor the check. When the drawee did honor the check, the transfer of the funds became absolute. Thus, if *either* the date of delivery *or* the date of honor<sup>346</sup> occurred within the preference period, the payment could be recovered for the benefit of creditors.<sup>347</sup>

Under this analysis, the true significance of § 96(a)(2) of the Bankruptcy Act lay not in its having been construed as supporting a "date-of-honor" rule, but in the transformation of its language into § 547(e) of the Code. Not only does § 547(e)(1) abandon the Act's hypothetical-judgment analysis of transfers, but under § 547(e)(2) a transfer occurs when even a conditional interest in the funds is created, although, until that interest is

---

<sup>342</sup> *Id.* § 547(e)(2).

<sup>343</sup> *Id.*

<sup>344</sup> *Barnhill*, 931 F.2d at 694 n.3.

<sup>345</sup> *Global Distribution Network v. Star Expansion*, 949 F.2d 910 (7th Cir. 1991).

<sup>346</sup> An exception would exist under § 547(e) for checks honored during the preference period but within ten days of (prepetition) receipt.

<sup>347</sup> *Global Distribution*, 949 F.2d at 914.

perfected, it may be subordinated to the interests of other creditors.<sup>348</sup> Further, as had the Sixth Circuit in *Belknap*, the Seventh Circuit saw no reason to differentiate the meaning of "transfer" under § 547(b) from its meaning under § 547(c), because the Code's own definitions of "transfer" in §§ 101(54) and 547(e) did not recognize such a distinction.<sup>349</sup>

The Seventh Circuit also attacked the rationales by which the Tenth Circuit had supported the "date of honor" rule. Though a transfer may be more objectively indicated by bank records than by creditors' recollections of when they received a check, even the date stamped on a check by the drawee bank may be misleading: the U.C.C. allows the bank to dishonor a check stamped "paid" until midnight of the "banking day" (which, under local law, might not include Saturdays) after its receipt.<sup>350</sup>

Next, the court questioned the degree to which the "date of honor" rule could conform to the U.C.C., because state law on perfection would be applicable only to determining the date of absolute transfer (*i.e.*, the date of honor), and not of the earlier date of conditional transfer (the date of delivery). Also, the Code's goal of preventing inequitable distribution among creditors did not favor a ninety-day period over an eighty-day or 100-day one, or necessarily interpret "transfer" as delivery: "Far more important . . . is that the rule be simple and frustrate me-first strategies by creditors."<sup>351</sup>

Finally, the Seventh Circuit embraced precisely the argument that the Tenth Circuit had rejected: that § 547(e)'s "jar-ring" reference to "perfection" in fact referred to the honoring of the check by the drawee bank, after which no superior judicial lien could attach to these assets of the debtor.<sup>352</sup> This court of appeals observed that "[a]lthough 'perfection' in the U.C.C. refers to security interests, the term is not so limited in § 547(e)," which itself was found to be only a modification of § 96(a)(2) of the Bankruptcy Act.<sup>353</sup>

## 2. Resolving the Limits of "Plain Meaning"?

In a majority opinion written by Chief Justice Rehnquist, the Court affirmed the Tenth Circuit's decision to apply the "date of

---

<sup>348</sup> *Id.* at 912-14.

<sup>349</sup> *Id.* at 913.

<sup>350</sup> *Id.* at 911-12.

<sup>351</sup> *Id.* at 912.

<sup>352</sup> *Id.* at 913.

<sup>353</sup> *Id.*

honor" rule. While it recognized that the delivery of a check transferred to the creditor a conditional right in the debtor's bank account, the Court held that this right did not amount to a conditional right to "property or an interest in property" of the debtor under § 101(54) of the Code.

Between the check's delivery and its presentment, the account might be closed by the debtor or attached by another creditor, or the bank might mistakenly refuse to honor the check. During this period, the creditor would have only a contingent right, under U.C.C. § 3-122(3),<sup>354</sup> to sue the debtor for payment if the check were dishonored. To the Court, treating this "nebulous" right "as a 'conditional transfer' of the property would accomplish a near-limitless expansion of the term 'conditional.' In the absence of any right against the bank or the account, we think the fairer description is that petitioner had received no interest in debtor's property, not that his interest was 'conditional.'"<sup>355</sup>

Rather, the Court found that the transfer, or § 101(54)'s "mode, direct or indirect. . . of disposing of property or an interest in property," had been effected only by the drawee bank's honoring the check and subtracting that amount from the debtor's claim against the funds held by the bank for his account. In addition, the Court held that the "date of honor" rule was in accord with the Code's § 547(e)(2)(A), which provides that a transfer occurs at the time that the transfer "takes effect between the transferor and the transferee." Since the debtor could stop payment on the check until the moment the check was honored, it was only at that moment that the transfer to the creditor would be deemed to have taken place.

For three reasons, the Court found the legislative history of § 547(c) of little relevance. First, the majority flatly deemed § 547(b) clear enough not to require the Court to examine the provision's legislative history.<sup>356</sup> Second, even if the statutory history were relevant, the available passages concerned the "specialized purpose" of § 547(c), not of § 547(b).<sup>357</sup> Finally, the

---

<sup>354</sup> U.C.C. § 3-122(3) provides that "[a] cause of action against a drawer of a draft or an indorser of any instrument accrues upon demand following dishonor of the instrument. Notice of dishonor is a demand."

<sup>355</sup> *Barnhill*, 112 S. Ct. at 1391.

<sup>356</sup> *Id.* at 1391. "[A]ppeals to statutory history are well-taken only to resolve 'statutory ambiguity.' We do not think this is such a case." *Id.* (citing *Toibb*, 111 S. Ct. at 2200).

<sup>357</sup> *Id.*



Court noted that in *Wolas*,<sup>358</sup> it had dissolved any distinction between "long-term" and "short-term" debts, which the cited portions of the legislative history had addressed. Thus, the Court held in *Barnhill* that "it would clearly be inappropriate to extrapolate from that history for purposes of interpreting the scope of § 547(b) and § 101(54)."<sup>359</sup>

In a dissent joined by Justice Blackmun, Justice Stevens cited "established practices in the business community"<sup>360</sup> as supporting the conclusion that the delivery of the check, and the concomitant conditional transfer of the right to funds in the debtor's bank account, did constitute a "transfer" under § 101(54). Under § 547(e)(2), the transfer would occur on the date of delivery, on the condition that the transfer was perfected within ten days. If the check was not honored within ten days, the transfer would be deemed to occur on the date of honor.

The dissent resolved the question of the "perfection" of transfers in the context of the Code by noting that the term has a "broader meaning" in § 547(e) than in the U.C.C.<sup>361</sup> Under that provision, perfection of a transfer by check occurs on the date of honor, after which date no party can acquire a judicial lien that takes priority over the creditor's interest in the transferred funds.

Citing the Sixth Circuit's analysis in *Belknap*, the dissent noted the courts of appeals' decisions and the legislative history supporting the "date of delivery" rule in the context of transfers by check. In connection with the definition of "transfer," Justice Stevens observed that "[n]ormally, we assume that the same terms have the same meaning in different sections of the same statute. That rule is not inexorable, but nothing in the structure or purpose of § 547(b) and § 547(c) suggests a reason for interpreting these adjacent subsections differently."<sup>362</sup>

Beyond its immediate practical implications,<sup>363</sup> *Barnhill* illus-

---

<sup>358</sup> See *supra* notes 146-70 and accompanying text for a detailed discussion of *Wolas*.

<sup>359</sup> *Barnhill*, 112 S. Ct. at 1391 n.9. The Court declined to address whether the "date of delivery" rule applied to check payments under § 547(c).

<sup>360</sup> *Id.* at 1392 (Stevens, J., dissenting).

<sup>361</sup> *Id.* at 1393 (Stevens, J., dissenting).

<sup>362</sup> *Id.* at 1393-94 (Stevens, J., dissenting) (citation omitted).

<sup>363</sup> *Barnhill* encourages creditors to endorse and present as soon as possible to the drawee banks all checks received from troubled creditors. While a "date of delivery" rule would take the timing of a transfer by check out of a creditor's hands (except to the extent that the payee could influence a teetering debtor to deliver checks more promptly), under the "date of honor" rule endorsed by the Supreme

trated the continuing indeterminacy in the Court's methods of statutory interpretation. First, the proper justification for interpreting the same word differently in separate subsections of the Code remained in the eye of the beholder. Justice Scalia, who in his *Dewsnup* dissent had excoriated the Court's "one-subsection-at-a-time approach to statutory exegesis,"<sup>364</sup> agreed with the *Barnhill* majority that the legislative history of § 547(b) could not be extended to the "specialized purpose" of § 547(c). Yet it was Justice Stevens, late of the *Dewsnup* majority, who here decried the different meaning of "transfer" attributed to each of these subsections.<sup>365</sup>

Second, while *Dewsnup* had resisted readings of the Code that would alter the expectations of the parties, the *Barnhill* majority was faulted by the dissent for rejecting a rule "consistent with . . . traditional commercial practice [and] the treatment of checks in tax law."<sup>366</sup> Not only had the majority failed to address these considerations directly, but the linchpin of its logic — the conclusion that the transfer of a check did not constitute a "conditional transfer" of the underlying funds — would directly contradict the expectations of many commercial debtors, payees, and their counsel. Indeed, the majority had explicitly acknowledged the Code's "expansive" definition of "transfer."<sup>367</sup>

Finally, as its sole support for this restriction, the Court offered only its general reluctance to foster "a near-limitless expansion of the term 'conditional.'" Those seeking a firmer analytical base for *Barnhill* could only acknowledge, as did Justice Scalia in

---

Court the behavior of the creditor itself affects the timing of the transfer for preference avoidance purposes.

In this connection, the thirty-day period identified by U.C.C. § 3-503(2)(a) as a "reasonable time for presentment" of "an uncertified check which is drawn and payable within the United States and which is not a draft drawn by a bank" might be seen as an outer limit for presentment; a prudent creditor will have presented the check as soon as is practicable.

The thirty-day limit remains relevant if the creditor anticipates arguing that, under § 547(c), the transfer is not a preference. (It should be remembered that U.C.C. § 3-511(2)(a) allows the debtor to consent, "expressly or by implication," to a longer period for the initiation of collection.) Similarly, a payee should not diminish its efforts to ensure, and to record, its prompt receipt of the debtor's checks, as the "date of delivery" rule still applies in those circuits that have considered § 547(c) preference calculations.

<sup>364</sup> *Dewsnup*, 112 S. Ct. at 781. See *supra* notes 250-73 and accompanying text for commentary on Justice Scalia's vigorous dissent in *Dewsnup*.

<sup>365</sup> See *supra* note 363.

<sup>366</sup> *Id.* at 1392 (Stevens, J., dissenting).

<sup>367</sup> *Id.* at 1390.

*Dewsnup*,<sup>368</sup> that "a bankruptcy law has little to do with natural justice."

I. *Patterson v. Shumate*<sup>369</sup>

In *Patterson*, the Court unanimously held that creditors cannot reach individual debtors' interests in certain pension plans. Applying the "plain meaning" doctrine to interpret an ambiguous section of the Code, the Court resolved a 4-4 split among the United States Circuit Courts of Appeals concerning the status of the Employee Retirement Income Security Act of 1974 ("ERISA")<sup>370</sup> as "applicable nonbankruptcy law."

1. Background

In keeping with the Code's policy of providing a "fresh start," the debtor may separate from the bankruptcy estate created under § 541(a) of the Code<sup>371</sup> assets that are either "excluded"<sup>372</sup> or "exempted"<sup>373</sup> from the estate. An excluded asset never enters the bankruptcy estate. The individual debtor can argue in the alternative that the asset is exempted from the bankruptcy estate under a specific exception contained either in the Code or in the relevant federal, state or local law.

The *exclusion* of a debtor's interest in a pension plan is governed by § 541(c)(2), which provides that "a restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under *applicable nonbankruptcy law* is enforceable" in bankruptcy proceedings.<sup>374</sup> The *exemption* of an individual debtor's interest in a pension plan is governed by § 522. Section 522(b)(1) provides that, in those states that have not precluded the "federal exemptions" of § 522(d), debtors may avail them-

---

<sup>368</sup> *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting).

<sup>369</sup> 112 S. Ct. 2242 (1992). The following discussion has been adapted with permission from that presented in Walter A. Effross, *Debtor's Interest in ERISA Plans Exempt from Estate*, 131 N.J.L.J. 759 (1992).

<sup>370</sup> PUB. L. No. 93-406, 88 Stat. 898 (1974). ERISA, which protects employees' retirement income held in a fund created or maintained by their employer, is codified at 29 U.S.C. §§ 1001-1144, and in several sections of the Internal Revenue Code, 26 U.S.C. § 1 *et seq.*

<sup>371</sup> See *supra* note 277 and accompanying text.

<sup>372</sup> For a more extensive analysis of exclusion issues and of the circuit courts' 4-4 division on this issue before the Supreme Court's decision in *Shumate*, see Walter A. Effross, *ERISA Meets Title 11: The Looking-Glass Logic of Pension Benefits in Bankruptcy*, in EMERGING BANKRUPTCY ISSUES OF THE 90's 181-244 (New Jersey Institute for Continuing Legal Education Seminar Materials, 1992).

<sup>373</sup> See *supra* notes 278-79 and accompanying text.

<sup>374</sup> 11 U.S.C. § 541(c)(2) (1988) (emphases added).

selves of any or all of those eleven specific exemptions.<sup>375</sup> One of the federal exemptions, § 522(d)(10)(E), exempts the debtor's right to receive "a payment under a stock bonus, pension, profit-sharing, annuity, or similar plan or contract on account of illness, disability, death, age or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor."<sup>376</sup> As an alternative to the federal exemptions, § 522(b)(2)(A) allows individual debtors to claim as exempt any property that is exempt from attachment by creditors under applicable state or local law or under any federal law other than the federal exemptions.<sup>377</sup>

Thus, a debtor's interest in a pension plan might be: (a) excluded from the bankruptcy estate under applicable nonbankruptcy law; (b) exempted from the estate under a specific federal exemption, to the extent necessary for the support of the debtor and her dependents; (c) exempted under applicable state or local law (for example, if the plan qualifies as a spendthrift trust<sup>378</sup>); or (d) exempted from federal law other than the federal exemptions. At the time that Shumate began his litigation, the Supreme Court had not ruled on whether ERISA qualified either as "applicable nonbankruptcy law" under (a) or as relevant federal law under (d).

When Coleman Furniture ("Coleman") filed a chapter 11 petition for reorganization in 1982, Joseph B. Shumate Jr., Coleman's president and the chairman of its board of directors, had been with the company for more than thirty years. Shumate's

---

<sup>375</sup> See *supra* notes 278-80 and accompanying text. The federal exemptions are operative in the District of New Jersey.

<sup>376</sup> 11 U.S.C. § 522(d)(1)(E) (1988).

<sup>377</sup> See *supra* note 277 and accompanying text.

<sup>378</sup> On July 9, 1993, the New Jersey Assembly enacted a bill, effective immediately, rendering exempt from creditors certain pension or profit-sharing assets and distributions. P.L. 1992, Chapter 177 (Assembly Committee Substitute for 1992 Assembly Nos. 288 and 1462).

The Act revised N.J. STAT. ANN. 25:2-1 to render "void as against creditors" "every deed of gift and every conveyance, transfer and assignment of goods, chattels or things in action, made in trust for the use of the person making the same." Two sets of exceptions remain to this general rule. First, creditors can attack transfers as preferences or fraudulent conveyances made in violation of the Uniform Fraudulent Transfer Act, N.J. STAT. ANN. 25:2-20 *et. seq.*, or any other state or federal law. Second, the statute will not shelter the assets of a qualifying trust from claims made under any order for child support or spousal support or from the claims of an alternate payee, under a qualified domestic relations order ("QDRO"). (However, the interest of any alternate payee under a QDRO will be exempt from all claims of any creditor of the alternate payee.)

interest in Coleman's pension plan (the "plan"), which had almost 400 participants and which was funded solely by Coleman's contributions, was estimated at \$250,000.<sup>379</sup>

These contributions were tax-deductible to Coleman, and, with their earnings, were taxed as income to plan participants only on their withdrawal of the funds. The plan's favorable tax treatment resulted from its being "ERISA-qualified," that is, meeting various requirements of that statute.<sup>380</sup> Notably, by prohibiting participants from assigning or alienating their benefits, the plan complied with 29 U.S.C. § 1056(d)(1) of ERISA<sup>381</sup> and with a counterpart provision of the Internal Revenue Code ("IRC"), 26 U.S.C. § 401(a)(13).<sup>382</sup> In these respects, the plan resembled a spendthrift trust, whose corpus and benefits many states protect from a beneficiary's creditors if the beneficiary (1) is not the creator of the trust; (2) has no control over the trust funds; and (3) cannot voluntarily or involuntarily control his interest in the trust.<sup>383</sup>

In 1984, Shumate filed a chapter 13 petition, which, like Coleman's, was converted to a chapter 7 liquidation. All of the Coleman pension claims except Shumate's were paid in full; Shumate and his trustee in bankruptcy, John R. Patterson, each asserted the right to recover Shumate's interest in the plan from Coleman's bankruptcy trustee, Roy V. Creasey. Because of the procedural posture of the parties in related litigation, the district court assumed jurisdiction over the bankruptcy court proceedings with regard to the disposition of Shumate's interest in the plan.<sup>384</sup>

---

<sup>379</sup> *Patterson*, 112 S. Ct. at 2245.

<sup>380</sup> *Id.*

<sup>381</sup> 29 U.S.C. § 1056(d)(1) provides that "[e]ach pension plan shall provide that the benefits provided under the plan may not be assigned or alienated."

<sup>382</sup> 26 U.S.C. § 401(a)(13) (1988) provides that "[a] trust shall not constitute a qualified trust under this section unless the plan of which such a trust is a part provides that benefits provided under the plan may not be assigned or alienated."

The terms "assignment" and "alienation" include:

- (i) Any arrangement providing for the payment to the employer of plan benefits which otherwise would be due the participant under the plan, and
- (ii) Any direct or indirect arrangement (whether revocable or irrevocable) whereby a party acquires from a participant or beneficiary a right or interest enforceable against the plan in, or to, all or part of a plan benefit payment which is, or may become, payable to the participant or beneficiary.

Treas. Reg. § 1.401(a)-(13)(c).

<sup>383</sup> See, e.g., 119 A.L.R. 19 (regarding "Validity of Spendthrift Trusts").

<sup>384</sup> *Patterson*, 112 S. Ct. at 2245.

The district court denied Shumate's motion to compel his chapter 7 trustee to turn over Shumate's interest in the plan. First, the court analyzed whether this asset could be *excluded* from Shumate's estate under the "applicable non-bankruptcy law" referred to in § 541(c)(2).<sup>385</sup> Since the Fourth Circuit had construed that phrase to refer only to state law,<sup>386</sup> the district court restricted its examination to whether the plan was a valid spendthrift trust under Virginia law.<sup>387</sup>

The court observed that Shumate's voting control over his own Coleman stock, and his right to vote other stock held in a voting trust, had enabled him to terminate the plan at any time under its terms and to opt for a lump sum of his own interest plus the reversion of excess pension funds as a dividend to himself. Shumate had "exercised such power over the . . . pension trust that he could control it to suit his needs. Such dominion is inconsistent with the notion of spendthrift trusts."<sup>388</sup> Thus, Shumate could not exclude from his bankruptcy estate his interest in the plan.

