No. 15-1509

In the Supreme Court of the United States

U.S. BANK NATIONAL ASSOCIATION, TRUSTEE, ET AL., PETITIONERS

v.

THE VILLAGE AT LAKERIDGE, LLC, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING RESPONDENTS

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QUESTION PRESENTED

The Bankruptcy Code, 11 U.S.C. 101 *et seq.*, contains a non-exhaustive list of persons and entities who are considered "insiders" under the Code. Creditors who do not fall within any of the enumerated categories but have a comparably close relationship to the debtor may likewise be treated as insiders. The Code provides that, before a Chapter 11 plan of reorganization may be approved, at least one class of impaired claims must vote in favor of the plan, determined "without including any acceptance of the plan by any insider." 11 U.S.C. 1129(a)(10). The question presented is as follows:

Whether a bankruptcy court's determination of insider status with respect to a particular claimholder should be reviewed de novo or for clear error.

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INTEREST OF THE UNITED STATES

The Attorney General appoints United States Trustees to supervise the administration of bankruptcy cases and trustees throughout the country. 28 U.S.C. 581-589a. United States Trustees "serve as bankruptcy watch-dogs to prevent fraud, dishonesty, and overreaching in the bankruptcy arena," H.R. Rep. No. 595, 95th Cong., 1st Sess. 88 (1977), and they "may raise and may appear and be heard on any issue in any case or proceeding under" Title 11, 11 U.S.C. 307. The United States is also the largest creditor in the Nation, frequently appearing as creditor in Chapter 11 cases. Finally, as a frequent litigant in the federal courts, the United States has a strong interest in the correct application of standards of appellate review.

At the Court's invitation, the United States filed a brief as amicus curiae at the petition stage of this case.

STATEMENT

1. a. Chapter 11 of the Bankruptcy Code (Code) provides for the reorganization of financial obligations of a business enterprise or individual. 11 U.S.C. 1101 *et seq.* Chapter 11 bankruptcies are implemented according to a "plan" (usually, but not always, filed by the debtor, 11 U.S.C. 1121) that assigns to "classes" the various allowed claims against the debtor and specifies the treatment each class of claims shall receive, 11 U.S.C. 1122, 1123. A court generally may confirm a proposed Chapter 11 plan only if each class of creditors "has accepted the plan" or "is not impaired under the plan." 11 U.S.C. 1129(a)(8)(A) and (B); see 11 U.S.C. 1124. The proposed plan must also satisfy more than a dozen other statutory requirements, including that the plan "has been proposed in good faith," that objecting creditors will fare at least as well in reorganization as they would in liquidation, and that the plan is feasible. 11 U.S.C. 1129(a)(3), (7) and (11).

In certain circumstances, the Code authorizes confirmation of a plan that impairs the claims or interests of a non-consenting class of creditors. 11 U.S.C. 1129(b). Such a plan is commonly known as a "cramdown" plan. See *RadLAX Gateway Hotel, LLC* v. *Amalgamated Bank*, 566 U.S. 639, 641-642 (2012). In order to be confirmable over the objection of an impaired class, a cramdown plan must "not discriminate unfairly" and must be "fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." 11 U.S.C. 1129(b)(1). The Code further provides that such a plan may be confirmed only if "at least one class of claims that is impaired under the

plan has accepted the plan, determined without including any acceptance of the plan by any insider." 11 U.S.C. 1129(a)(10).

For purposes of Section 1129(a)(10), "[a] class of claims has accepted a plan if such plan has been accepted by creditors * * * that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors * * * that have accepted or rejected such plan." 11 U.S.C. 1126(c). When a class of claims contains only one creditor, that creditor (if he is a non-insider) may decide whether to accept or reject a plan. *Ibid.* When a class of claims contains multiple creditors, only the votes of non-insider creditors may be considered in determining whether the class has accepted a proposed plan. 11 U.S.C. 1129(a)(10). The question presented in this case concerns the standard of review that applies to a bankruptcy court's determination that a particular creditor is or is not an "insider" for purposes of Section 1129(a)(10).

b. The Bankruptcy Code contains a non-exhaustive list of persons and entities with "insider" status. 11 U.S.C. 101(31). Persons or entities falling into one of the categories enumerated in Section 101(31) are commonly called "statutory insiders." Pet. App. 9a. Where, as here, the debtor is a corporation, "[t]he term 'insider' includes * * * (i) director of the debtor; (ii) officer of the debtor; (iii) person in control of the debtor; (iv) partnership in which the debtor is a general partner; (v) general partner of the debtor; or (vi) relative of a general partner, director, officer, or person in control of the debtor." 11 U.S.C. 101(31)(B).