Nor could this interest be *exempted* from the estate. Because Virginia did not give effect to the federal exemptions of § 522(d), the specific exemption of § 522(d)(10)(e) would not apply.<sup>389</sup> Shumate nonetheless argued for exemption under § 522(b)(2)(a), contending that 29 U.S.C. § 1056(d) of ERISA would prevent any assignment of his interest in the plan, even to Coleman's bankruptcy trustee. However, the court noted that the House and Senate reports on that provision of the Code did not refer to ERISA.<sup>390</sup> Indeed, the federal laws listed in those reports were related to benefits granted not by private employers, but by the federal government itself (*e.g.*, Social Security payments, veterans' benefits) or by federally protected industries (*e.g.*, the Foreign Service, railroads).<sup>391</sup>

Before hearing Shumate's appeal, the Fourth Circuit had reversed its earlier position on the construction of "applicable bankruptcy law": for purposes of *exclusion*, this reference would

---

<sup>385</sup> *Creasey v. Coleman Furniture Corp.*, 83 B.R. 404 (W.D. Va. 1988).

<sup>386</sup> *McLean v. Central States, S. & S. Areas Pension Fund*, 762 F.2d 1204 (4th Cir. 1985) (examining, in determining whether debtor's interest in trust fund is property of estate, enforceability under state law of pension trust agreement's restrictions on transfer).

<sup>387</sup> *Creasey*, 83 B.R. at 406.

<sup>388</sup> *Id.* at 408.

<sup>389</sup> *Id.* at 409 (citing VA. CODE ANN. § 34-31 (Michie 1985)).

<sup>390</sup> *Id.* at 410.

<sup>391</sup> *Id.*

now be taken to include ERISA.<sup>392</sup> The court of appeals thus found that, despite Shumate's control over the disposition of plan assets, the only relevant inquiry was whether the plan was ERISA-qualified — that is, whether it contained a nonalienation provision.<sup>393</sup> The approach would harmonize ERISA's policy of protecting the pension benefits of employees with the Code's "fresh-start" policy of excepting certain assets from the bankruptcy estate.<sup>394</sup> Reversing the district court, the Fourth Circuit upheld the exclusion from Shumate's estate of his interest in the plan. Since its resolution of this issue was dispositive, the appeals court declined to address whether Shumate's interest in the plan could be exempted from the estate under § 522(b).<sup>395</sup>

Although the Fourth Circuit was the first court of appeals to adopt this position, it would be joined by the Third, Sixth and Tenth Circuits by the time the issue reached the Supreme Court.<sup>396</sup> Among the arguments cited by these courts of appeals were: (i) that the phrase should be read literally;<sup>397</sup> (ii) that the same phrase is used elsewhere in the Code to refer both to state and to federal law;<sup>398</sup> and (iii) that the Code specifies where only state law is intended.<sup>399</sup> These four circuits also held that an examination of the legislative history was, alternatively, inappropriate (under *Toibb*, because there was no ambiguity in § 541(c)(2));<sup>400</sup> irrelevant, because the pension plans at issue in these cases were unlike those addressed by state spendthrift trust law;<sup>401</sup> and, finally, inconclusive.<sup>402</sup> Moreover, the exclusion of the debtor's interest in his ERISA-qualified plan would: give full force to both ERISA and the Code;<sup>403</sup> further ERISA's broader

---

<sup>392</sup> *Anderson v. Raine (In re Moore)*, 907 F.2d 1476 (4th Cir. 1990).

<sup>393</sup> *Shumate v. Patterson*, 943 F.2d 362 (4th Cir. 1991).

<sup>394</sup> *Id.* at 365.

<sup>395</sup> *Id.*

<sup>396</sup> *Gladwell v. Harline (In re Harline)*, 950 F.2d 669 (10th Cir. 1991), *cert. denied*, 112 S. Ct. 2991 (1992); *Velis v. Kardanis (In re Velis)*, 949 F.2d 78 (3d Cir. 1991); *Forbes v. Lucas (In re Lucas)*, 924 F.2d 597 (6th Cir.), *cert. denied sub nom. Forbes v. Holiday Corp. Sav. and Retirement Plan*, 111 S. Ct. 2275 (1991).

<sup>397</sup> *Harline*, 950 F.2d at 674; *Velis*, 949 F.2d at 81; *Lucas*, 924 F.2d at 601; *Moore*, 907 F.2d at 1477.

<sup>398</sup> *Harline*, 950 F.2d at 674; *Velis*, 949 F.2d at 81; *Lucas*, 924 F.2d at 601; *Moore*, 907 F.2d at 1477-78.

<sup>399</sup> *Harline*, 950 F.2d at 674; *Velis*, 949 F.2d at 81; *Lucas*, 924 F.2d at 601-02; *Moore*, 907 F.2d at 1478.

<sup>400</sup> *Harline*, 950 F.2d at 674; *Lucas*, 924 F.2d at 601; *Moore*, 907 F.2d at 1478.

<sup>401</sup> *Harline*, 950 F.2d at 674.

<sup>402</sup> *Lucas*, 924 F.2d at 602; *Moore*, 907 F.2d at 1479.

<sup>403</sup> *Harline*, 950 F.2d at 675; *Patterson*, 943 F.2d at 365; *Lucas*, 924 F.2d at 603; *Moore*, 907 F.2d at 1480.

purpose of ensuring uniform treatment throughout the country;<sup>404</sup> and prevent being disqualified from the entire plan from tax-exempt status in the event that a single bankrupt participant's interest in the plan was turned over to his bankruptcy trustee.<sup>405</sup> Nor did these courts find § 541(c)(2) to be redundant with § 522.<sup>406</sup>

Four other circuit courts of appeals would reach the opposite conclusion.<sup>407</sup> The arguments against exclusion included: (i) that § 522(d)(10)(E)'s specific exemption of income from qualified plans indicated that Congress intended the debtor's right to payment from spendthrift trusts to be included in the original bankruptcy estate;<sup>408</sup> (ii) that the legislative history indicated that ERISA-qualified plans were not intended to be exempted from the estate under § 522;<sup>409</sup> and (iii) that, while ERISA might preempt state law, it was subordinate to the Code's policy of distributing the debtor's property among creditors.<sup>410</sup>

## 2. "Plain Meaning" Triumphant

The Supreme Court granted certiorari to examine whether for purposes of exclusion ERISA constituted "applicable nonbankruptcy law."<sup>411</sup> Justice Blackmun's "plain meaning" analysis quickly dispatched the problems raised by *Patterson*: indeed, the first sentence of the Court's analysis indicated that "In

---

<sup>404</sup> *Lucas*, 924 F.2d at 603; *Moore*, 907 F.2d at 1480.

<sup>405</sup> *Moore*, 907 F.2d at 1480.

<sup>406</sup> *Velis*, 949 F.2d at 81-82 (Section 522 deals with distributions made from pension plan and distributions that debtor has present and immediate right to receive; even if pension plan assets in hands of trustee are beyond reach of creditors because not part of debtor's estate under § 541(c)(2), distributions made from plan to debtor would not enjoy such protection, in absence of exemption under § 522(d)(10)(E)).

<sup>407</sup> *Daniel v. Security Pacific Nat'l Bank* (*In re Daniel*), 771 F.2d 1352 (9th Cir. 1985), *cert. denied*, 474 U.S. 1016 (1986); *Lichstrahl v. Bankers Trust* (*In re Lichstrahl*), 750 F.2d 2488 (11th Cir. 1985); *Samore v. Graham* (*In re Graham*), 726 F.2d 1268 (8th Cir. 1984); *Goff v. Taylor* (*In re Goff*), 706 F.2d 574 (5th Cir. 1983). These circuits would later be joined by the Ninth Circuit. See *Reed v. Drummond* (*In re Reed*), 951 F.2d 1046 (9th Cir. 1991), *cert. granted and judgment vacated*, 113 S. Ct. 314 (1992), opinion withdrawn and superseded, 985 F.2d 1026 (9th Cir. 1993); *Pitrat v. Garlikov*, 947 F.2d 419 (9th Cir. 1991), *reversed*, 992 F.2d 224 (9th Cir. 1993) (reversing prior opinion in light of Supreme Court's *Patterson* decision); *John Hancock Mutual Life Insur. Co. v. Watson* (*In re Kincaid*), 917 F.2d 1162 (9th Cir. 1990).

<sup>408</sup> *Graham*, 726 F.2d at 1272.

<sup>409</sup> *Daniel*, 771 F.2d at 1360-61; *Lichstrahl*, 750 F.2d at 1491; *Graham*, 726 F.2d at 1273-74; *Goff*, 706 F.2d at 583-85.

<sup>410</sup> *Goff*, 706 F.2d at 588-89.

<sup>411</sup> *Patterson v. Shumate*, 112 S. Ct. 2242 (1992).



our view, the plain language of the Bankruptcy Code and ERISA is our determinant."<sup>412</sup> The "natural reading" of § 541(c)(2)<sup>413</sup> indicated that "applicable nonbankruptcy law" "encompasses any relevant nonbankruptcy law, including federal law such as ERISA. We must enforce the statute according to its terms."<sup>414</sup> Moreover, other provisions of the Code demonstrated that Congress, when it desired to do so, "knew how to restrict the scope of applicable law to 'state law' and did so with some frequency."<sup>415</sup> Finally, the Court found that ERISA's restriction on assignment or alienation of the benefits of a qualified plan fell within § 541(c)'s "restriction on the transfer" of a debtor's "beneficial interest" in the trust.<sup>416</sup>

This straightforward application of the plain-meaning doctrine generally dispensed with consideration of the provision's legislative history.<sup>417</sup> Nonetheless, the Court observed that what "meager excerpts" could be gleaned from the House and Senate Reports accompanying the Bankruptcy Reform Act of 1978 indicated only that the exclusion was intended to include, but not that it was limited to, spendthrift trusts.<sup>418</sup> In short, the Fourth Circuit and its supporters, "by ignoring the plain language of § 541(c)(2) and relying on isolated excerpts from the legislative history[,] have misconceived the appropriate analytical task."<sup>419</sup>

The trustee argued that excluding debtors' entire interests in ERISA-qualified plans would directly contradict § 522(d)(10)(E)'s limited federal exemption for such interests. However, the Court found that its broad interpretation of § 541(c)(2) had not eviscerated this exemption, which also covered interests in plans that were *not* excludable under a broad reading of "applicable nonbankruptcy law," including individual retirement accounts (IRA's) and pension plans established by

---

<sup>412</sup> *Patterson*, 112 S. Ct. at 2246 (citing *Toibb*, 111 S. Ct. at 2199).

<sup>413</sup> *Id.*

<sup>414</sup> *Id.* at 2247 (citing *Ron Pair*, 489 U.S. at 241). Indeed, lower courts had construed the phrase "applicable nonbankruptcy law" in other sections of the Code to include federal law. *Id.* n.2.

<sup>415</sup> *Id.* (citing, *inter alia*, 11 U.S.C. § 522(b)(1) (providing exemptions tracking "the State law that is applicable to the debtor") and 11 U.S.C. § 523(a)(5) (determining "in accordance with State or territorial law" the nondischargeability of debt for alimony, maintenance or support)).

<sup>416</sup> *Id.*

<sup>417</sup> *Id.* at 2248. "[T]he clarity of the statutory language at issue in this case obviates the need for any . . . inquiry [into legislative history]." *Id.* (citing *Toibb*, 111 S. Ct. at 2200; *Ron Pair*, 489 U.S. at 241).

<sup>418</sup> *Id.*

<sup>419</sup> *Id.* n.4.

churches and by governmental agencies.<sup>420</sup>

Finally, the Court cited legislative and social policies in support of its construction of the Code. The exclusion from the debtor's estate of his interest in an ERISA-qualified plan "ensures that the treatment of pension benefits will not vary based on the beneficiary's bankruptcy status": that is, lenders unable to reach such interests outside of the bankruptcy process would have no additional incentive to file involuntary petitions against borrowers.<sup>421</sup> Nor should ERISA's protection of pension benefits be withheld from debtors. Moreover, the Court's broad reading of "applicable non-bankruptcy law" to incorporate ERISA would promote nationwide uniformity in the bankruptcy treatment of pension benefits, rather than leaving them to "the vagaries of state spendthrift trust law."<sup>422</sup>

Yet the majority's application of the "plain meaning" rule did not satisfy Justice Scalia. Just as his ninety-nine-word concurrence in *Wolas* had reproached the "legal culture" for encouraging litigation that "the plain text of the statute should have made . . . unnecessary and unmaintainable,"<sup>423</sup> his two-paragraph con-

---

<sup>420</sup> *Id.* at 2248-49.

<sup>421</sup> *Id.*

<sup>422</sup> *Id.* at 2250. *Patterson's* pro-debtor stance was reinforced by the Court's denial of certiorari in *Farm Services v. Morter*, 937 F.2d 354 (7th Cir. 1991), *cert. denied*, 112 S. Ct. 2991 (1992), in which the Seventh Circuit excluded a debtor's interest in a non-traditional pension plan. *Morter* held that, so long as the retirement plan did not allow the beneficiary and his creditors to reach the plan corpus, the plan would qualify as a spendthrift trust under state law, and thus could be excluded under § 541(c)(2). *Morter*, 937 F.2d at 358. "The fact that the plan administrators might have to dip into the fund to make up any shortfall [in distributions] is not as important to the analysis as the extent of access to the plan and who has that access." *Id.*

Although it reconciled the most serious conflict between ERISA and bankruptcy law, *Patterson* left several other issues unresolved. For instance, the Court did not address whether the federal exemption of § 522(d)(10)(E) applies to the entire undistributed corpus of a pension trust or only to distributions that a debtor has an immediate and present right to receive. *Patterson*, 112 S. Ct. at 2249 n.5. Nor did the Court decide whether ERISA constitutes relevant federal law for exemptions under § 522(b)(2)(A). *Id.* at 2250.

In addition, *Patterson* noted without comment the Internal Revenue Service's position that the conveyance to a debtor's bankruptcy trustee of the debtor's interest in a pension plan would revoke the plan's ERISA-qualified status, and thus extinguish the tax benefits to employers and participants. *Id.* at 2247 n.3. In a recent letter ruling, the IRS had itself endorsed the exclusion of such interests under § 541(c)(2), but had nonetheless approved a method of protecting the plan's ERISA-qualified status: subject to IRS approval, the plan trustee could forward to the bankruptcy trustee a loan check and hardship withdrawal check payable to the debtor, who would endorse the checks to the bankruptcy trustee in the bankruptcy trustee's presence. Priv. Ltr. Rul. 91-09-051 (Dec. 5, 1990).

<sup>423</sup> *Union Bank v. Wolas*, 112 S. Ct. 527, 534 (1991) (Scalia, J., concurring).

currence in *Patterson* found "mystifying" the ability of three Courts of Appeals to interpret "applicable nonbankruptcy law" as excluding federal law.<sup>424</sup> To this Justice, "the phenomenon calls into question whether our legal culture has so far departed from attention to text, or is so lacking in agreed-upon methodology for creating and interpreting text, that it any longer makes sense to talk of 'a government of laws, not of men.'"<sup>425</sup>

Justice Scalia was mollified, however, by the majority's emphasis on the connotations of "state law" and "applicable non-bankruptcy law" elsewhere in the Code: he perceived this approach as a harbinger of the Court's return to the proposition that phrases should be interpreted uniformly across the provisions of the Code. Although he had castigated the majority in *Dewsnup* for its "one-subsection-at-a-time approach to statutory exegesis,"<sup>426</sup> in *Patterson* this Justice concluded his dissent with the presumption that "in our search for a neutral and rational interpretive methodology we have now come to rest, so that the symbol of our profession may remain the scales, not the see-saw."<sup>427</sup>

This interpretation, though, may have been premature. First, although the *Patterson* majority noted that its interpretation of "applicable non-bankruptcy law" was consonant with lower court opinions construing that phrase elsewhere in the Code, it carefully refrained from commenting on "the correctness of [those] decisions."<sup>428</sup> Second, the *Dewsnup* majority, which explicitly limited its holding to the situation then before the Court,<sup>429</sup> involved an ambiguity more complex than that of *Shumate*: indeed, one whose resolution required a review of legislative history and pre-Code practice. The Code's "plain meaning" approach might not be stepping off the Scalia see-saw so quickly!

*J. Pioneer Investment Services v. Brunswick Associates Limited Partnership*<sup>430</sup>

The Court's next venture into the "plain meaning" of the Code concerned the "excusable neglect" exception to the Rule

---

<sup>424</sup> *Patterson*, 112 S. Ct. at 2250 (Scalia, J., concurring).

<sup>425</sup> *Id.* at 2250-51 (Scalia, J., concurring).

<sup>426</sup> See *supra* notes 250-73 and accompanying text for a discussion of Justice Scalia's dissenting opinion in *Dewsnup*.

<sup>427</sup> *Patterson*, 112 S. Ct. at 2251 (Scalia, J., concurring).

<sup>428</sup> *Id.* at 2247 n.2.

<sup>429</sup> *Dewsnup v. Timm*, 112 S. Ct. 773, 778 (1992).

<sup>430</sup> 113 S. Ct. 1489 (1993).

of Bankruptcy Procedure that prohibited the late filing of a proof of claim. Just as the Court had in *Dewsnup* construed the phrase "allowed secured claim" "term-by-term to refer to any claim that is, first, allowed, and, second, secured,"<sup>431</sup> so did the majority here endorse a collegiate dictionary's definition of "neglect," as modified by the Court's construction of "excusable." Yet, the dissent, adopting a legal dictionary's strict interpretation of "excusable neglect" as an indivisible term of art, rejected the Court's multifactored approach to the equities of permitting an untimely action.

### 1. Background

Pioneer Investment Services ("Pioneer") filed a chapter 11 petition on April 12, 1989.<sup>432</sup> The debtor's list of its twenty largest unsecured creditors included plaintiffs Brunswick Associates Limited Partnership ("Brunswick"), Clinton Associates Limited Partnership ("Clinton"), and West Knoxville Associates Limited Partnership ("W.Knoxville"), but not plaintiff Ft. Oglethorpe Associates Limited Partnership ("Ft. Oglethorpe").<sup>433</sup>

The following day, the bankruptcy court clerk's office mailed a Notice for Meeting of Creditors that scheduled for May 5, 1989 the creditors' meeting called for by § 341(a) of the Code.<sup>434</sup> The same notice fixed August 3, 1989 as the bar date for unsecured creditors to file proofs of claim, and warned that "[y]ou must file a proof of claim if your claim is scheduled as disputed, contingent or unliquidated, is unlisted or you do not agree with the amount. See 11 U.S.C. § 1111 & Bankruptcy Rule 3003. Bar date is August 3, 1989."<sup>435</sup>

---

<sup>431</sup> *Dewsnup*, 112 S. Ct. at 777.

<sup>432</sup> *Brunswick Associates Limited Partnership v. Pioneer Investment Services Company* (*In re Pioneer Investment Services Company*), 943 F.2d 673, 675 (6th Cir. 1991).

<sup>433</sup> *Id.*

<sup>434</sup> *Id.* at 674-75. Section 341(a) provides that "[w]ithin a reasonable time after the order for relief in a case under [title 11], the United States trustee shall convene and preside at a meeting of creditors." Section 343 requires the debtor to appear at this meeting to submit to examination under oath by "[c]reditors, any indenture trustee, any trustee or examiner in the case, or the United States trustee." 11 U.S.C. § 343 (1988).

<sup>435</sup> *Pioneer Inv.*, 943 F.2d at 675. Section 1111(a) provides that a proof of claim or interest is not deemed filed merely because the debtor has scheduled it as disputed, contingent or unliquidated. 11 U.S.C. § 1111(a) (1988).

Bankruptcy Rule 3003(c)(2) generally requires creditors or equity security holders whose claims or interests are not scheduled or are scheduled as disputed, contingent, or unliquidated to file a proof of claim or interest by the bar date set by the court (or by such later date as shall be set by the court). If a creditor's proof of

The bankruptcy court found that Mark Berlin, an attorney and experienced businessman who was the president not only of Clinton's, W.Knoxville's and Brunswick's general partner, but also of Ft. Oglethorpe's general partner, had received and read this notice, and had appeared at the May 5 meeting of creditors.<sup>436</sup>

Pioneer's statement of affairs and relevant schedules, which the debtor had received an extension of time to file, were filed in May and did not name any of the plaintiffs as a creditor holding contingent, unliquidated or disputed claims. However, on May 25 these documents were subsequently amended to so identify all of the plaintiffs except Ft. Oglethorpe.<sup>437</sup>

In mid-June 1989, the plaintiffs retained an experienced bankruptcy attorney, Marc Richards. Berlin's affidavit suggested that Berlin had provided Richards with a complete copy of the bankruptcy file for the partnerships, including the notice of the bar date. Berlin also stated in his affidavit that he had been advised by Richards that the file did not indicate a bar date and that there was thus no immediate need to file proofs of claim.<sup>438</sup>

The plaintiffs filed their proofs of claim on August 23, 1989, twenty days after the bar date. Accompanying these filings was a motion that the court allow the late filing under Rule 9006(b)(1), as "the result of excusable neglect,"<sup>439</sup> namely, the disarray caused by Richards's withdrawal from his former law firm on July 31, 1989 and his alleged consequent inability to gain access to the case file until mid-August.<sup>440</sup> However, the bankruptcy court interpreted "excusable neglect" narrowly, as encompassing only

---

claim is not timely filed, that creditor "shall not be treated as a creditor with respect to such claim for the purposes of voting and distribution." FED. R. BANKR. P. 3003(c)(2).

<sup>436</sup> *Pioneer Inv.*, 943 F.2d at 675.

<sup>437</sup> *Id.*

<sup>438</sup> *Id.*

<sup>439</sup> *Pioneer Inv.*, 113 S. Ct. at 1492. Rule 9006(b)(1) provides:

Except as provided in paragraphs (2) and (3) of this subdivision, when an act is required or allowed to be done at or within a specified period by these rules or by a notice given thereunder or by order of court, the court for cause shown may at any time in its discretion (1) with or without motion or notice order the period enlarged if the request therefor is made before the expiration of the period originally prescribed or as extended by a previous order or (2) *on motion made after the expiration of the specified period permit the act to be done where the failure to act was the result of excusable neglect.*

FED. R. BANKR. P. 9006(b)(1) (emphasis added).

<sup>440</sup> *Pioneer Inv.*, 113 S. Ct. at 1492-93.

circumstances beyond a party's reasonable control.<sup>441</sup> Since the partnerships had received timely notice of the bar date, they could have complied with this filing deadline.<sup>442</sup>

The district court reversed, citing the Sixth Circuit's more liberal interpretation of "excusable neglect" in the context of other federal rules.<sup>443</sup> To determine this question for purposes of Bankruptcy Rule 9006(b), the district court endorsed the application of the Ninth Circuit's standard, enunciated in *In re Dix*,<sup>444</sup> which entails consideration of:

- (1) whether granting the delay will prejudice the debtor;
- (2) the length of the delay and its impact on efficient court administration;
- (3) whether the delay was beyond the reasonable control of the person whose duty it was to perform;
- (4) whether the creditor acted in good faith; and
- (5) whether clients should be penalized for their counsel's mistake or neglect.<sup>445</sup>

The bankruptcy court was also advised to take into account the factors identified by the Sixth Circuit in *INVST Financial Group, Inc. v. Chem Nuclear Systems, Inc.* concerning "whether the filing of the late proofs of claim resulted from negligence, indifference or culpable conduct on the part of the moving creditors or their counsel."<sup>446</sup>

On remand, the bankruptcy court once again found no "excusable neglect." In an unpublished opinion the court concluded, after applying the *Dix* factors, that: (1) the debtor would not be prejudiced by the late filings; (2) the twenty-day delay in filing would not adversely affect efficient court administration; (3) the delay had not been caused by circumstances outside the creditors' control; (4) the creditors and their counsel had acted in good faith; and (5) because Berlin was a sophisticated businessman and had been aware of the bar date, it was not inappropriate to penalize the creditors for

---

<sup>441</sup> *Pioneer Inv.*, 943 F.2d at 676. The bankruptcy court derived its test from *South Atlantic Financial Corp.*, 767 F.2d 814, 817 (11th Cir. 1985), *cert. denied sub nom. Biscayne 21 Condominium Associates, Inc. v. South Atlantic Financial Corp.*, 475 U.S. 1015 (1986). *Pioneer Inv.*, 113 S. Ct. at 1493.

<sup>442</sup> *Id.*

<sup>443</sup> *Pioneer Inv.*, 943 F.2d at 676-77 (citing *INVST Financial Group, Inc. v. Chem. Nuclear Systems, Inc.*, 815 F.2d 391, 397-400 (6th Cir.), *cert. denied sub nom. Garrett v. INVST Financial Group, Inc.*, 484 U.S. 927 (1987) (determination of "excusable neglect" under Fed. R. Civ. P. 60(b), which concerns motions to set aside default judgments, involves considerations of prejudice to plaintiff, of merits of defendant's defenses, and of any culpable conduct on defendant's part)).

<sup>444</sup> 95 B.R. 134 (BAP 9th Cir. 1988).

<sup>445</sup> *Pioneer Inv.*, 943 F.2d at 677 (quotation omitted).

<sup>446</sup> *INVST Financial Group*, 815 F.2d at 398-99.

the neglect of their counsel.<sup>447</sup> The bankruptcy court also found that Richards had been negligent in failing to meet the bar date, and inferred from this failure the attorney's indifference to the bar date and to the court's orders.<sup>448</sup> The district court affirmed, also in an unpublished opinion.

The Sixth Circuit reversed, holding that in applying the fifth *Dix* factor the bankruptcy court had "inappropriately penalized the plaintiffs for the errors of their counsel."<sup>449</sup> Because Berlin's experience in business did not extend to bankruptcy, his failure to note a brief reference to a "bar date" in a form headed "Notice for Meeting of Creditors," as well as his reliance on Richards's representations concerning the absence of a filing deadline, should not disadvantage the debtors.<sup>450</sup> Indeed, Berlin's specific questions to Richards regarding filing deadlines, and his reliance, as a businessman without expertise in bankruptcy, on Richards's answer, undercut the effect of the only *Dix* factor that might have militated against the creditors—that the late filing had been within their control.<sup>451</sup> The court of appeals held that delayed claims should not be precluded where "the fault is clearly attributable to the attorney, and no prejudice results to the debtor."<sup>452</sup>

## 2. Equitable Excuses and Dueling Dictionaries

In affirming the Sixth Circuit's liberal interpretation of "excusable neglect,"<sup>453</sup> the Supreme Court emphasized the equita-

---

<sup>447</sup> *Pioneer Inv.*, 113 S. Ct. at 1493.

<sup>448</sup> *Pioneer Inv.*, 943 F.2d at 677.

<sup>449</sup> *Id.* The Court recommended that "the *Dix* factors should be applied as aids for case-by-case adjudication, rather than [as] a necessary or complete list of the factors to be considered." *Id.*

<sup>450</sup> *Id.* at 678. After noting the more explicit language recommended by Official Bankruptcy Form 16 for a notice of a proof of claims deadline in a Chapter 11 bankruptcy, the Sixth Circuit observed that

[W]hile we do not suggest that the court was obligated to notify creditors in precisely this form, the comparison between this Form 16 notice and the notice actually given in this case suggests the dramatic ambiguity of the latter. This ambiguity is exacerbated by the fact that the notice was simply and inconspicuously labeled "Bar date" without any reference to its significance as a deadline for the filing of proof of claims.

*Id.*

<sup>451</sup> *Id.*

<sup>452</sup> *Id.*

<sup>453</sup> That reading of Rule 9006(b)(1) had been adopted by the Tenth Circuit in *In re Centric Corp.*, 901 F.2d 1514, 1517-18 (10th Cir.), *cert. denied sub nom. Trustees of Centennial State Carpenters Pension Trust Fund v. Centric Corp.*, 498 U.S. 852 (1990) (approving bankruptcy court's application of five-factor test for "excusable neglect"), but opposed by four other circuit courts. See *In re Davis*, 936 F.2d 771,

ble nature of bankruptcy practice. Justice White observed that, in light of the "range of possible explanations for a party's failure to comply with a court-ordered filing deadline,"<sup>454</sup> Rule 9006(b)(1) should not be construed rigidly, that is, to excuse late filings only if the delay resulted from circumstances beyond a completely blameless party's reasonable control.

On a literal level, the expression "excusable neglect" invited a lenient approach. The Court observed that a collegiate dictionary's definition of "neglect" extended beyond "simple, faultless omissions to act [to include,] more commonly, omissions caused by carelessness."<sup>455</sup> This more compassionate reading was sup-

---

774 (4th Cir. 1991) ("excusable neglect" inquiry centers on whether delay could have been prevented by exercise of diligence by party that failed to perform); *In re Danielson*, 981 F.2d 296, 298 (7th Cir. 1992) ("excusable neglect" is common term in rules of procedure, and Congress regularly holds that the term does not include sloth, ignorance and other negligence); *Hanson v. First Bank of South Dakota, N.A.*, 828 F.2d 1310, 1314-15 (8th Cir. 1987) (conduct does not constitute "excusable neglect" when delay was within creditor's control and could have been prevented by exercise of diligence by party that failed to perform); *In re Analytical Systems, Inc.*, 933 F.2d 939, 942 (11th Cir. 1991) (standard of "excusable neglect" is whether failure to timely perform duty was due to circumstances that were beyond reasonable control of person whose duty it was to perform). *Pioneer Inv.*, 113 S. Ct. at 1494 n.3.

<sup>454</sup> *Id.* The Court explained:

At one end of the spectrum, a party may be prevented from complying by forces beyond its control, such as by an act of God or unforeseeable human intervention. At the other, a party simply may choose to flout a deadline. In between lie cases where a party may choose to miss a deadline for a very good reason, such as to render first aid to an accident victim discovered on the way to the courthouse, as well as cases where a party misses a deadline through inadvertence, miscalculation, or negligence.

*Id.*

<sup>455</sup> *Id.* at 1494-95 (citing WEBSTER'S NINTH NEW COLLEGIATE DICTIONARY 791 (1983) (defining "neglect" as "to give little attention or respect to a matter" or, alternately, "to leave undone or unattended to esp[ecially] through carelessness.")). *Cf.* *Begier v. U.S.*, 496 U.S. 53 (1990) (citing "common meaning of 'withholding,'" as evidenced by entry in *Webster's Third New International Dictionary*, in support of literal interpretation of Internal Revenue Code regarding employers' withholding of wages).

The Court noted the general principle that, in the absence of evidence otherwise, Congress is presumed to have intended words in statutes to carry "their ordinary, contemporary, common meaning." *Id.* at 1495 (quoting *Perrin v. United States*, 444 U.S. 37, 42 (1979) (looking beyond development and evolution of early common-law definition, to ordinary meaning of term, "bribery" at time Congress enacted Travel Act, 18 U.S.C. § 1952)). *Cf.* *Rowland v. California Men's Colony*, 113 S. Ct. 716 (1993) (extended discussion by both majority and dissent regarding meaning of "person" under Dictionary Act, 1 U.S.C. § 1, which contains definition of "person" applicable to every congressional statute "unless the context indicated otherwise"; under literal reading of statute in question, only a natural person, and not a corporation is eligible for treatment *in forma pauperis*).



ported on a policy level by the applicability of Rule 9006(b)(1)'s "excusable neglect" standard to filings of proofs of claim in chapter 11 cases, which in the context of providing the debtor with a "fresh start" commonly involve equitable considerations, but not to chapter 7 cases, which primarily concern the efficient dismantling and distribution of the bankruptcy estate.<sup>456</sup> Moreover, the predecessors of Rule 9006(b), and of Rule 3003(c), which governs the time to file claims in chapter 11 proceedings, had explicitly been intended for equitable, not strict, application.<sup>457</sup>

In addition, an expansive construction of "excusable neglect" was supported by the interpretation of that phrase as it appeared in the Federal Rules of Civil Procedure: in Rule 6(b), the model for Rule 9006(b)(1)<sup>458</sup>; in Rule 13(f), which allows a counterclaim to be introduced by amendment where the deadline has passed because of the party's "oversight, inadvertence, or ex-

---

<sup>456</sup> *Id.* The Court noted that, while Rule 9006(b)(3) prohibits extension of the deadlines for filing proofs of claim in chapter 7 beyond the provisions of Rule 3002(c), which addresses the filing of such claims, Rule 9006(b) does not similarly restrict the deadline for filing chapter 11 proofs of claim to the times specified in Rule 3003(c). *Id.* n.4.

<sup>457</sup> *Id.* Former Rule 10-401(b) (the counterpart to Rule 3003(c)), concerned the filing deadlines for proofs of claim under chapter X of the Bankruptcy Act of 1898, the forerunner of the Code's chapter 11. Rule 906, like its successor, today's Rule 9006, provided that courts could accept late filings in reorganization proceedings "where the failure to act was the result of excusable neglect." The Advisory Committee Note to Rule 10-401(b) indicated that the extension of the filing deadline in these circumstances "is in accord with Chapter X generally which is to preserve rather than to forfeit rights." *Id.* The note itself quoted a Senate Report that referred to the Bankruptcy Rules' "enlargement of the fixed bar date in a particular case with leave of court and for cause shown in accordance with the equities of the situation." FED. R. BANKR. P. 10-401(b) (advisory committee note) (repealed) (quoting S. REP. NO. 1916, 75th Cong., 3d Sess. (1938)).

<sup>458</sup> Rule 6(b) provides:

When by these rules or by a notice given thereunder or by order of court an act is required or allowed to be done at or within a specified time, the court for cause shown may at any time in its discretion (1) with or without motion or notice order the period enlarged if request therefor is made before the expiration of the period originally prescribed or as extended by a previous order, or (2) *upon motion made after the expiration of the specified period permit the act to be done where the failure to act was the result of excusable neglect*; but it may not extend the time for taking any action under Rules 50(b) and (c)(2), 52(b), 59(b), (d) and (e), 60(b), and 74(a), except to the extent and under the conditions stated in them.

FED. R. CIV. P. 6(b) (emphasis added). The Court cited a variety of precedent from the courts of appeals, but none from the Supreme Court itself, to support a literal reading of "excusable neglect." *Pioneer Inv.*, 113 S. Ct. at 1496 n.7 and n.9.

cusable neglect, or where justice requires”<sup>459</sup>; and in Rule 60(b)(6), which allows courts to reopen a judgment “for any other reason justifying relief from [its] operation” after the expiration of the one-year period of Rule 60(b)(1), which concerns reopening judgments for “mistake, inadvertence, surprise, or excusable neglect.”<sup>460</sup>

Having concluded that “neglect” could appropriately be extended to include certain instances in which the movant had not been the victim of uncontrollable circumstances, the Court next evaluated the factors that would render neglect “excusable.” In the absence of Congressional elaboration of the latter term, and without further discussion, the Court held that “the determination is at bottom an equitable one, taking into account all of the relevant circumstances surrounding the party’s omission.”<sup>461</sup> Such circumstances would include those identified by the Sixth Circuit: “the danger of prejudice to the debtor, the length of the delay and its potential impact on judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith.”<sup>462</sup>

Yet the Court rejected the Sixth Circuit’s assessment of the relative responsibilities of the partnerships and of their counsel for the late filing of the proofs of claim. Rather than addressing the partnerships’ interactions with their attorney regarding the filing, and accordingly insulating them from the adverse effects of their counsel’s negligence, the Court reaffirmed its prior decisions that clients “be held accountable for the acts and omissions of their chosen counsel.”<sup>463</sup> The analysis should concentrate on whether the neglect itself is excusable, and not on whether the

---

<sup>459</sup> *Id.* at 1497 (quoting FED. R. CIV. P. 13(f)). The Court found that for purposes of this rule, lower courts had determined “excusable neglect” by evaluating, among other factors, “the good faith of the claimant, the extent of the delay, and the danger of prejudice to the opposing party.” *Id.* n.10.

<sup>460</sup> *Id.* at 1497 (quoting FED. R. CIV. P. 60(b)(6) & 60(b)(1)). Rule 60(b)(6) has been read to allow reopening of a default judgment against a party that had, during the one-year period, been incarcerated, suffered medical problems, and otherwise been the victim of factors beyond his control. The Court had characterized such circumstance as “an extraordinary situation which cannot fairly or logically be classified as mere ‘neglect’ on his part.” *Id.* (quoting *Klaprott v. United States*, 335 U.S. 601, 613-24 (1949)).

<sup>461</sup> *Id.* at 1498.

<sup>462</sup> *Id.* (citing *Pioneer Inv.*, 943 F.2d at 677).

<sup>463</sup> *Id.* at 1499 (citing *Link v. Wabash R. Co.*, 370 U.S. 626 (1962) (not inequitable to client to dismiss his claim because of his counsel’s unexcused failure to attend scheduled pretrial conference: attorney was client’s freely-chosen representative, whose acts, and receipt of notice, bound client); *United States v.*

clients are blameless.<sup>464</sup>

On balance, though, the Court noted that the *Dix* factors had favored the partnerships, which had been found to have acted in good faith and whose assertion of a late claim would neither prejudice the debtor nor disrupt the efficient administration of the bankruptcy proceeding.<sup>465</sup> Although the Court attached "little weight" to the disorder attending Richards's professional transition, it did recognize the unusually inconspicuous placement of the notice of bar date in the April 13 notice to creditors.<sup>466</sup> Richards should indeed have read carefully enough to become aware of the notice; but since there was no showing of prejudice to the partnerships or to the bankruptcy process, "or any indication at all of bad faith," the Court upheld the Sixth Circuit's conclusion that the neglect had been "excusable."<sup>467</sup>

Justice O'Connor's dissent, which was joined by Justices Scalia, Souter and Thomas, focused on the "plain language" of Rule 9006(b)(1), which authorizes a court "at any time in its discretion . . . [to] permit [an] act to be done where the failure to act

---

Boyle, 469 U.S. 241 (1985) (client may properly be penalized for counsel's late filing of tax return).

<sup>464</sup> *Id.*

<sup>465</sup> *Id.* at 1499. In fact, the debtor's second amended plan of reorganization had made provisions for the partnerships' claims. *Id.*

<sup>466</sup> *Id.* at 1499-500.