Because the statutory definition of "insider" states that the term "includes" persons within the enumerated categories, it leaves open the possibility that other

persons will be insiders in particular circumstances. 11 U.S.C. 101(31); see 11 U.S.C. 102(3) (providing that the terms "'includes' and 'including' are not limiting" in the Bankruptcy Code). Congress left the definition of "insider" somewhat "open ended because the term is not susceptible of precise specification." H.R. Rep. No. 595, 95th Cong. 1st Sess. 314 (1977) (House Report). As a result, other persons and entities can be "non-statutory insiders," or insiders not listed in Section 101(31). Pet. App. 9a. Such persons have "a sufficiently close relationship with the debtor that [their] conduct is made subject to closer scrutiny than those dealing at arms length with the debtor." S. Rep. No. 989, 95th Cong., 2d Sess. 25 (1978) (Senate Report); House Report 312; see 2 *Collier on Bankruptcy*, ¶ 101.31, at 101-142 (Allen N. Resnick & Henry J. Sommer, eds., 16th ed. 2016) (*Collier*) (explaining that "a creditor may only be a non-statutory insider of a debtor when the creditor's transaction of business with the debtor is not at arm's length") (citation omitted).

Under the Bankruptcy Code, dealings between an insider and a corporate debtor are subject to particularly close scrutiny. See 2 *Collier* ¶ 101.31, at 101-140 ("An 'insider' generally is an entity whose close relationship with the debtor subjects any transactions made between the debtor and such entity to heavy scrutiny."). The Code also bars insiders from exercising some of the prerogatives that other creditors possess. In a Chapter 7 case, for example, an insider is not permitted to vote for a candidate for trustee. 11 U.S.C. 702(a)(3). Insider status is also a factor in determining whether a sufficient number of creditors have joined together to initiate an involuntary bankruptcy, 11 U.S.C. 303(b)(2); whether a pre-petition transfer may be avoided, 11 U.S.C.

547(b)(4)(B), 548(a)(1)(B)(IV); and whether certain debts may be discharged in a Chapter 7 bankruptcy, 11 U.S.C. 727(a)(7).

2. Respondent[1] is a limited liability corporation with only one member, MBP Equity Partners 1, LLC (MBP). Pet. App. 3a. MBP is managed by a board of five members, one of whom is Kathy Bartlett. *Ibid.* MBP and Bartlett are both statutory insiders of respondent. *Id.* at 16a. Bartlett "shares a close business and personal relationship" with Robert Rabkin, "which is unrelated to Bartlett's position with MBP." *Id.* at 3a. The parties dispute whether Rabkin is also an insider of respondent.

In June 2011, respondent filed a voluntary petition for bankruptcy under Chapter 11 of the Bankruptcy Code. Pet. App. 3a. At that time, respondent had two creditors: Petitioner held a fully secured claim of approximately $10 million, and MBP held an unsecured claim of approximately $2.76 million. *Ibid.* In September 2011, respondent filed a proposed plan of reorganization that would impair both claims. See C.A. E.R. 340, 347-351, 379-383. Because petitioner did not consent to the proposed plan, see *id.* at 578-579, the plan could not be confirmed unless another non-insider class that would be impaired by the plan voted to accept the plan. See 11 U.S.C. 1129(a)(10). But the only claim in the only other class was held by MBP, a statutory insider. See 11 U.S.C. 101(31)(B). In the absence of a confirmable plan, respondent would have been liquidated, and MBP

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[1] Although the case caption on this Court's docket indicates that there are multiple petitioners and respondents in this case, petitioner's brief indicates (Br. ii) that U.S. Bank National Association is the sole petitioner and that The Village at Lakeridge, LLC is the sole respondent. In this brief, we refer to those parties as petitioner and respondent, respectively.

would have had little hope of recovering on its unsecured claim or on its ownership of respondent. See Pet. App. 20a-21a.