<sup>467</sup> *Id.*

Judge Irenas of the United States District Court for the District of New Jersey recently reversed a bankruptcy court's order, issued before *Pioneer Investment*, that had rejected the appellant's motion to file a late proof of claim; the district court remanded the decision to the bankruptcy court for reconsideration. *Linder v. Trump's Castle Assocs.*, 155 B.R. 102 (D.N.J. 1993). The bankruptcy court was found not to have taken into account the last two of the three factors that the Supreme Court's decision "requires a court to weigh . . . in deciding whether there is excusable neglect under Rule 9006(b)(1): the conduct of the party and his counsel; prejudice to the debtor; and the interests of efficient judicial administration." *Id.* at 108.

The district court noted three elements of the situation before it that made the case for allowing a late filing "more compelling" than in *Pioneer Investment*. *Id.* First, the claimant, a slip-and-fall plaintiff, had selected her lawyer to represent her in her personal injury action, not in the defendant's subsequent bankruptcy proceedings; indeed, the record did not reflect that the claimant and her lawyer had possessed any actual knowledge of the debtor's bankruptcy when the notice of the bar date had been mailed. Second, this notice had not been mailed directly to the claimant. (Although the debtor's claims agent had certified that it had mailed this notice to the claimant's lawyer, the lawyer denied having received it, or having otherwise become aware of any obligation to file a proof of claim or of a deadline for doing so). Finally, this individual claimant was not, as in *Pioneer Investment*, "[a] sophisticated bankruptcy entit[y] with actual knowledge of the bar date," nor was her chosen lawyer "experienced bankruptcy counsel." *Id.*

[previously] was the result of excusable neglect.”<sup>468</sup> In the dissent’s reading, a court was first called on to determine whether the situation evidenced “excusable neglect”: *only after* finding such neglect was it to address the equities of extending the deadline.<sup>469</sup> By instituting a balancing test involving a multitude of equitable factors, the majority had diverted attention from the “threshold” inquiry: “the reason the deadline was missed.”<sup>470</sup>

Moreover, the Court had unjustifiably concluded from the absence of statutory benchmarks for “excusable neglect” that equitable considerations underlay the inquiry *ab initio*,<sup>471</sup> and accordingly had improperly introduced “a multifactor balancing test covering numerous equitable considerations.”<sup>472</sup> Indeed, in a recent decision interpreting the corresponding portion of Federal Rule of Civil Procedure 6(b), the Court’s analysis of “excusable neglect” had addressed, rather than the equities of the matter, the degree of fault of the party that had failed to file.<sup>473</sup>

The dissent identified several “guideposts” of its own, albeit not of the most explicit nature, for a stricter interpretation of the rule. First, it read Rule 9006(b)(1) as requiring a retroactive determination of “excusable negligence,” based on the movant’s own blameworthiness, rather than a prospective determination that would take into account the effect on the parties and on the proceedings of allowing the late filing. The language of the Rule concerned whether “the failure to act *was* the *result* of excusable neglect,”<sup>474</sup> thereby clearly indicating that the relevant evalua-

---

<sup>468</sup> *Id.* at 1500 (O’Connor, J., dissenting) (quoting FED. R. BANKR. P. 9006(b)(1)).

<sup>469</sup> *Id.* The majority protested that, although reducing the factors of the test for “excusable neglect,” the dissent had hardly precluded litigation over the application of the remaining factors. Only a bright-line test prohibiting any late filings where the movant had been to any degree negligent would avert such litigation; and yet, the majority found such a test irredeemably inflexible. *Id.* at 1498 n.14 (O’Connor, J., dissenting).

<sup>470</sup> *Id.* at 1505 (O’Connor, J., dissenting).

<sup>471</sup> *Id.* at 1500 (O’Connor, J., dissenting).

<sup>472</sup> *Id.*

<sup>473</sup> *Id.* at 1501 (O’Connor, J., dissenting) (citing *Lujan v. National Wildlife Federation*, 497 U.S. 871 (1990) (refusal to permit late filing under “excusable neglect” standard of Rule 6(b) was within discretion of district court)).

The majority had distinguished *Lujan* by observing that it did not “define ‘excusable neglect’ or even decide whether that standard could have been met on the facts of that case.” *Id.* at 1498 n.13. Admitting that *Lujan* had offered no definition of the phrase, the dissent nonetheless insisted that the decision had “applied that phrase to the facts before us,” and had in fact characterized the “excusable neglect” standard as “the greatest of all” obstacles to allowing an extension of time. *Id.* (quoting *Lujan*, 497 U.S. at 897).

<sup>474</sup> FED. R. BANKR. P. 9006(b)(1) (emphasis added).

tion should not incorporate considerations of developments after the neglect itself had occurred.<sup>475</sup> Second, to replace the majority's reliance on a collegiate dictionary's definition of "neglect,"<sup>476</sup> the dissent found "dispositive," in the absence of congressional indications to the contrary, a standard *legal* dictionary's entry for the term of art, "excusable neglect," which emphasized the circumstances rather than the consequences of the failure to act in a timely manner.<sup>477</sup>

Not only would the determination of "excusable neglect" from a retroactive and equitable vantage point be unavoidably self-defining, asserted the dissent, but it would vitiate the very requirement that such neglect be "excusable." If "excusable neglect" merely consisted of those actions that the court, after examining the equities, found worthy of redemption, there would by implication be no neglect that automatically would not be excused, even "the highly culpable and the willful."<sup>478</sup> The majority thus had provided no guidance to those who, in its words, might "freely ignor[e] court-ordered deadlines in the hopes of winning a permissive reprieve under Rule 9006(b)(1)."<sup>479</sup>

Noting the disagreement between the Sixth Circuit Court of Appeals and the bankruptcy and district courts, Justice O'Connor criticized the the majority's balancing test as unduly indetermi-

---

<sup>475</sup> *Pioneer Inv.*, 113 S. Ct. at 1501-02. This reading neglected, however, the explicit statutory authorization of the court to extend the time period "at any time in its discretion," which might be seen to allow for post-deadline inquiries. FED. R. BANKR. P. 9006(b)(1).

<sup>476</sup> *Pioneer Inv.*, 113 S. Ct. at 1494-95. See *supra* note 455 and accompanying text.

<sup>477</sup> *Id.* at 1502 (O'Connor, J., dissenting) (quoting BLACK'S LAW DICTIONARY 566 (6th ed. 1990) (defining "excusable neglect" as "a failure to take the proper steps at the proper time, not in consequence of the party's own carelessness, inattention, or willful disregard of the process of the court, but in consequence of some unexpected or unavoidable hindrance or accident, or reliance on the care and vigilance of his counsel or on promises made by the adverse party. As used in rule (*e.g.*, Fed. R. Civ. P. 6(b)) authorizing court to permit an act to be done after expiration of the time within which under the rules such act was required to be done, where failure to act was the result of 'excusable neglect,' the quoted phrase is ordinarily understood to be the act of a reasonably prudent person under the same circumstances.")). Cf. *Farrey*, 111 S. Ct. at 1829 ("No one asserts that the two verbs underlying [§ 522(f)(1)] possess anything other than their standard legal meaning: 'avoid' meaning 'annul' or 'undo' . . . and 'fix' meaning to 'fasten a liability upon.'") (citing BLACK'S LAW DICTIONARY). See also LOOKING-GLASS, *supra* note 1, at 271. Humpty Dumpty explains to Alice that "'slithy' means 'lithe and slimy.' 'Lithe' is the same as 'active.' You see it's like a port manteau [suitcase] — there are two meanings packed up into one word."

<sup>478</sup> *Id.*

<sup>479</sup> *Id.*

nate and, therefore, appealable.<sup>480</sup> Equitable considerations should not be relevant in determining whether a party's negligence could constitute "excusable neglect," because the first part of the Court's test — whether the conduct at issue was excusable neglect at all — was dispositive. In the situation before the Court, the partnerships' neglect "was inexcusable under any standard."<sup>481</sup>

Though agreeing with the majority that a client cannot be insulated from the effects of his counsel's errors, the dissent observed that the bankruptcy court had not found that the partnerships' counsel had missed the bar date because of the unusual form of notice; in fact, that court had found that both the attorney and his clients had had actual notice of the deadline.<sup>482</sup> The former counsel had himself admitted that the failure to file the proofs of claim timely "really is probably mine!"<sup>483</sup> Without remanding the matter to the bankruptcy court for a factual finding on whether counsel's failure was indeed attributable to the form of notice, the dissent could not reach this conclusion.<sup>484</sup> Neither the partnerships, their former counsel, the court of appeals, or the majority had provided a clear explanation of the late filing: the bankruptcy court, however, had characterized the error as the result of the attorney's "indifference," which would remove it from the scope of "excusable neglect."<sup>485</sup>

By reaching for their dictionaries, both the majority and the dissent in *Pioneer Investment* might be said to have addressed the "plain meaning" of the Rule at issue. However, their disagreement over whether the phrase "excusable neglect" should be interpreted as a term of art or as the conjunction of two ordinary words indicates a continuing confusion over the quantum of language that is susceptible to "plain meaning" analysis. Moreover, like Justice Scalia's dissent in *Dewsnup*, Justice O'Connor's dissent in *Pioneer Investment* illustrates the invocation of "plain meaning" considerations in the service of predictability, and thus of reduced appellate litigation in bankruptcy. Yet the narrow margin by which this interpretation was defeated implies that even the

---

<sup>480</sup> To the dissent, the ambiguity of the Court's new test "not only renders consistent application unlikely but also invites unproductive recourse to appeal." *Id.* at 1505 (O'Connor, J., dissenting).

<sup>481</sup> *Id.* at 1503 (O'Connor, J., dissenting).

<sup>482</sup> *Id.* at 1504 (O'Connor, J., dissenting).

<sup>483</sup> *Id.* (quoting the record).

<sup>484</sup> *Id.*

<sup>485</sup> *Id.*

Court may not be able to enunciate rules of "plain meaning" themselves sufficiently clear to preclude alternative readings of the Code.

K. *Nobelman v. American Savings Bank*<sup>486</sup>

With only a passing mention of its decision in *Dewsnup*, which barred "lien-stripping" of undersecured mortgages in *chapter 7* proceedings,<sup>487</sup> the Court held one term later that the "plain language" of § 1322(b)(2) prohibited *chapter 13* debtors from "stripping down" undersecured mortgages on their primary residences. *Nobelman* thereby overruled the decisions of four circuit courts of appeals.

Justice Scalia did not lament, as he had in *Wolas*<sup>488</sup> and *Patterson*,<sup>489</sup> the "legal culture" that had given rise to those decisions. The Justice's tolerance for ambiguity in this context was reflected by the Court's adoption of a "plausible" (rather than definitive) interpretation of the Code section in question, and abandonment of the "rule of the last antecedent," which itself would have provided an alternate interpretation "quite sensible as a matter of grammar." Indeed, despite a one-paragraph concurrence by Justice Stevens, who insisted that "the Court's literal reading of the text of the statute is faithful to the intent of Congress," *Nobelman* may indicate that the "plain meaning" analysis of the Code is substantively- rather than semantically-driven.

1. Background

In 1984, the debtors executed a note in favor of the American Savings Bank (the "Bank") in the amount of \$68,250.00. The note was secured by a deed of trust on the debtors' primary residence, a condominium in a Dallas complex, and by an undivided 0.67% interest in: the common areas of the complex; escrow funds; proceeds of hazard insurance; and rents. Six years later, the debtors filed a voluntary *chapter 13* petition. The Bank's proof of claim, originally in the amount of \$71,265.04 but subsequently amended to \$71,335.04, indicated that the claim would be secured to the extent of the Bank's security interest in the

---

<sup>486</sup> 113 S. Ct. 2106 (1993).

<sup>487</sup> See generally *Dewsnup v. Timm*, 112 S. Ct. 773 (1992); see also *supra* notes 204-73 and accompanying text.

<sup>488</sup> See *Union Bank v. Wolas*, 112 S. Ct. 527, 534 (1991) (Scalia, J., dissenting); see also *supra* note 203 and accompanying text.

<sup>489</sup> See *Patterson*, 112 S. Ct. at 2250-51 (Scalia, J., concurring); see also *supra* notes 424-25 and accompanying text.

property, and unsecured for any remainder.<sup>490</sup>

The debtors' plan of reorganization set the value of the residence at \$23,500.00, without objection, and proposed to make direct payments to the Bank of this amount at the mortgage contract rate. Under the operation of § 506(a),<sup>491</sup> the remaining \$41,257.66 of the Bank's claim would be treated as a general unsecured claim, *i.e.*, would not be paid.<sup>492</sup> In an unreported decision the bankruptcy court for the Northern District of Texas, agreeing with the objections of the Bank and the standing chapter 13 trustee, denied confirmation of the plan, on the grounds that the bifurcation of the Bank's claim by § 506(a) was a "modification" that would violate § 1322(b)(2).<sup>493</sup> Under the latter provision, a chapter 13 plan may "modify the rights of holders of secured claims, *other than a claim secured only by a security interest in real property that is the debtor's principal residence*, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims."<sup>494</sup>

#### a. The District Court Opinion

In affirming the bankruptcy court, the district court reviewed at length the divided precedent on the issue: three court of appeals decisions supporting the debtor's plan stood against "numerous bankruptcy court[ ]" decisions to the contrary.<sup>495</sup> In *Houghland v. Lomas & Nettleton Company (In re Houghland)*,<sup>496</sup> the Ninth Circuit had reduced the issue to a "relatively simple" question by relying on the plain meaning of the statutory language. Section 103(a)<sup>497</sup> indicated that § 506(a), and thus its division of each undersecured claim into a "secured claim" and an "unsecured claim," were directly applicable to claims in chapter 13

---

<sup>490</sup> *Nobelman v. American Savings Bank (In re Nobelman)*, 129 B.R. 98, 99 (N.D. Tex. 1991).

<sup>491</sup> See *supra* note 116.

In *Ron Pair*, the Court had interpreted this section as "provid[ing] that a claim is secured only to the extent of the value of the property on which the lien is fixed; the remainder of that claim is considered unsecured." *U.S. v. Ron Pair Enterprises*, 489 U.S. 235, 239 (1989).

<sup>492</sup> The debtors' proposed plan, however, would have cured the prepetition arrearages owed to the Bank. *Nobelman*, 129 B.R. at 99.

<sup>493</sup> *Id.*

<sup>494</sup> 11 U.S.C. § 1322(b)(2) (emphasis added).

<sup>495</sup> *Nobelman*, 129 B.R. at 101.

<sup>496</sup> 886 F.2d 1182, 1183 (9th Cir. 1989).

<sup>497</sup> Section 103(a) provides, in relevant part, that chapter 5 of title 11 applies to a case under chapter 13 of the same title. See generally 11 U.S.C. § 103(a) (1988).



proceedings.<sup>498</sup>

Proceeding to analyze the language of § 1322(b)(2) directly, *Houghland* observed that

the "other than" clause . . . follows the secured claim portion of the sentence and precedes the unsecured claim portion. Certainly it refers to what preceded it, and indicates that a secured residential real estate claim will have special protection. Indeed, if the referent of the "other than" clause is not the secured claim language which precedes it, what could the referent be? It would be most unusual if it were the unsecured claim language or the whole sentence. That strongly indicates that only the "secured claim" portion is protected.<sup>499</sup>

The Ninth Circuit foresaw little prejudice to residential real estate lenders from its decision to protect against modification only the secured portion of an undersecured lender's claim: most of such lenders, it noted, take care to avoid being undersecured.<sup>500</sup> In addition, even if the legislative history had been relevant, commentators had found in it only an indication that Congress had intended to benefit these lenders.<sup>501</sup>

In its own examination of the question, the Third Circuit had found "no language of [§ 1322(b)(2)] which is inconsistent with [*Houghland's*] construction,"<sup>502</sup> and agreed that the legislative history of this section "does not provide. . . much insight into the critical

---

<sup>498</sup> *Houghland*, 886 F.2d at 1183.

<sup>499</sup> *Nobelman*, 129 B.R. at 100 (quoting *Houghland*, 886 F.2d at 1184). The court dismissed suggestions that Congress would have signalled such an intent by referring in the "other than" clause to a "secured claim" or to "such claim." These constructions would have resulted in "an awkward and wooden sentence structure. . . . As it is, the sentence has a natural rhythm and flow that does not disturb its clarity." *Houghland*, 886 F.2d at 1183.

The Ninth Circuit concluded that

Congress quite plainly has provided for the separation of undersecured claims into two components—a secured component and an unsecured component. It has then provided for their treatment in Chapter 13 proceedings. The secured portion has special protection when residential real estate lending is involved. The unsecured portion does not.

*Id.* at 1185.

<sup>500</sup> *Id.* The Court declined to specify whether its interpretation of § 1322(b)(2) applied to "persons who are not true residential real estate lenders [who] secure their loans by taking a security interest in a debtor's home so that they can take advantage of the Chapter 13 provisions." *Id.*

<sup>501</sup> *Id.*

<sup>502</sup> *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123, 127 (3d Cir. 1990), cited by *Houghland*, 129 B.R. at 100.

question here.”<sup>503</sup> The Tenth Circuit had similarly detected “nothing in the plain language of § 1322(b)(2) which ‘instructs us to go beyond the Code’s statutory definition of the term secured claim’ to protect the unsecured portion of an undersecured home mortgage.”<sup>504</sup> The court of appeals had accordingly endorsed

a literal reading of 11 U.S.C. § 1322(b)(2) [as] less speculative and less quasi-legislative than attempting to ferret its meaning from its legislative history, which . . . is not clear enough with respect to this issue to show a “demonstrably” different congressional intent than that indicated by the plain meaning of the statute itself.<sup>505</sup>

The district court in *Nobelman*, itself citing the “plain language of § 1322(b)(2),”<sup>506</sup> rejected the analyses of these circuit courts of appeals as “strained and unconvincing.”<sup>507</sup> First, unlike *Houglan*, the court found “an inescapable, although limited, conflict”<sup>508</sup> be-

---

<sup>503</sup> *Wilson*, 895 F.2d at 127. Tracing the evolution of § 1322(b)(2) from the recommendations of the Committee on the Bankruptcy Laws of the United States, which Congress had created in 1970, through the separate bills introduced in the Senate and the House, the Third Circuit concluded that

although it is clear that [this section] was inserted on behalf of the home-mortgage industry, the fact that the provision itself was a compromise [between the Senate’s proposed restriction on the modification of not only residential but also non-residential real estate mortgages, and the House’s tolerance for unrestricted modification of all secured and unsecured claims] suggests that the residential mortgage providers did not emerge with all the protection they may have sought.

*Id.* at 128.

<sup>504</sup> *Eastland Mortgage Co. v. Hart (In re Hart)*, 923 F.2d 1410, 1415 (10th Cir. 1991), *quoted by Nobelman*, 129 B.R. at 101. The Tenth Circuit agreed with the Third and Ninth Circuits that

an undersecured mortgage is, for the purposes of the bankruptcy code, two *claims*, and only the secured *claim* is protected by section 1322(b)(2). More importantly, we recognize that while bifurcations, in the literal sense, may be a modification of the *mortgage* represented in the secured and unsecured claims, bifurcation is not, of itself, a “modification” of the secured claim made impermissible by section 1322(b)(2). Indeed, the act of bifurcation recognizes, but does not affect, the secured claim.

*Id.* at 1415.

<sup>505</sup> *Id.*

<sup>506</sup> *Nobelman*, 129 B.R. at 104.

<sup>507</sup> *Id.* at 101.