Acting on behalf of MBP's board, Bartlett approached Rabkin and offered to sell him MBP's $2.76 million claim for $5000. Pet. App. 4a. Rabkin agreed to the proposal without negotiating the price or investigating what the claim might be worth. *Id.* at 4a, 19a-20a. Petitioner then moved to designate Rabkin's claim as an insider claim and to disallow it for voting purposes. *Id.* at 5a. While the motion was pending, petitioner voted to reject respondent's proposed reorganization plan, and Rabkin voted to accept it. J.A. 95-102.

3. After holding an evidentiary hearing, the bankruptcy court granted petitioner's motion to disallow Rabkin's vote. Pet. App. 61a-70a. The court concluded that Rabkin was a statutory insider because, "as the assignee of the claim," he had "acquired the same status as" statutory insider MBP when he purchased MBP's claim. *Id.* at 67a.

By contrast, the bankruptcy court concluded that Dr. Rabkin was not a non-statutory insider. "[A]mong other things," the court found that:

> (a) Dr. Rabkin does not exercise control over the Debtor; (b) Dr. Rabkin does not cohabitate with Ms. Bartlett, and does not pay Ms. Bartlett's bills or living expenses; (c) Dr. Rabkin has never purchased expensive gifts for Ms. Bartlett; (d) Ms. Bartlett does not exercise control over Dr. Rabkin; (e) Ms. Bartlett does not pay [D]r. Rabkin's bills or living expenses; and (f) Ms. Bartlett has never purchased expensive gifts for Dr. Rabkin.

Pet. App. 66a. The court further found that MBP's "insider claim was not assigned to Dr. Rabkin in bad faith

to create an impaired, consenting class for purposes of cramdown." *Id.* at 67a.

4. The Bankruptcy Appellate Panel for the Ninth Circuit affirmed in part and reversed in part. Pet. App. 28a-60a.

The panel rejected the bankruptcy court's conclusion that Rabkin was a statutory insider. It held that he did not fall within any of the categories enumerated in the statutory definition, Pet. App. 39a-41a; see 11 U.S.C. 101(31), and that the assignee of an insider claim does not automatically become a statutory insider by virtue of the assignment, Pet. App. 45a-48a.

The panel upheld the bankruptcy court's determination that Rabkin was not a non-statutory insider. Pet. App. 41a-44a. The panel noted that "a non-statutory insider is one 'who has a sufficiently close relationship with the debtor that his conduct is made subject to closer scrutiny than those dealing at arms length with the debtor.'" *Id.* at 41a (quoting *In re Freidman*, 126 B.R. 63, 70 (B.A.P. 9th Cir. 1991)). That closer scrutiny, the panel explained, requires an assessment of whether "the creditor 'exercises such control or influence over the debtor as to render their transaction not arms-length.'" *Id.* at 42a (quoting *In re Schuman*, 81 B.R. 583, 586 (B.A.P. 9th Cir. 1987)). The panel concluded that, "[w]hile others might come to a different conclusion," the bankruptcy court had not clearly erred in finding on the basis of Rabkin's and Bartlett's testimony that Rabkin was not a non-statutory insider. *Id.* at 44a.

The panel also affirmed the bankruptcy court's finding that Rabkin had voted to accept the plan in good faith. Pet. App. 54a.

5. The court of appeals affirmed. Pet. App. 1a-27a.

a. All three members of the court of appeals panel agreed that "[a] person does not become a statutory insider solely by acquiring a claim from a statutory insider." Pet. App. 10a; see *id.* at 19a. The majority noted that "bankruptcy law distinguishes between the status of a claim and that of a claimant," and it explained that "[i]nsider status pertains only to the claimant." *Id.* at 10a.