<sup>508</sup> *Id.* at 102 n.2. “It is clear that a limited conflict exists, in that section 506 can be used to undermine the protection afforded by section 1322(b)(2) under the very narrow circumstances defined by that statute.” *Id.* at 102. *Cf. Hart*, 923 F.2d at 1415 n.4 (term “secured claim” as used in § 1322(b)(2) is defined by § 506(a), thereby requiring bifurcation); *Wilson*, 895 F.2d at 128 (“construing section 1322(b)(2) to allow bifurcation of secured and unsecured portions and to allow modification of the unsecured portion makes it consistent with section 506, a sec-

tween § 506(a) and § 1322(b)(2), in light of which the more specific provisions of the latter subsection should control the more general provisions of the former.<sup>509</sup> Second, in *Houghland* the Ninth Circuit had restricted § 1322(b)(2)'s operation to preventing further modification of a claim already stripped down to its secured portion, thereby effectively rendering that subsection meaningless.<sup>510</sup> Third, that circuit's "plain meaning" analysis had overlooked the Code's definition of "claim" as a "right to payment," whether such right is secured or unsecured.<sup>511</sup> Fourth, in enacting the Code Congress had not indicated any intent to alter the existing practice of not allowing chapter 13 debtors to modify claims secured by a mortgage on the debtor's residence.<sup>512</sup> Finally, on a policy level, the debtor would receive an unintended augmentation of his "fresh start" if allowed to retain any post-discharge appreciation in the property's value.<sup>513</sup>

#### b. *The Fifth Circuit Opinion*

Before the Fifth Circuit Court of Appeals issued its decision affirming the district court, several significant developments had occurred. First, the Supreme Court had handed down *Dewsnup v. Timm*,<sup>514</sup> which bars individual debtors in chapter 7 liquidation proceedings from stripping down the liens of undersecured creditors. However, the *Dewsnup* holding had specifically been restricted to "the case before us," and would not necessarily govern "all possible fact situations."<sup>515</sup> In addition, that decision did not address the connotations of the phrase "allowed secured claim" in any section of the Code other than § 506(d).<sup>516</sup>

---

tion of general applicability"); *Houghland*, 886 F.2d at 1184 (sections "are in harmony when read in the context of the whole statute").

<sup>509</sup> *Nobelman*, 129 B.R. at 102.

<sup>510</sup> *Id.*

<sup>511</sup> *Id.* (quoting 11 U.S.C. § 101(5) (1988)).

<sup>512</sup> *Id.* at 103-04 (citing *In re Mitchell*, 125 B.R. 5, 8 (D.N.H. 1990); *In re Kaczmarczyk*, 107 B.R. 200, 203 (Bankr. D. Neb. 1989). In addition, the Fifth Circuit's review of the legislative history of § 1322(b)(2) had identified a congressional intent to provide "home mortgagor lenders, [who perform] a valuable social service through their loans, . . . special protection against modification thereof (*i.e.*, reducing installment payments, secured valuations, etc.)." *Grubbs v. Houston First American Savings Assoc.*, 730 F.2d 236, 246 (5th Cir. 1984) (citation omitted), *quoted by Nobelman*, 129 B.R. at 103.

<sup>513</sup> *Id.* at 104 (citing *First Interstate Bank of Oklahoma, N.A. v. Woodall* (*In re Woodall*), 123 B.R. 95, 97-98 (Bankr. W.D. Okla. 1990).

<sup>514</sup> 112 S. Ct. 773 (1992). See *supra* notes 196-262 for an analysis of the *Dewsnup* decision.

<sup>515</sup> *Id.* at 778.

<sup>516</sup> *Id.* at 778 n.3.

Three months after *Dewsnup*, the Second Circuit Court of Appeals, finding that decision's construction of "secured claim" inapplicable to § 1322(b)(2), joined the Third, Ninth and Tenth Circuits in allowing liens to be stripped down in chapter 13 proceedings.<sup>517</sup> Two months later, reaffirming its own pre-*Dewsnup*

---

<sup>517</sup> In *Bellamy v. Federal Home Loan Mortgage Corporation (In re Bellamy)*, the court perceived that

[t]he real question is whether the "rights" to which § 1322(b)(2) refers include the mortgagee's rights concerning its claim or its rights with respect to its *secured claim*. If the former, then § 1322(b)(2) must be read as prohibiting modification of a mortgagee's right to payment of the full amount of its allowed claim, i.e., the amount of its note. But construing this section of the Code in that light would be directly contrary to one of the Code's cornerstones, aimed at making a fundamental change from the Bankruptcy Act, that treatment under the Code turns on whether a *claim* is secured or unsecured, not on whether a *creditor* is secured or unsecured.

962 F.2d 176, 179 (2d Cir. 1992) (citation omitted). According to the Second Circuit, the bifurcation of an undersecured claim under § 506(a) did not modify the creditor's "rights," but merely resolved the manner in which the Code would satisfy the creditor's right to payment. *Id.* at 180.

*Bellamy* held that "[t]he 'other than' clause [of § 1322(b)(2)] is most logically read to refer to those words that precede it: 'secured claims.'" *Id.* at 180. Not only was there no conflict between the two sections, *id.*, but the legislative history "indicates only that § 1322(b)(2) was designed to provide greater protection to home mortgage lenders than other secured creditors in the Chapter 13 context. This is, of course, plain on the face of the statute itself," as well as consistent with the Second Circuit's reconciliation of the two sections at issue. *Id.* at 182.

*Bellamy* found *Dewsnup* inapplicable to chapter 13 proceedings because the *Dewsnup* opinion had construed "secured claim," in the context of § 506(d), as indicating a claim that was secured to *any* extent. By contrast, the Second Circuit read § 506(a)'s reference to "secured claim" to denote to the precise extent to which the claim in question *was in fact* secured. *Id.* at 183.

For several reasons, the circuit court found that the former approach would make § 1322(b)(2) "difficult to comprehend and would render it in conflict with the Code's overall scheme." *Id.* at 183. The court raised the following considerations:

(1) § 506(d) refers only to "secured claims." However, § 1322(b)(2) refers as well to "unsecured claims," which could be presumed to have the same meaning in that section as in § 506(a), and thereby (circularly) to accord "secured claims" the same meaning as in both sections.

(2) Both § 506(a) and § 1322(b)(2) involve the treatment of claims, and are to be interpreted in light of the Code's focus on the status of claims, and not of creditors, as secured or unsecured; and deviation from this "expressed treatment of claims (designed specifically as a change from pre-Code practice . . .)" would be so exceptional as necessarily to have been indicated explicitly by Congress either in the Code itself or in its legislative history. By contrast, § 506(d) concerns the treatment of liens.

(3) The *Dewsnup* Court had declined to apply to § 506(d) the definition of "secured claim" under § 506(a), reasoning that Congress had not indicated its intent to diverge from pre-Code practice regarding the treatment of liens. The Code directly indicates, however, that, contrary to pre-Code practice, the debtor may modify the claims of creditors that hold real property as security.

(4) Although *Dewsnup* prohibits lien-stripping in a chapter 7 proceeding, in

precedent that had allowed lien-stripping in chapter 13, the Third Circuit cited the Second Circuit's analysis approvingly.<sup>518</sup>

Like the district court, the Fifth Circuit held that the specific provisions of § 1322(b)(2) conflicted with, and thereby controlled, the more general provisions of § 506(a).<sup>519</sup> In addition, the language of § 1322(b)(2) prohibited the modification not of those *claims* that were secured solely by a security interest in the debtor's principal residence, but of "*the rights of holders of*" such claims, whether under-, over- or fully-secured.<sup>520</sup> Finally, reviewing its previous examination of this section's legislative history, the Court reiterated that Congress had "desire[d] to afford some protection to the home mortgage industry."<sup>521</sup>

## 2. Preferring "Plausible" to "Quite Sensible" Construction

In a relatively brief opinion by Justice Thomas, the Supreme Court unanimously affirmed the Fifth Circuit's decision. As had the district court and the court of appeals, the Justices emphasized the focus of § 1322(b)(2) on restricting not the modifications of certain claims themselves but instead the modification of the "rights" of the holders of those claims. However,

---

which a debtor's personal liability would be discharged on liquidation, a chapter 13 debtor would remain personally liable for certain obligations until he or she made all payments called for by the plan of reorganization. Thus, lien-stripping in a chapter 13 context would have a more significant and long-lasting impact on the debtor's "fresh start" and chances of successful reorganization: "discharging the unsecured portion of the debt allows the debtor to pay off the secured position of the note at an earlier date and lessens the total debt burden." *Id.* at 183-86.

Even if authorizing lien-stripping would permit the debtor to benefit from subsequent appreciation in the value of the property, the Court noted, the legislative history of § 1322(b)(2) did not oppose this outcome. "In addition, these speculative contingencies regarding fluctuating real estate prices are not sufficient to justify a result contrary to that required by the Code's language." *Id.* at 186.

<sup>518</sup> In *Sapos v. Provident Institution of Savings*, 967 F.2d 918 (3d Cir. 1992), the court followed the analysis of *Bellamy*, noting as well the *Dewsnup* Court's restriction of its decision to "the [chapter 7] case before us." *Id.* (quoting *Dewsnup*, 112 S. Ct. at 778). The Third Circuit concluded, in relevant part, that a "Chapter 13 debtor with an undersecured debt, whether that debt be secured solely by residential real estate or by realty and personalty, may resort to bifurcation under section 506(a)." *Sapos*, 967 F.2d at 928. *Cf. Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *see also supra* notes 502-03 and accompanying text.

<sup>519</sup> *Nobelman v. American Savings Bank*, 989 F.2d 483, 488 (5th Cir. 1992) (citations omitted).

<sup>520</sup> *Id.* (quoting 11 U.S.C. § 1322(b)(2) (emphasis added)).

<sup>521</sup> *Id.* at 489 (citing *Grubbs v. Houston First America Sav. Assoc.*, 730 F.2d 236, 245-46 (5th Cir. 1984)). Although the court cited *Grubbs*, that decision had not focused on the interplay between § 1322(b)(2) and § 506(a). *Id.*

[t]he term "rights" is nowhere defined in the Bankruptcy Code. In the absence of a controlling federal rule, we generally assume that Congress has "left the determination of property rights in the assets of a bankrupt's estate to state law," since such "[p]roperty interests are created and defined by state law."<sup>522</sup>

The rights protected by § 1322(b)(2) were thus those rights granted to the creditor by the mortgage instrument, as construed and enforced under Texas law: namely, the rights to repayment, retention of the lien, acceleration of the loan upon default, foreclosure and public sale, and suit to recover any deficiency remaining after foreclosure.<sup>523</sup>

The Court explicitly rejected the "rule of the last antecedent," by which the "other than" clause of § 1322(b)(2) would have been taken to refer to the immediately preceding phrase, "secured claims," as that term was defined by § 506(a). "We acknowledge that this reading of the clause is quite sensible as a matter of grammar. But it is not compelled. Congress chose to use the phrase 'claim secured . . . by' in § 1322(b)(2)'s exception, rather than repeating the term of art 'secured claim.'"<sup>524</sup> Thus, the Court found it "also plausible," in light of the Code's broad definition of "claim," to interpret "a claim secured only by a [homestead lien]" as connoting both the secured and unsecured elements of the claim.<sup>525</sup> That, in fact, was found to be the sense of the phrase "claim. . . secured by a lien" in § 506(a).<sup>526</sup>

Moreover, even if it were accepted that the debtor's stripping down the Bank's undersecured lien to its secured portion would not "modify" the unsecured component of the lien, it would undeniably change the interest rate, amount of monthly payment, and/or term of the note, thereby effecting "a significant modification of a contractual right."<sup>527</sup> In fact, neither the mortgage contract nor the Code indicated how such a modification would be implemented.<sup>528</sup>

---

<sup>522</sup> *Nobelman*, 113 S. Ct. at 2110 (quoting *Butner v. United States*, 440 U.S. 48, 54-55 (1979)).

<sup>523</sup> *Id.* Indeed, the Court observed that "[t]hese are the rights that were 'bargained for by the mortgagor and the mortgagee.'" *Id.* (quoting *Dewsnup v. Timm*, 112 S. Ct. 773, 778 (1992)).

<sup>524</sup> *Id.* at 2111.

<sup>525</sup> *Id.* (citing 11 U.S.C. § 101(5) (1988) (defining "claim" to include any "right to payment, whether. . . secure[d] or unsecured," or any "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether. . . secure[d] or unsecured.")).

<sup>526</sup> *Id.*

<sup>527</sup> *Id.*

<sup>528</sup> *Id.*

Perhaps uncomfortable with the Court's implication that the Code "should provide less protection to an individual's interest in retaining possession of his or her home than of other assets," Justice Stevens added in a one-paragraph concurrence that, as indicated by the Fifth Circuit's review of the legislative history of § 1322(b)(2), "favorable treatment of residential mortgagees was intended to encourage the flow of capital into the home lending market."<sup>529</sup> Thus, "it . . . seems quite clear that the Court's literal reading of the text of the statute is faithful to the intent of Congress."<sup>530</sup>

As compared to the robust analyses advanced by the Court in its other "plain meaning" decisions (for instance, *Dewsnup* and *Patterson*), the logic of *Nobelman* seems curiously flabby. Dismissing the application of a well-respected rule of statutory interpretation as "quite sensible as a matter of grammar [but] not compelled," the Court instead introduced a broad definition of "claim" to advance an interpretation that it could most strongly characterize as "also plausible"<sup>531</sup> and, in light of certain practical considerations, "more reasonable."<sup>532</sup> A paragraph-long digression on the debtor's ability to pay off arrearages, and on the effect of the automatic stay on the lender, seems extraneous.<sup>533</sup> Moreover, both the omission of any extended discussion of *Dewsnup*, and Justice Stevens's election to offer an explicit reconciliation of the Court's conclusion with the literal terms of the statute suggest that the "plain meaning" doctrine is far from plain, and at its core concerns much more than mere syntax.<sup>534</sup>

---

<sup>529</sup> *Id.* (Stevens, J., concurring) (citing *Grubbs*, 730 F.2d at 245-46).

<sup>530</sup> *Id.*

<sup>531</sup> *Cf. U.S. v. Nordic Village, Inc.*, 112 S. Ct. 1016 (1992). Justice Scalia, writing for the majority, held that because of the existence of "plausible" alternative readings of § 106(c), which concerns the applicability to bankruptcy proceedings of the principle of sovereign immunity, that section could not be "unambiguously" construed to impose monetary liability on the federal government. Yet Justice Stevens's dissent, which was joined by Justice Blackmun, dismissed the alternate readings as "obviously less satisfactory—both as a matter of sound bankruptcy policy and as a principled interpretation of the English language—than a literal reading of the statute." *Id.* at 1019 (Stevens, J., dissenting). The *Nordic Village* dissent also observed that "[t]he legislative history unambiguously demonstrates that Congress intended the statute to be read literally." *Id.* at 1018 (Stevens, J., dissenting).

<sup>532</sup> *Id.* at 2111.

<sup>533</sup> *Id.* at 2110.

<sup>534</sup> In one of the first judicial analyses of *Nobelman*, the bankruptcy court for the Eastern District of Pennsylvania observed:

[I]t is important to emphasize what *Nobelman* did not decide. Firstly, the Court did not rely on the reasoning employed in the context of a Chapter 7 case in *Dewsnup v. Timm* [citation omitted]. It did not hold

*L. Rake v. Wade*<sup>535</sup>

If the Court's unanimity, and assignment of a "plain meaning" opinion to its most junior Justice, had signalled *Nobelman*'s resounding rejection of an interpretation admittedly "plausible," Justice Thomas's opinion for the entire court in *Rake v. Wade* offered no such concessions. Reconciling three Code provisions to allow postpetition interest on arrearages to holders of oversecured home mortgages that did not explicitly provide for such interest, the Court endorsed a holistic hermeneutics.

### 1. Background

In this consolidated case, three married couples that had each filed for chapter 13 protection all appealed on the same issue. Each couple was in default on a promissory note secured by an oversecured first mortgage on its principal residence; each had proposed a chapter 13 plan that would satisfy the schedule set forth in its mortgage for future payments of principal and interest. Each pair of debtors also anticipated curing their default by paying over time the missed monthly payments, as well as the attorney's fees and default penalties, required by their mortgage. The mortgages assessed a five-dollar late payment charge, and provided that upon a default in payment the lender could fore-

---

that a "strip down" of a mortgagee's lien was not permissible in a Chapter 13 case. Thus . . . the Court did not hold that the reasoning of *Dewsnup* applied to a Chapter 13 (or a Chapter 11) case. If the Court had so reasoned, it would have been unnecessary for it to reach the issue of the impact of § 1322(b)(2) upon "lien stripping" . . .

Secondly, the Court did not comment on the issue of whether 11 U.S.C. § 1322(b)(2) was applicable to the mortgage at issue, given the particular security interests taken therein, because the *Nobelman* debtor apparently assumed or conceded that the mortgage in issue was within the scope of § 1322(b)(2).

*Hirsch v. Citicorp Mortgage Corp.* (*In re Hirsch*), 155 B.R. 688, 689, 690 (Bankr. E.D. Pa. 1993).

Because the debtor/mortgagor in *Hirsch* had granted a security interest in "rents," "profits," present and future "fixtures," and all "replacements and additions" to the debtor's residence, the court found that the mortgagee did not have a claim secured "only by . . . real property," and thus that § 1322(b)(2) (and the *Nobelman* analysis) did not apply. *Id.* at 690-91. Accordingly, the debtor was permitted to utilize § 506(a) to strip down the mortgage, conditional on his being granted confirmation of a Chapter 13 plan that would pay the mortgagee's allowed secured claim in full under § 1325(a)(5)(B) and ultimately on the debtor's obtaining a discharge. *Id.* at 691 (citing *In re Taras*, 136 B.R. 941, 949, 950 (Bankr. E.D. Pa. 1992)) (until Third Circuit holds otherwise, *Dewsnup* does not affect bankruptcy court's duty to follow Third Circuit's construction of § 506 in *Wilson*, in allowing debtors to bifurcate mortgagee's claims).

<sup>535</sup> 113 S.Ct. 2187 (1993).



close on the property, in which case the arrearages and the lender's costs and attorney's fees would become due and payable immediately. These documents, however, did not explicitly require interest to be paid on such amounts.<sup>536</sup>

Because the debtors' proposed plans did not provide for the payment of such interest, William Wade, the assignee of the debtors' promissory notes and also their trustee in bankruptcy, objected to the confirmation of their plans. Wade argued that under § 506(b), as interpreted by *Ron Pair*,<sup>537</sup> his nonconsensual oversecured claim was entitled to postpetition interest. He derived further support from § 1325(a)(5), which permits a chapter 13 plan to be "crammed down" (*i.e.*, confirmed) over the objections of the holder of an allowed secured claim if that creditor is allowed to retain its lien on the collateral and if the plan pays the creditor "value, as of the effective date of the plan, . . . not less than the allowed amount of such claim."<sup>538</sup> The latter condition has been interpreted as requiring the payment to the creditor of the present value of his claim, including postpetition interest.<sup>539</sup>

The bankruptcy court held in each case, and the district court affirmed (after the cases were consolidated for appeal), that Wade was not entitled to such interest in the absence of an explicit provision of such interest by the mortgage instruments themselves.<sup>540</sup> Further, § 506(b)<sup>541</sup> and § 1325(a)(5) were inap-

<sup>536</sup> *Id.* at 2189; *Wade v. Hannon*, 968 F.2d 1036,1037 (10th Cir.1992)

<sup>537</sup> *Id.* at 2189; *Wade*, 968 F.2d at 1037.

<sup>538</sup> An alternative condition for cram-down is for the debtor to surrender the collateral to the creditor, under § 1325(a)(5)(C).

Section 1325(a) provides that

(a) Except as provided in subsection (b), the court shall confirm a plan if—

(5) with respect to each allowed secured claim provided for by the plan—

(A) the holder of such claim has accepted the plan;

(B)(i) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to the holder[.]

<sup>539</sup> 968 F.2d at 1037, citing *Memphis Bank & Trust Co. v. Whitman*, 692 F.2d 427 (6th Cir. 1982). See also *Rake*, 113 S.Ct. at 2191 (all parties, and the United States as *amicus*, agree that § 1325(a)(5)(B) requires payment to holders of allowed secured claims of present value of their claims, which implies payment of interest).

<sup>540</sup> *Rake*, 968 F.2d at 1037. See also *Rake*, 113 S. Ct. at 2189 (quoting district court opinion to effect that § 1322(b)(2) and § 1322(b)(5) "do not alter the contract between the parties governing such matters as interest, if any, to be paid on arrearage.").

plicable to the debtors because § 1322(b)(2) prohibits the modification of "rights of holders of secured claims. . . secured only by a security interest in property that is the debtor's principal residence."<sup>542</sup>

a. *Circuit Court Precedent*

In reversing the lower courts' unpublished decisions, the Tenth Circuit reviewed the five previous court of appeals decisions on the issue,<sup>543</sup> four of which it opposed. It agreed only with the analysis of the Sixth Circuit (the first to have addressed this question), which held that the payment of interest on arrearages did not modify the agreement for the oversecured loan.<sup>544</sup> That court of appeals had observed that under § 1322(b)(5), "notwithstanding [§ 1322(b)(2), a chapter 13 plan] shall provide for the curing of any default. . . ."<sup>545</sup> The payment of interest would be "merely incident to the 'cure,' which is excepted from the rule of section 1322(b)(2)."<sup>546</sup> Nor should § 1322(b)(2) be seen as an exception to a secured creditor's general entitlement to such interest for his oversecured claim under § 506(b) and § 1325(a).<sup>547</sup>

Senior Circuit Judge Celebrezze's dissent from the Sixth Circuit's opinion maintained that it was the mortgage itself that defined the "curing" of a default; unless the instrument contained an explicit provision for the payment of interest on arrearages, to provide such interest would be to modify the parties' bargain and to provide a windfall to the creditor.<sup>548</sup> Moreover, the dissent attacked as "both inappropriate and unpersuasive" the majority's analogy to § 506(b) and § 1325: the mortgagee does not have a secured or unsecured claim, as addressed by those sections, but instead has a security interest in the debtor's principal residence, as specifically addressed by § 1322(b)(2) and (b)(5), and as reflected in the legislative history of those sections.<sup>549</sup>

---

<sup>541</sup> Section 103(a) renders § 506(b) applicable to chapter 13 cases: "Except as provided in [§] 1161, which concerns railroad cases], chapters 1, 3, and 5 of this title apply in a case under chapter . . . 13 of this title."

<sup>542</sup> 11 U.S.C. § 1322(b)(2) (1988).

<sup>543</sup> *Rake*, 968 F.2d at 1038-40.

<sup>544</sup> *Cardinal Fed. Sav. & Loan Ass'n v. Colegrove* (*In re Colegrove*), 771 F.2d 119 (6th Cir. 1985).

<sup>545</sup> 11 U.S.C. § 1322(b)(5) (1988).

<sup>546</sup> *Colegrove*, 771 F.2d at 122.

<sup>547</sup> *Id.*

<sup>548</sup> *Id.* at 123-24 (Celebrezze, J., dissenting).

<sup>549</sup> *Id.* at 124-125 (Celebrezze, J., dissenting) (citing Congressional Record to the effect that § 1322(b)(2) constituted a compromise between counterpart provisions

Rejecting the Sixth Circuit's analysis, the Eleventh Circuit five months later cited legislative history in concluding that § 1322(b)'s treatment of the modification of debts secured by the debtor's home "was intended to create a special exception to section 1325(a)(5)(B), [which itself was] intended for those creditors whose rights may be modified or whose collateral is subject to rapid depreciation."<sup>550</sup> Other courts had read the requirement of § 1325(a)(5)(B), that the plan provide a secured creditor with "value, as of the effective date of the plan," as calling for the payment to oversecured creditors of interest on past due installments. The Eleventh Circuit, though, found this section inapplicable to residential mortgages.<sup>551</sup> If the lenders had wanted to receive such interest, they could have incorporated a provision to this effect into their contracts; indeed, § 1322(b)(2) would have prevented the modification of such an arrangement.<sup>552</sup>

The Third Circuit agreed with the Eleventh Circuit in refusing to allow interest on arrearages.<sup>553</sup> Like the dissent from the Sixth Circuit's opinion, this Court found that a "cure" of the debtor's default under § 1322(b)(5), which would reinstate a creditor's contractual rights, did not constitute a "modification" of those rights under § 1322(b)(2), and thus rendered inapplicable the present value test of § 1325(a)(5).<sup>554</sup> Indeed, to require creditors to pay interest on arrearages in contradiction of the terms of the mortgage instrument would "disrupt the [contractual] scheme for cure embodied in § 1322(b)[(5)]."<sup>555</sup> It would also depart from the pre-Code judicial practice, which Congress had not indicated an intent to alter, of "first, enjoining foreclosure, and then permitting cure in accordance with nonbankruptcy

---

in the House bill and Senate amendment on the protection of security interests in a debtor's principal residence). See *supra* note 521 and accompanying text for further discussion of the legislative history of § 1322(b)(2).

<sup>550</sup> *Foster Mortgage Corporation v. Terry* (*In re Terry*), 780 F.2d 894, 896-97 (11th Cir.1985).

<sup>551</sup> *Id.* at 896 (quoting § 1325(a)(5)(B)(ii) and citing *Memphis Bank & Trust Co. v. Whitman*, 692 F.2d 427 (6th Cir. 1982) (section requires debtor to pay interest to oversecured creditor interest on arrearages) and *In re Corliss*, 43 B.R. 176 (Bankr. D. Or. 1984) (same)).

<sup>552</sup> *Id.* at 897.

<sup>553</sup> *Appeal of Capps*, 836 F.2d 773 (3d Cir. 1987).

<sup>554</sup> *Id.* at 776 (citing *In re Roach*, 824 F.2d 1370 (3d Cir. 1987) (legislative history of § 1322(b)(2), as well as similar provisions elsewhere in the Code, indicate that debtor's cure of default was not intended by Congress to modify creditor's rights; thus, chapter 13 debtor's right of redemption of property terminated with creditor's foreclosure judgment)).

<sup>555</sup> *Id.* at 777.

law and the provisions of the contract.”<sup>556</sup> In short, the specific provisions of § 1322(b) for home mortgagees would trump those of § 1325(a)(5)(B)(ii) for secured creditors in general.<sup>557</sup>

Similarly, after distinguishing between cure and modification, the Fourth Circuit, the first court of appeals to address this issue after the *Ron Pair* decision, proceeded to find *Ron Pair* irrelevant to the mortgage cure situation.<sup>558</sup> The Supreme Court had in *Ron Pair* interpreted § 506(b) to allow oversecured creditors to incorporate into the secured portion of their claims the late charges and attorney’s fees that had been provided for in the agreement, as well as interest. These interest amounts would become part of the creditor’s secured claim whether or not the written agreement between the creditor and debtor had provided for such interest (indeed, whether or not such an agreement had ever existed). However, to the Fourth Circuit the adherence to the mortgage agreement in the cure process rendered “[t]he valuation of the claim or the collateral [under § 506]. . . simply immaterial.”<sup>559</sup> Unlike the other courts of appeals that had faced the issue, the Fourth Circuit reviewed the caselaw and statutes of the relevant state to determine whether they independently required the payment of interest on arrearages; however, this search proved fruitless.<sup>560</sup>

The Ninth Circuit followed the analyses of the Third, Fourth and Eleventh Circuits, and of the Sixth Circuit’s dissent, in denying interest on arrearages to oversecured mortgagees with no contractual right to such interest.<sup>561</sup>

#### b. *The Tenth Circuit’s Opinion*

Contrary to “thirteen of the fifteen judges who have decided this issue at the circuit level, and . . . the writer of the principal treatise on bankruptcy law,”<sup>562</sup> the Tenth Circuit found it “incon-

---

<sup>556</sup> *Id.* at 777 n.9. See also *infra* note 562.

<sup>557</sup> *Id.* at 777.

<sup>558</sup> *Landmark Financial Services v. Hall*, 918 F.2d 1150,1154 (4th Cir. 1990).

<sup>559</sup> *Id.* at 1155.

<sup>560</sup> The court concluded that “[t]he decision to rely on state law . . . does not simplify the matter because we can uncover nothing in the statutes or case law of Virginia which clearly governs the situation involving interest on mortgage arrearages.” *Id.*

<sup>561</sup> *Shearson Lehman Mortgage Corporation v. Laguna (In re Laguna)*, 944 F.2d 542 (9th Cir. 1991), *cert. denied*, 112 S. Ct. 1577 (1992).

<sup>562</sup> *Rake*, 968 F.2d at 1040 (citing COLLIER ON BANKRUPTCY, ¶ 1322.90[04], at 1322-23, 1324). The Tenth Circuit quoted this commentary:

[Section] 1322(b)(5) was intended to codify the practice under which foreclosure was enjoined during the pendency of a Chapter XIII plan

gruous and at odds with the Supreme Court's recent admonitions to us on how we are to read and construe statutes" to deny over-secured creditors interest on arrearages.<sup>563</sup>

First, the court held that a debtor's cure of default under § 1322(b)(5) *was* a modification of the creditor's rights under § 1322(b)(2), since it thwarted the mortgage's acceleration clause, denied the mortgagee the right to foreclose, and subverted the mortgage's provision that all payments in default were immediately due and payable.<sup>564</sup> Because the Third and Eleventh Circuits had acknowledged that the process of cure did in fact affect the mortgagees' rights, the Tenth Circuit could only conclude that they "must be using modification as a term of art [without] explain[ing] the basis for creating or defining this term of art."<sup>565</sup> Nor did these decisions clearly differentiate between

---

under the former Bankruptcy Act, with the debtor given a reasonable amount of time to cure defaults. Since that cure occurred under applicable nonbankruptcy law, the interest and costs to which the mortgagee was entitled were determined under applicable nonbankruptcy law. Nothing in the Code or its legislative history indicates any intent to alter those rights where a cure is effectuated under section 1322(b)(5).

... The present value tests [of § 1325(a)] compensate creditors whose rights have been modified by reductions in payments, interest charges or the total amount due; where a default is cured, however, the creditor's rights are not modified. Since the contract terms remain in force (except for the injunction against foreclosure), the time value of money is irrelevant. The creditor receives the interest, charges and costs to which it is entitled under the contract and applicable nonbankruptcy law. Typically, the creditor is not entitled under its contract to receive interest on previously accrued interest (compound interest) or on attorneys' fees and costs, as would result under the *Colegrove* Court's decision.

*Id.* The Third, Fourth, and Ninth Circuits had cited this analysis as support for their own reading of sections 1322(b)(5) and 1325(a). *Laguna*, 944 F.2d at 545 ("No other circuit has adopted the majority's reasoning in *Colegrove*, and it has been strongly criticized by the leading bankruptcy treatise as well"); *Landmark Financial Services*, 918 F.2d at 1155 (mortgagee receives only the interest and other charges to which it is entitled under mortgage agreement and applicable nonbankruptcy law); *Capps*, 836 F.2d at 775 (creditor receives interest, charges and costs to which it is entitled under contract and under applicable nonbankruptcy law) and *id.* at 777 n.9 (cure historically rested on contractual provisions and on nonbankruptcy law).

<sup>563</sup> *Id.* (citing *Patterson*, 112 S. Ct. at 2242).

<sup>564</sup> *Id.* Contradicting mortgage instruments that require immediate repayment of any arrearages, § 1322(b)(5) allows the plan to "provide for the curing of any default within a reasonable time."

<sup>565</sup> *Id.* (citing *Terry*, 780 F.2d at 896 ("residential mortgages that would otherwise permit the lender to declare the entire debt presently due, may be *modified* by the plan to cure the default and reinstate regular installment payments")) (emphasis added) and *Capps*, 836 F.2d at 776-77 (creditor may be "adversely affected to some

granting interest on arrearages, which had been regarded as a modification, and affecting contractually-determined cure periods, acceleration clauses, and foreclosure rights, which had not been so perceived.<sup>566</sup>

Second, the Tenth Circuit rejected the argument that in a cure situation under § 1322(b)(5) a mortgagee's right to interest on arrearages was predicated on the contract's terms and on nonbankruptcy law. The cure process itself modified material terms of the contract: "[i]t seems wholly unreasonable to eviscerate the contract provisions of acceleration and foreclosure and then find binding the absence of a term regarding interest on arrearages."<sup>567</sup> Nor could the relegation of the residential mortgagee to contractual remedies be premised on the mortgagee's having, as the Sixth Circuit's dissent had found,<sup>568</sup> a mere "security interest" rather than a "claim": both § 1322(b)(2)<sup>569</sup> and § 1322(b)(5) referred to the residential mortgagee's "claim." Moreover, *Ron Pair* had construed § 506(b) to require that the debtor pay postpetition interest on an oversecured creditor's claim even if the contract did not provide for such interest (and in fact, even if the lien was noncontractual); and there was no indication that Congress had intended to treat home mortgage claims differently.<sup>570</sup>

Finally, the Court faulted those decisions that had analyzed the legislative history of § 1322 in this context, for not having first determined that such inquiry was justified by the the statute's ambiguity.<sup>571</sup> The Tenth Circuit itself found no such ambi-

---

degree by a bankruptcy and a plan of the kind here proposed," but these "incidental adverse effects . . . were regarded by Congress as insignificant when compared with the adverse effects of modifications and other aspects of the bankruptcy laws.").

<sup>566</sup> *Id.* at 1040-41.

<sup>567</sup> *Id.* at 1041.

<sup>568</sup> See *supra* notes 548-49 and accompanying text.

<sup>569</sup> *Id.* at 1041.

Section 1322(b)(2) refers to the modification of "the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence. . . ." (emphasis added)

Section 1322(b)(5) allows a plan to "provide for the curing of any default within a reasonable period of time and maintenance while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due." (emphasis added).

<sup>570</sup> *Id.* at 1041.

<sup>571</sup> *Id.* (citing *Toibb*, 111 S. Ct. at 2200 (although court appropriately may refer to statute's legislative history to resolve statutory ambiguity, there is no need to do so where language of statute is not unclear)). See also *supra* note 140 and accompanying text.

guity: in its reading, § 1322(b)(2) prohibited modification of the amounts of future payments, the interest rates, or the term of the mortgage note, while the cure provision of § 1322(b)(3) authorized the modification, under a chapter 13 plan, of the note's provisions for payment of arrearages.<sup>572</sup> Indeed, recourse to the legislative history would have been unavailing, since "we find no reference to interest or arrearages, or anything that would require [residential mortgagees] to be treated less charitably than other oversecured creditors."<sup>573</sup>

## 2. Finding the "Most Natural" Meaning

In affirming the Tenth Circuit's allowance of interest on arrearages, the Supreme Court used "plain meaning" techniques first to subordinate § 1322(b) to § 506(b), thereby allowing preconfirmation interest, and then to harmonize § 1322(b) with § 1325(a)(5), thus allowing postconfirmation interest.

The Court began its analysis by reviewing *Ron Pair's* conclusion that § 506(b) by its literal terms "directs that postpetition interest be paid on *all* oversecured claims,"<sup>574</sup> to the extent of the value of the collateral,<sup>575</sup> until the chapter 13 plan's confirmation or effective date.<sup>576</sup> Because the arrearages owed on the mortgages were "plainly" included in the trustee's oversecured claims, "[u]nder the unqualified terms of § 506(b), [the trustee] is entitled to preconfirmation interest on these arrearages."<sup>577</sup> Nor did § 1322(b)(5)'s provisions for the curing of defaults prohibit the inclusion of such preconfirmation interest in the allowed amount of the arrearages to be cured under the plan. Thus, the Court reconciled the two sections: "We generally avoid construing one provision in a statute so as to suspend or supersede another provision."<sup>578</sup>

Next, the Court examined the "plain language of the Code"

---

<sup>572</sup> *Id.* at 1042.

<sup>573</sup> *Id.* The Court noted that *Ron Pair's* own examination of postpetition interest had found no guidance in the Code's legislative history. *Id.*

<sup>574</sup> *Rake*, 113 S. Ct. at 2191 (quoting *Ron Pair*, 489 U.S. at 245).

<sup>575</sup> *Id.* at 2187 n.4 (quoting *United Savings Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 372 (1988) (§ 506 denies oversecured creditors postpetition interest to extent that such interest, when added to principal amount of claim, will exceed value of collateral.)).

<sup>576</sup> *Id.* See also *id.* at 2187 (citing 3 COLLIER ON BANKRUPTCY ¶ 506.05, 506-43, and n.5c to this effect, and observing that parties agreed that rights granted under § 506(b) are relevant only until confirmation of plan).

<sup>577</sup> *Id.* at 2191.

<sup>578</sup> *Id.* at 2192.

to dispose of the debtors' argument that § 1322(b) had been intended by Congress to exempt residential mortgage claims from the present value calculation of § 1325(a)(5)(B).<sup>579</sup> Section 1325(a)(5) was by its terms applicable to "each allowed secured claim provided for by the plan."<sup>580</sup> Determining that "[t]he most natural reading of the phrase to 'provid[e] for by the plan' is to 'make a provision for' or 'stipulate to' something in a plan,"<sup>581</sup> the Court found that the debtors' chapter 13 plans had specifically "provided for" the payment of the arrearages.<sup>582</sup> The trustee was thus entitled to interest on the arrearages under the "present value" analysis of § 1325(a)(5)(B)(ii).<sup>583</sup> This conclusion was also supported by a close reading of another provision of the Code. Although § 1328(a) provides generally for the "discharge of all debts provided for by the plan,"<sup>584</sup> § 1328(a)(1) excerpts from discharge claims "provided for under section 1322(b)(5) of this title."<sup>585</sup> As the Court observed, this exception would be unnecessary unless claims subject to § 1322(b)(5) had been considered to be "provided for by the plan."<sup>586</sup>

With this opinion, the Court's "plain meaning" bankruptcy decisions of the 1922-93 term came to a close.

### III. INTERNAL AMBIGUITIES OF THE "PLAIN MEANING" APPROACH

"[H]ere's a question for you. How old did you say you were?"

Alice made a short calculation, and said "Seven years and six months."

---

<sup>579</sup> *Id.* See *supra* note 554 and accompanying text.

<sup>580</sup> 11 U.S.C. § 1325(a)(5) (1988).

<sup>581</sup> *Rake*, 113 S. Ct. at 2192 (citing AMERICAN HERITAGE DICTIONARY 1053 (10th ed. 1982) ("provide for" defined as "to make a stipulation or condition")).

<sup>582</sup> "While payments of principal and interest on the underlying debts were simply 'maintained' according to the terms of the mortgage documents during the pendency of petitioners' cases, each plan treated the arrearages as a distinct claim to be paid off within the life of the plan pursuant to repayment schedules established by the plans." *Id.* at 2192-93.

<sup>583</sup> *Id.* at 2193. In this connection, the Court accepted the Tenth Circuit's conclusions that a cure of a default under § 1322(b) does constitute a modification of the mortgagee's contractual rights and that Congress did not intend § 1322(b)(2) to be construed as a special exception for holders of home mortgage claims from the "present value" cramdown provision of § 1325(a)(5)(B)(ii). *Id.* at 2193 n.9.

<sup>584</sup> 11 U.S.C. § 1328(a) (1988).

<sup>585</sup> *Id.* § 1328(a)(1).

<sup>586</sup> *Rake*, 113 S. Ct. at 2193.



"Wrong!" Humpty Dumpty exclaimed triumphantly. "You never said a word like it!"

"I thought you meant 'How old *are* you?' " Alice explained.

"If I'd meant that I would have said it," said Humpty Dumpty.

Alice didn't want to begin another argument, so she said nothing.

"Seven years and six months!" Humpty Dumpty repeated thoughtfully. "An uncomfortable sort of age! Now if you'd asked *my* advice, I'd have said 'Leave off at seven' — but it's too late now."<sup>587</sup>

In the four terms since the Court decided *Ron Pair*,<sup>588</sup> its conflicting hermeneutic approaches have left unsettled not only the contextual basis for construing the Code's literal meaning but also the conditions under which the statute's legislative history may appropriately be reviewed. Although ostensibly a significant step towards judicial predictability,<sup>589</sup> the "plain meaning" approach has proven to be less a cohesive, coherent method of statutory interpretation than a loose collection of principles, which themselves may often be breached.<sup>590</sup>

The Court's "plain meaning" analysis can be seen as incorpo-

---

<sup>587</sup> LOOKING GLASS, *supra* note 1, at 265-66.

<sup>588</sup> The *Ron Pair* decision was handed down on February 22, 1989.

<sup>589</sup> See *Pioneer Investments*, slip op. at 16 (to dissent, "indeterminacy [of the majority's test for 'excusable neglect'] not only renders consistent application unlikely but also invites unproductive recourse to appeal"); *Patterson*, 112 S. Ct. at 2250 (Justice Scalia concurrence welcoming Court's return to "neutral and rational interpretive methodology"); *Taylor*, 112 S.Ct. at 1648 ("[d]eadlines may lead to unwelcome results, but they prompt parties to act and they produce finality"); *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting) (Scalia dissent foreseeing "destruction of predictability" under majority's scheme of analysis); *Wolas*, 112 S. Ct. at 534 (Scalia, J., concurring) (Scalia concurrence observing that "the plain text of the statute should have made this litigation unnecessary and unmaintainable").

<sup>590</sup> See Charles J. Tabb & Robert M. Lawless, *Of Commas, Gerunds, and Conjunctions: The Bankruptcy Jurisprudence of the Rehnquist Court*, 41 SYRACUSE L. REV. 823, 880 (1991) (recent emphasis on textualism has led to "the lack of a consistent jurisprudence in the Court's bankruptcy decisions . . . [T]he Rehnquist Court appears to drift from bankruptcy decision to bankruptcy decision."). These commentators question another's suggestion that textualism produces greater predictability: "such an argument can only be accepted if one also accepts the somewhat dubious premise that the diverse persons that make up this nation's federal judiciary should, and can, interpret language in an identical manner." *Id.* at 881 (citing Adam J. Wiensch, Note, *The Supreme Court, Textualism, and the Treatment of Pre-Bankruptcy Code Law*, 79 GEO. L.J. 1831, 1857-58 (1991) (consistent use of textualist approach reduces uncertainty over how bankruptcy courts will decide issues, and develops "bright line rules"))).

rating material from six realms of relevance, each progressively more inclusive and farther removed from the literal meaning of the code section in question. Each level of this inquiry, contains inherent ambiguities and contradictions.

A. *The Six Stages of "Plain Meaning"*

1. One Subsection's Language in a Vacuum

At the most basic level, the "plain meaning" approach concerns the significance of the language of a single word or phrase in a Code subsection, without reference to any other Code section or subsection, any other statute, or any legislative history, judicial precedent, or commercial practice. However, the richness of the interconnections between Code provisions, and the frequent interaction between the Code and other statutes, renders such analytical purity unlikely. In *Barnhill*, for example, the Court's endorsement of the "date of honor" rule for identifying preferential transfers by check hinged on its reluctance to embrace "a near-limitless expansion of the term 'conditional' " in the Code's definition of "transfer."<sup>591</sup> Yet before narrowing its focus to this point, the Court had reviewed another subsection of the Code and a provision of the U.C.C., as well as the legislative history of a third Code subsection.<sup>592</sup>

Moreover, the Court is divided over the quantum of statutory language to be subjected to "plain meaning" analysis. In *Dewsnup*, the majority unpacked § 506(d)'s phrase, "allowed secured claims," reading it "term-by-term to refer to any claim that is, first, allowed, and, second, secured."<sup>593</sup> The dissent, however, read the phrase in its entirety, attributing to it the meaning found in other Code sections.<sup>594</sup> This disagreement is also evident in the question of whether specific phrases constitute terms of art. For example, in *Pioneer Investment*, the Court began its interpretation of Rule 9006(b)(1)'s phrase, "excusable neglect," by first analyzing a *collegiate* dictionary's definition of "neglect"; by contrast, the dissent based its arguments on a *legal* dictionary's definition of "excusable neglect" as that phrase had emerged over centuries of caselaw.<sup>595</sup> In *Nobelman*, the circuit court of ap-

---

<sup>591</sup> *Barnhill*, 112 S. Ct. at 1391.

<sup>592</sup> *See supra* at 354-60.

<sup>593</sup> *Dewsnup*, 112 S. Ct. at 777.

<sup>594</sup> *Id.* at 778 n.3.

<sup>595</sup> *Pioneer Investment*, 113 S. Ct. at 1494-95. Interestingly, the Court did not review that dictionary's definition of "excusable." *See id.* at 1502 (O'Connor, J., dissenting).

peals appeared to diverge over the use of the word "modification" as a term of art.<sup>596</sup>

## 2. Within One Section

On a second level of inquiry, controversy has marked the Court's decisions concerning whether the same phrase is to be interpreted similarly in separate subsections of the same Code section. *Ron Pair*<sup>597</sup> and *Wolas*<sup>598</sup> viewed subsections through the lens of the purpose and language of the section containing them. However, in *Dewsnup*, Justice Scalia's dissent excoriated the majority's "one-subsection-at-a-time approach to statutory exegesis;"<sup>599</sup> and in *Barnhill*, Justice Stevens found "nothing in [their] structure or purpose" to justify a distinction between § 547(b)'s and § 547(c)'s meaning of "transfer."<sup>600</sup>

Nor does the Court's approach to grammatical questions encourage predictability. In restricting lien-stripping of home mortgages in chapter 13 proceedings, *Nobelman* jettisoned the "rule of the last antecedent," under which an ambiguous clause would be taken to refer to the immediately preceding clause. The Court "acknowledge[d] that this reading of the clause is quite sensible as a matter of grammar. But it is not compelled."<sup>601</sup> The majority championed own interpretation less than warmly, as "also plausible" and as "more reasonable" than an alternative construction.<sup>602</sup>

## 3. Across Different Sections

The method of inter-section comparison of the Code's connotations has been no better established. At least one Justice has recognized that, although "[n]ormally, we assume that the same terms have the same meaning in different sections of the same statute. . . . [t]hat rule is not inexorable . . . ."<sup>603</sup> Indeed, although *Ron Pair*<sup>604</sup> and *Patterson*<sup>605</sup> detected congressional in-

---

<sup>596</sup> See *supra* note 565.

<sup>597</sup> *Ron Pair*, 109 S. Ct. at 1031 n.5 (rejecting interpretation of § 506(b) that would bring that subsection into conflict with other subsections of § 506).

<sup>598</sup> *Wolas*, 112 S. Ct. at 532 n.13 (§ 547(c)(2) not intended to codify "current expense" exception to preference rule, because § 547 provided other exceptions to address this concern).

<sup>599</sup> *Dewsnup*, 112 S. Ct. at 781 (Scalia, J., dissenting).

<sup>600</sup> *Barnhill*, 112 S. Ct. at 1393-94.

<sup>601</sup> *Nobelman*, 113 S. Ct. at 2111.

<sup>602</sup> *Id.*

<sup>603</sup> *Id.* at 1393 (Justice Stevens, dissenting) (citations omitted).

<sup>604</sup> *Ron Pair*, 489 U.S. at 242 (had Congress intended § 506(b) to apply only to

tent behind the omission from certain Code sections of provisions that appeared explicitly in others, this negative inference was clearly rejected in *Midlantic*. There, the Court read into the abandonment power an environmental exception that did not appear in § 554's plain language but that *was* an existing exception to the automatic stay.<sup>606</sup>

Code provisions not directly at issue have been cited by both a majority and a dissenting opinion to minimize the apparent threat posed by the Court's interpretation of one section: those sections indicate either that the danger is actually present (and presumably tolerated),<sup>607</sup> or has been addressed,<sup>608</sup> elsewhere in the Code. In *Taylor*, the Court noted the range of Bankruptcy Rules and Code provisions that would counter a debtor's option to declare all of his property exempt.<sup>609</sup> Justice Scalia's dissent in *Dewsnup* observed that debtors could deny creditors the appreciation in the value of collateral not only by stripping down liens in chapter 7 cases but by applying the "cram-down" provisions of chapter 11 or chapter 13.<sup>610</sup>

Also thrown into doubt has been the effectiveness of the well-established "rule against superfluity." This principle was most recently endorsed in *Rake*, which honored the Court's tendency "generally [to] avoid construing one provision in a statute so as to suspend or supersede another provision."<sup>611</sup> Yet the fact that *Rake* overruled four courts of appeals suggests that the rule against superfluity is only one of several factors in the interpreta-

---

consensual liens, it could have so indicated by use of phrase "security interest," which Code defines, and uses in other sections for this purpose).

<sup>605</sup> *Patterson*, 112 S. Ct. at 2247 (because Congress has restricted scope of "applicable nonbankruptcy law" to state law with regard to other sections of Code, where it had not indicated such a restriction "applicable nonbankruptcy law" will include federal laws); *id.* at 2250 (Justice Scalia's concurrence, applauding Court's return to principle that "consistency of usage within the same statute is to be presumed").

<sup>606</sup> *Midlantic*, 474 U.S. at 503-04.

<sup>607</sup> *Dewsnup*, 112 S. Ct. at 785 (dissent's observation that appreciation in value of collateral could be denied to creditors not only by stripping down liens in chapter 7 cases but by applying "cram-down" provisions of chapter 11 or chapter 13).

<sup>608</sup> *Taylor*, 112 S. Ct. at 1648 (indicating the range of Bankruptcy Rules and Code provisions that would minimize threat that debtor would declare all her property exempt).

<sup>609</sup> *Id.*

<sup>610</sup> *Dewsnup*, 112 S. Ct. at 785 (Scalia, J., dissenting).

<sup>611</sup> *Rake*, 113 S. Ct. at 2192. *Cf.* *Connecticut Nat'l Bank v. Germain*, 112 S. Ct. 1146, 1149 (1992) ("Redundancies across statutes are not unusual events in drafting, and so long as there is no 'positive repugnancy' between two laws . . . a court must give effect to both"; since giving effect to both provisions at issue would not render either wholly superfluous, rule against superfluity did not apply).

tion of the Code, and that the judgment that one provision is being interpreted to suspend or supersede another may vary with the observer. Similarly, in *Patterson* the Court overturned the decisions of two circuits by finding that a broad interpretation of § 541(c)(2) would not render superfluous § 522(d)(10)(E)'s limited federal exemption for a debtor's interest in ERISA-qualified plans.<sup>612</sup>

Indeed, in *Kelly*, the dissent proposed that the majority had violated this rule. To these two Justices, the finding that the debtor's restitution payments were made to and for the benefit of the state was justified in the case before the Court only because the victim was a governmental unit. If the Court was in fact adopting the broader principle that *any* restitution payment, to *whomever* made, was to or for the benefit of the government, it would be removing any independent meaning from this element of nondischargeability under § 523(a)(7).<sup>613</sup>

#### 4. In the Context of the Code's Policies

The fourth stage of "plain meaning" analysis involves consideration of the policies underlying the Bankruptcy Code. Although *Patterson* suggested that "policy considerations [might not even be] relevant where the language of the statute is . . . clear,"<sup>614</sup> the Court has often confronted the intrinsic conflicts among the Code's goals. In *Davenport*, the Justices were reluctant to disturb the existing balance between incentives for debtors to seek the protectional chapter 7 rather than chapter 13.<sup>615</sup> Examining in *Wolas* the "sometimes conflicting policies" underlying the preference provisions, they concluded that "[w]hether Congress has wisely balanced [them] is not a question that we are authorized to decide."<sup>616</sup> The policy factor extends to the projected use and users of the Code itself: attacking the majority's prohibition of lien-stripping in chapter 7 proceedings, Justice

---

<sup>612</sup> *Patterson*, 112 S. Ct. at 2248-49.

<sup>613</sup> *Kelly*, 107 S. Ct. at 363 n.3.

<sup>614</sup> *Patterson*, 112 S. Ct. at 2249.

<sup>615</sup> *Davenport*, 495 U.S. at 563.

<sup>616</sup> *Wolas*, 112 S. Ct. at 533. The preference policies are: (1) to prevent creditors from "racing to the courthouse to dismember the debtor during his slide into bankruptcy" and, (2) "more important," to distribute the debtor's assets equally among creditors. *Id.* See Wiensch, *supra* note 590, at 1855-56 (One "reason supporting the Court's textualist approach is that the Court strikes a carefully crafted balance among competing interests."); see also *id.* at 2856 (citing *Ron Pair*, 489 U.S. at 245-46 ("Congress expressly chose to create . . . alleged tension" by enacting, in the face of policy of equal payments, provisions of Code regarding payments of interest only to oversecured creditors.)).

Scalia in *Dewsnup* emphasized that to allow such strip-downs would not thereby render chapter 7 more attractive to debtors than chapter 13.<sup>617</sup>

This stage of inquiry also includes arguments based on existing commercial practice, to the extent that it can be argued that the Code should not deprive the debtor and creditors of the benefit of their bargain. The *Dewsnup* decision was based in part on the principle that a court should not rewrite mortgages that had been negotiated and executed prepetition.<sup>618</sup> Similarly, in *Nobelman*, the Court referred to *Dewsnup* in defining the creditor's rights by reference to the terms of the home mortgage at issue, as construed and enforceable under state law; since these rights would be modified if the undersecured mortgage lien were stripped down, § 1322(b)(2) prohibited the debtor from reducing the creditor's claim.<sup>619</sup> However, this policy has not always carried the day. In *Barnhill*, Justice Stevens's dissent cited "established business practices in the business community" in favoring the "date of delivery" rather than the "date of honor" rule for preference purposes.<sup>620</sup> More recently, *Rake*'s expansive interpretation of § 1325(a)(5) allowed oversecured home mortgagees interest on arrearages even though such interest had not been provided for in the mortgage instruments.<sup>621</sup>

##### 5. In Conjunction with Extra-Code Policies

On the fifth level of abstraction, the Court may look outside the Code and bankruptcy policies to the goals of other statutes, both federal and state. For example, in *Midlantic*, the Court observed that statutes enacted after the Code indicated Congress's environmental concerns.<sup>622</sup> In *Kelly*, the Court bowed to the policy that "federal bankruptcy courts should not invalidate the results of state criminal proceedings" or affect those courts' choice of alternatives among imprisonment, fines and restitution.<sup>623</sup> In *Patterson*, the Court emphasized that lenders should be given no

---

<sup>617</sup> *Dewsnup*, 112 S. Ct. at 785-85. Cf. Tabb & Lawless, *supra* note 590, at 878 (faulting *Toibb* for failing to discuss policy issues, in light of issues regarding "the ability of overloaded bankruptcy courts to accommodate square-peg individual chapter 11 petitions in the round hole of the courts' dockets.").

<sup>618</sup> *Dewsnup*, 112 S. Ct. at 778.

<sup>619</sup> *Nobelman*, 113 S. Ct. at 2110. This constituted the *Nobelman* Court's only reference to *Dewsnup*.

<sup>620</sup> *Barnhill*, 112 S. Ct. at 1392 (Stevens, J., dissenting).

<sup>621</sup> *Rake*, 113 S. Ct. at 2189.

<sup>622</sup> *Midlantic*, 109 S. Ct. at 762-63.

<sup>623</sup> *Ron Pair*, 479 U.S. at 4749.

incentive to file involuntary petitions against borrowers in order thereby to reach their pension interests more easily, and that ERISA's protection of pension benefits should not be withheld from debtors.<sup>624</sup> And in *Pioneer Investment*, the Court analogized to various Federal Rules of Civil Procedure to construe the "excusable neglect" provision of Bankruptcy Rule 9006(b)(1).<sup>625</sup>

#### 6. Consideration of Equities

Finally, the Court may review the equities of the matter. In particular, § 105 authorizes a bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Code]."<sup>626</sup> The Court has not been eager to address the implications of this provision.<sup>627</sup> In *Taylor*, though holding that all objections to a debtor's claimed exemptions must be filed within the statutorily prescribed period, whether or not they are justified by the Code or even asserted in good faith by the debtor, the Court refused on procedural grounds to consider the application of § 105. In fact, Justice Stevens's lone dissent suggested that consideration of the equities would lead the Court to "readily ignore what it treats as the insurmountable barrier of 'plain meaning.'" <sup>628</sup>

The tables were turned in *Pioneer Investment*, where the Court explicitly rejected a strict reading of Rule 9006(b)(1)'s "excusable neglect," adopting instead a more lenient construction because "the determination at bottom is an equitable one, taking account of all relevant circumstances surrounding the party's omission."<sup>629</sup> In her dissent, Justice O'Connor specifically objected to the "indeterminacy [of the majority's test, which] not only renders consistent application unlikely but also invites unproductive recourse to appeal."<sup>630</sup>

#### B. Recourse to Legislative History

Reinforcing the textual emphasis of its "plain meaning" approach is the Court's reticence towards examining the legislative

---

<sup>624</sup> *Patterson*, 112 S. Ct at 2248-50.

<sup>625</sup> *Pioneer Investment*, 113 S. Ct. at 1496-97.

<sup>626</sup> 11 U.S.C. § 105 (1988).

<sup>627</sup> See Wiensch, *supra* note 590, at 1859 (perceiving textualist approach as a product of "the Court's increasingly narrow view of the equitable powers of the bankruptcy courts.").

<sup>628</sup> *Taylor*, 112 S. Ct. at 1652 (Stevens, J., dissenting).

<sup>629</sup> *Pioneer Investment*, 113 S. Ct. at 1498.

<sup>630</sup> *Id.* at 1504 (O'Connor, J., dissenting).

history of Code sections. Like the "plain meaning" approach itself, the Court's restrictions on the relevance of legislative history have had an uncertain development.

### 1. Tacit Incorporation of Pre-Code Precedent

In two early cases, the Court construed the literal meaning of the Code in the light of pre-Code precedent, under the "normal rule of statutory construction . . . that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific."<sup>631</sup> *Midlantic* cited pre-Code precedent in support of its imposition of environmental restrictions on the simple language of the Code provision concerning abandonment. Yet the dissent observed that this body of precedent consisted of only three decisions, which, even if relevant, could not be presumed to have come to the attention of Congress when it drafted the Code.<sup>632</sup> In *Kelly*, the issue was not the substantiality but the effect of the precedent: the Court inferred congressional agreement with pre-Code precedent that had actually *contradicted* the explicit language of the earlier Bankruptcy Act.<sup>633</sup> *Kelly* noted that any intention for the Code to deviate from this precedent would have been reflected in the statute's legislative history.<sup>634</sup>

*Ron Pair* attempted to restrict the application of legislative history to the interpretation of "statutory language which, at least to some degree, [is] open to interpretation,"<sup>635</sup> where "under the proposed interpretation, [the Code provision is] in clear conflict with state or federal laws of great importance."<sup>636</sup> However, the Court indicated neither the requisite degree of ambiguity that could exist, nor the criteria for a "clear conflict," nor the factors that would qualify laws as of "great importance." (Presumably, any issue on which the circuit courts of appeal had split would qualify, Justice Scalia's disappointment with the prev-

---

<sup>631</sup> *Midlantic*, 474 U.S. at 501.

<sup>632</sup> *Id.* at 512 (Rehnquist, J., dissenting).

<sup>633</sup> *Kelly* 479 U.S. at 45-47.

It is questionable whether the explicit tilt of the present Court, at least in theory, towards the "plain meaning" of the Code will prevent current drafters of Code revisions from arguing that Congress, in enacting these measures, will be deemed to have approved tacitly of existing bodies of opinions that diverge from this literal approach to the current statutory language.

<sup>634</sup> *Id.* at 51.

<sup>635</sup> *Ron Pair*, 109 S. Ct. at 1032.

<sup>636</sup> *Id.*



alent "legal culture"<sup>637</sup> notwithstanding.) In fact, in *Toibb*, Justice Stevens's dissent suggested, without citing the *Ron Pair* test, that the majority's logical interconnection of various Code sections to extend chapter 11 protection to individuals could be undone by a simple ambiguity that would broaden the scope of inquiry to include both other Code provisions and the Code's legislative history.<sup>638</sup>

Curiously, in *Wolas* Justice Stevens himself engaged in an extended analysis of the legislative history of § 547, construing *Ron Pair* as indicating that, "[g]iven the clarity of the statutory text, respondent's burden of persuading us that Congress intended to create or preserve a special rule for long-term debt is exceptionally heavy."<sup>639</sup> Indeed, in the face of straightforward statutory text,<sup>640</sup> *Ron Pair* would have precluded an examination of legislative history, especially where the proposed interpretation — here, that payments on long-term as well as short-term debt qualify for the ordinary course of business exception to the trustee's power to avoid preferences — is not "in clear conflict with state or federal laws of great importance."<sup>641</sup> The Court's indulgence in this analysis is all the more puzzling given its enunciation in *Wolas* of the general principle that "[t]he fact that Congress may not have foreseen all of the consequences of a statutory enactment is not a sufficient reason for refusing to give effect to its

---

<sup>637</sup> See *Patterson*, 112 S. Ct. at 2250 (ability of three courts of appeals to interpret "applicable bankruptcy law" as excluding federal law "calls into question whether our legal culture has so far departed from attention to text, or is lacking in an agreed-upon methodology for creating and interpreting text, that it any longer makes sense to talk of 'a government of laws, not men.'"); *Wolas*, 112 S. Ct. at 534 ("It is regrettable that we have a legal culture in which such arguments [as the distinction between long-term and short-term debt, where the Code addresses neither] have to be addressed (and indeed are credited by a Court of Appeals). . . .")

<sup>638</sup> Section 109(d) . . . states that "only a person that may be a debtor under Chapter 7 . . . may be a debtor under Chapter 11. . . ." (Emphasis added.) It does not, however, state that every person entitled to relief under Chapter 7 is also entitled to relief under Chapter 11. In my judgment, the word "only" introduces sufficient ambiguity to justify a careful examination of other provisions of the Act [adopting the Code], as well as the legislative history.

*Toibb*, 111 S. Ct. at 2202 (Stevens, J., dissenting).

<sup>639</sup> *Wolas*, 112 S. Ct. at 530 (citing *Ron Pair*, 489 U.S. at 241-42).

<sup>640</sup> Justice Scalia's concurrence found the statute "utterly devoid of language that could remotely be thought to distinguish between long-term and short-term debt." *Id.* at 534 (Scalia, J., concurring).

<sup>641</sup> *Ron Pair*, 489 U.S. at 245.

plain meaning.”<sup>642</sup>

For its part, *Dewsnup*, in reviewing the legislative history of § 506(d), interpreted *Ron Pair* as indicating that “this 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.”<sup>643</sup> “Of course,” the Court added, “where the language is unambiguous, silence in the legislative history cannot be controlling.”<sup>644</sup> But it did not find that § 506(d) met that standard of clarity.<sup>645</sup>

In his dissent, Justice Scalia found that “[a]lmost point for point, today’s opinion is the methodological antithesis of *Ron Pair* — and I have the greatest sympathy for the Court of Appeals who must predict which manner of statutory construction we shall use for the next Bankruptcy Code case.”<sup>646</sup> Not only did *Wolas* indicate that deference should be granted to the congressional redrafting of the provision in question, but in *Ron Pair*, “[h]aving found a ‘natural interpretation of the statutory language [that] does not conflict with any significant state or federal interest, nor with any other aspect of the Code,’ . . . we deemed the pre-Code practice to be irrelevant.”<sup>647</sup>

In *Barnhill*, the Court saw *Toibb* as holding that “appeals to statutory history are well-taken only to resolve ‘statutory ambiguity’”; and it accordingly denied that such ambiguity surrounded the question of whether the “date of honor” or the “date of delivery” should be used for avoidance of transfers by checks as preferences.<sup>648</sup> “But even if legislative history were relevant, the statements on which petitioner relies, by their own terms, apply only to § 547(c), not § 547(b).”<sup>649</sup> In his dissent, Justice Stevens seemed to infer such ambiguity from the unanimity of the courts of appeals decisions that had adopted the “date of delivery” rule for purposes of § 547(c): he noted that these decisions “are consistent with the legislative history, which, though admittedly not conclusive, identifies the date of delivery of a check as the date of

---

<sup>642</sup> *Wolas*, 112 S. Ct. at 531.

<sup>643</sup> *Dewsnup*, 112 S. Ct. at 779.

<sup>644</sup> *Id.*

<sup>645</sup> *Id.*

<sup>646</sup> *Id.* at 787 (Scalia, J., dissenting).

<sup>647</sup> *Id.* (quoting *Ron Pair*, 489 U.S. at 245) (citations omitted).

<sup>648</sup> *Barnhill*, 112 S. Ct. at 1391 (quoting *Toibb*, 111 S. Ct. at 2200).

<sup>649</sup> *Id.*

transfer for purposes of § 547(c)."<sup>650</sup>

The Court in *Patterson* found dispositive the plain meaning of § 541(c)(2)'s reference to "nonbankruptcy law," as including both state and federal law. Although *Toibb* stood for the principle that "courts 'appropriately may refer to a statute's legislative history to resolve statutory ambiguity,'"<sup>651</sup> in *Patterson*, as in *Ron Pair*, that "the clarity of the statutory language [in question] obviates the need for any such inquiry."<sup>652</sup> Moreover, the Court indicated that even if it were to review the legislative materials, it would find no clear indications that the import of the statute was contrary to its plain meaning.<sup>653</sup>

Indeed the "meager excerpts" available "[b]y no means . . . provide a sufficient basis for concluding, in derogation of the statute's clear language, that Congress intended to exclude other state and federal law from the provision's scope."<sup>654</sup>

Each of these three "plain meaning" decisions addressed the connotations of common words or phrases that have not been explicitly redefined by the Code. Perhaps because of the equitable considerations involved in its examination of "excusable neglect", in *Pioneer Investment* the Court delved deeply into "the history of the present bankruptcy rules," without any references to *Toibb* or *Ron Pair*.<sup>655</sup> In *Nobelman*, although the Court's focus on "rights" and on grammatical constructions did not concern the Code's legislative history, Justice Stevens in a one-paragraph concurrence observed that this perspective could resolve the apparent "anomaly" that "the Bankruptcy Code should provide less protection to an individual's interest in retaining possession of his or her home than of other assets."<sup>656</sup> Finally, *Rake*, which was concerned largely with determining the appropriate definitions of "rights," "cure," "modification," and "provide for," did not mention legislative history.<sup>657</sup>

## 2. Utility of Congressional Statements and Reports

Even if legislative history is deemed germane to interpreting the Code, questions remain regarding the extent to which state-

---

<sup>650</sup> *Id.* at 1393.

<sup>651</sup> *Patterson*, 112 S. Ct. at 2248 (quoting *Toibb*, 111 S. Ct. at 2200).

<sup>652</sup> *Id.* (citing *Toibb*, 111 S. Ct. at 2200; *Ron Pair*, 489 U.S. at 241).

<sup>653</sup> *Id.*

<sup>654</sup> *Id.*

<sup>655</sup> *Pioneer Investment*, 113 S. Ct. at 1495.

<sup>656</sup> *Nobelman*, 113 S. Ct. at 2111-12 (Stevens, J., concurring).

<sup>657</sup> *Rake*, 113 S. Ct. at 2187 (1993).

ments made on the floor of Congress, and House or Senate Reports themselves, can be taken to indicate legislative intent. Of the decisions previously analyzed, several have briefly evaluated congressional statements and reports on the Code provisions in question, whether or not such legislative history was formally deemed relevant. Generally, such examinations have produced little direct history, and have thus been useful only to discount allegations of an intent to change pre-Code practice.<sup>658</sup>

In *Hoffman v. Connecticut Dep't of Income Maintenance*,<sup>659</sup> a notably fractured Court held that § 106(c) does not authorize a bankruptcy court to issue a money judgment against a state. Under the relevant law, such a judgment could be effected only if Congress had made "unmistakably clear in the language of the statute" its intention to abrogate the states' Eleventh Amendment immunity from suit in federal court.<sup>660</sup> Justice White's plurality opinion, joined by Chief Justice Rehnquist, Justice O'Connor and Justice Kennedy, rejected as irrelevant legislative history arguments based on floor statements regarding this provision.<sup>661</sup> According to the Court, "[i]f congressional intent is unmistakably clear in the language of the statute, reliance on committee reports and floor statements will be unnecessary, and if it is not, [this textual standard] will not be satisfied."<sup>662</sup>

Justice Stevens, joined by Justice Blackmun, wrote a separate opinion "to explain why the legislative history of § 106 lends ad-

---

<sup>658</sup> *Patterson*, 112 S. Ct. at 2248 (maintaining that House and Senate reports "contain only the briefest of discussions addressing § 541(c)(2)," insufficient to overcome the provisions plain meaning); *Barnhill*, 112 S. Ct. at 1391 (positing that statements on which petitioner relies, by their own terms, apply to different subsections of the Code than are at issue); *Dewsnup*, 112 S. Ct. at 779 (asserting that House report indicates "full understanding of [pre-Code] practice," but not intent to grant broad new remedy to debtor); *Wolas*, 112 S. Ct. at 533 n.14, n.15 (legislative history does not mention rule in question; House Committee Report concludes that pre-Code law is "hopelessly complex," thereby undercutter arguments that Code intended to preserve pre-existing law); *Toibb*, 111 S. Ct. at 2200 (citing "scant legislative history of this precise issue" and "apparently conflicting views" in such history as had been produced); *Ron Pair*, 489 U.S. at 243 n.6 (opining that neither Committee Reports nor statements by managers of legislative discuss relevant question at all) and at 254 (no statement expressing intent to work major change in pre-Code law); *Kelly*, 479 U.S. at 50-51 (noting no indication in House and Senate Reports supporting proposed interpretation).

Some decisions of the Rehnquist Court, however, have addressed in depth the relevance of such legislative history.

<sup>659</sup> *Begier v. U.S.*, 496 U.S. 53, 64 n.5 (1990).

<sup>660</sup> *Id.* at 65 (quoting 124 CONG. REV. at 32417 (remarks of Rep. Edwards)).

<sup>661</sup> *Id.* at 66 (citing H.R. REP. NO. 95-595, 95th Cong., 2d Sess., at 373 (1977), reprinted in 1978 U.S.C.C.A.N. 6329).

<sup>662</sup> *Id.* at 70 (Scalia, J., concurring).

ded support to [the] reading of the statute" that had been advanced in Justice Marshall's dissent, which these two Justices and Justice Brennan had joined.<sup>663</sup> This opinion relied heavily on the floor statements of the House and Senate sponsors (Rep. Edwards and Sen. DeConcini) to the effect that § 106, as proposed, had permitted the bankruptcy courts to bind governmental units or matters other than the amount and dischargeability of tax liabilities owing by the debtor or the estate, and authorized the courts to subject the government to the avoidance of preferential transfers.<sup>664</sup>

The next term, Justice Marshall's majority opinion on the interpretation of § 541 noted that "[b]ecause of the absence of the conference and the key roles played by Representative Edwards and his counterpart floor manager Senator DeConcini, we have treated their floor statements on the Bankruptcy Act of 1978 as persuasive evidence of congressional intent."<sup>665</sup> In particular, because the Code did not specifically address the avoidance of voluntary prepetition payments of trust fund taxes, the Court focused on Representative Edwards' remark that "[t]he courts should permit the use of reasonable assumptions under which the Internal Revenue Service, and other tax authorities, can demonstrate that amounts of withheld taxes are still in the possession of the debtor at the commencement of the case."<sup>666</sup> That "reasonable assumption" was provided in a House Report which indicated that a payment of withholding taxes would generally not be seen as a preference.<sup>667</sup>

Yet Justice Scalia's concurrence, though arriving at the same conclusion though "the standard tools of legal reasoning," attacked the majority's "scouring the legislative history for some scrap that is on point and therefore *ipso facto* relevant, no matter how unlikely a source of congressional reliance or attention).<sup>668</sup> There was no indication in the record he charged, that Representative Edwards's remarks had been heard by anyone except the presiding officer, or even that they had been made on the floor rather than having been retroactively inserted into the Congress-

---

<sup>663</sup> *Id.* at 67-68 (Scalia, J., concurring).

<sup>664</sup> *Id.*

<sup>665</sup> *Id.* at 68 (Scalia, J., concurring).

<sup>666</sup> *Id.* at 69 (Scalia, J., dissenting). The dissent dismissed these documents as "a kind of legislative-history 'rider' that even the most ardent devotees of legislative history should ignore." *Id.*

<sup>667</sup> 112 S. Ct. 1011, 1016 (1992).

<sup>668</sup> To be effective, waivers of the government's sovereign immunity must be "unequivocally expressed." *Id.* at 1014 (citations omitted).

sional Record.<sup>669</sup> Moreover, these statements (on the tracing of tax trust funds for bankruptcy purposes) were not directly relevant to the House proposal at issue.<sup>670</sup> To this Justice, "Congress conveys its directions in the Statutes at Large, not in excerpts from the Congressional Record that do not clarify the text of any pending legislative proposal."<sup>671</sup> In addition, Justice Scalia found it "both demeaning and unproductive for us to ponder whether to adopt literal or not-so-literal readings of Committee Reports, as though they were controlling statutory text."<sup>672</sup>

In *United States v. Nordic Village Inc.*,<sup>673</sup> Justice Scalia, writing for the majority, rejected questions of legislative history as irrelevant to the question of whether § 106(c) imposed mandatory liability on the federal government unambiguously:<sup>674</sup> "if clarity does not exist [in the statutory text], it cannot be supplied by a committee report."<sup>675</sup> However, Justice Stevens' dissent, which was joined by Justice Blackmun, found that the statements of Representative Edwards and Senator DeConcini indicated a "congressional purpose to waive sovereign immunity [that] is pellucidly clear."<sup>676</sup> Unusually, the opinion would have used legislative history to support a *literal* reading of the statute.

#### IV. CONCLUSION

Though the Court's "plain meaning" approach to interpreting the Bankruptcy Code threatens to exclude considerations of legislative history, the gate is not yet closed. The dramatic rise over the last decade in the number and sophistication of bankruptcy filings has brought the Code's myriad ambiguities to the attention of more and higher courts, and has spawned a series of proposals for the statute's revision. Moreover, bankruptcy issues and policies are increasingly colliding with judicial interpretations of recent federal and state enactments in such disparate

---

<sup>669</sup> *Id.* at 1016.

<sup>670</sup> *Id.* at 1018 (citing 124 CONG. REC. 32394 (1978) (statement of Rep. Edwards); 124 CONG. REV. 33993 (statement of Sen. DeConcini) (both to effect that § 106(c) covered, in addition to determination of amounts and dischargeability of debtor's tax liability, matters such as avoidance of preferential transfers)).

<sup>671</sup> 109 S. Ct. 2818 (1989).

<sup>672</sup> *Id.* at 2822 (quoting *Atascadero State Hospital v. Scanlon*, 474 U.S. 234, 242 (1985)).

<sup>673</sup> *Id.* at 2823 (citing statements of Representative Edwards and Senator DeConcini to the effect that "[§] 106(c) permits a trustee or debtor in possession to assert avoiding powers under title 11 against a governmental unit").

<sup>674</sup> *Id.* at 2824.

<sup>675</sup> *Id.* at 2827 (Stevens, J., dissenting).

<sup>676</sup> *Id.* at 2828 (Stevens, J., dissenting).

fields as environmental, tax and labor law.<sup>677</sup>

Against this backdrop, the attempt of the “new literalism” to extract the “natural” sense<sup>678</sup> of a statute that may have “little to do with natural justice”<sup>679</sup> should continue to encourage both carefully-worded legislation and creatively-argued litigation. It remains to be seen, however, whether the Code or the “plain meaning” approach itself will present the greater hermeneutic challenge.

“It seems very pretty,” [Alice] said when she had finished [*Jabberwocky*], “but it’s rather hard to understand!” (You see, she didn’t like to confess, even to herself, that she couldn’t make it out at all.) “Somehow it seems to fill my head with ideas — only I don’t know exactly what they are!”<sup>680</sup>

—Alice, upon reading *Jabberwocky*.

---

<sup>677</sup> See Walter A. Effross, *The “Broken Bench” of Bankruptcy Law*, 44 HARV. L. BULL. 26 (1993).

<sup>678</sup> See *Rake*, 113 S. Ct. at 2192 (identifying “[t]he most natural reading” of § 1325(a)(5)); *Nobelman*, 113 S. Ct. at 1498 (rejecting construction of Rule 9006(b)(1) that “would ignore the most natural meaning of the word ‘neglect’”); *Patterson*, 112 S. Ct. at 2246 (reviewing “[t]he natural reading” of § 541(a)(1)); *Dewsnup*, 112 S. Ct. at 782 (Scalia, J., dissenting) (criticizing majority’s construction of § 506(d) as fostering unnatural reading of that subsection); *Ron Pair*, 489 U.S. at 241, 249 (endorsing “natural reading” of § 506(b)); *Kelly*, 479 U.S. at 44 (considering “most natural construction” of § 63 of Bankruptcy Act).

<sup>679</sup> *Dewsnup*, 112 S. Ct. at 787 (Scalia, J., dissenting).

<sup>680</sup> LOOKING-GLASS, *supra* note 1, at 197.