A majority of the court of appeals panel then upheld the bankruptcy court's determination that Rabkin was not a non-statutory insider. Pet. App. 13a-18a. The court of appeals explained that it reviews de novo "the bankruptcy court's definition of non-statutory insider status, which is a purely legal question," *id.* at 15a n.13, while "review[ing] the bankruptcy court's factual finding for clear error," *id.* at 15a; see also *id.* at 8a. With respect to the legal standard that governs the inquiry into insider status, the court agreed with the bankruptcy court that, in assessing whether a creditor is a non-statutory insider, "[a] court must conduct a fact-intensive analysis to determine if a creditor and debtor shared a close relationship and negotiated at less than arm's length." *Id.* at 14a. The majority also held that the bankruptcy court had not clearly erred in concluding that neither Rabkin's relationship with respondent nor Rabkin's relationship with Bartlett was "sufficiently close to compare with any category listed in § 101(31)." *Id.* at 16a. The majority further held that the bankruptcy court had not clearly erred in concluding that the sale of MBP's claim to Rabkin had been conducted at arm's length. *Id.* at 17a n.15.[2]

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[2] In response to the dissent's conclusion that Rabkin was a non-statutory insider, the majority explained that "[t]he dissent did not preside over the evidentiary hearing and did not hear the evidence

Judge Clifton dissented from the court of appeals' conclusion that Rabkin was not a non-statutory insider. Pet. App. 19a-27a. Although Judge Clifton agreed with the legal criteria used by the majority to identify non-statutory insiders, he suggested that the bankruptcy court had applied an incorrect legal test. *Id.* at 24a. In any event, he would have held that the bankruptcy court had clearly erred in concluding that Rabkin's acquisition of the claim was negotiated at arm's length. *Id.* at 24a-25a; see *id.* at 19a-22a. Judge Clifton concluded that "the only logical explanation for Rabkin's actions here" was that Rabkin "did a favor for a friend." *Id.* at 21a. Although Judge Clifton agreed that the bankruptcy court's analysis of the relationship between Rabkin and Bartlett "would support a finding that Rabkin and Bartlett are separate financial entities," in his view it would "not show that this transaction was conducted" at arm's length. *Id.* at 23a.

b. In a separate memorandum decision, the court of appeals affirmed the Bankruptcy Appellate Panel's judgment that the bankruptcy court did not clearly err in finding that Rabkin had voted in good faith. J.A. 156-160.

SUMMARY OF ARGUMENT

"Traditionally, decisions on 'questions of law' are 'reviewable *de novo*,' [and] decisions on 'questions of fact' are 'reviewable for clear error.'" *Highmark Inc.* v. *Allcare Health Mgmt. Sys., Inc.*, 134 S. Ct. 1744, 1748 (2014) (quoting *Pierce* v. *Underwood*, 487 U.S. 552, 558

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in person," and that the court of appeals "cannot substitute its judgment for that of the bankruptcy court 'simply because it is convinced that it would have decided the case differently.'" Pet. App. 16a n.14 (quoting *Anderson* v. *City of Bessemer*, 470 U.S. 564, 573 (1985)); see *id.* at 17a n.16.

(1988)). Although a particular question may contain both legal and factual components, "[c]ourts of appeals have long found it possible to separate factual from legal matters" and to apply the appropriate standard of review to each. *Teva Pharm. USA, Inc.* v. *Sandoz, Inc.*, 135 S. Ct. 831, 839 (2015).

That is the appropriate course here. Petitioner contends (Br. 29-34) that, because the Bankruptcy Code does not comprehensively define the term "insider," the application of that term is necessarily a mixed question of law and fact reviewed de novo. But petitioner's argument elides the discrete factual and legal components that may be at issue in any given appeal. When a trial court gives content to an undefined (or partially defined) statutory term and an appeal is subsequently taken, the appellant's challenge to the court's statutory construction presents a pure legal question that the appellate court reviews de novo. But if application of the correct legal standard requires subsidiary factual findings, those findings are reviewed for clear error, even if they are "nearly dispositive" in a particular case. *Teva Pharm.*, 135 S. Ct. at 842.

A widely accepted definition of non-statutory insider status—which this Court did not grant certiorari to review—states that "a creditor may only be a non-statutory insider of a debtor when the creditor's transaction of business with the debtor is not at arm's length." 2 *Collier* ¶ 101.31, at 101-142. Under that definition, a trial court's finding that a transaction was or was not conducted at arm's length is a factual question. It involves an inquiry into the parties' motivations: Did each act pursuant to its own commercial interests, or did their relationship introduce external considera-

tions? Consistent with this Court's longstanding recognition that "[t]reating issues of intent as factual matters for the trier of fact is commonplace," *Pullman-Standard* v. *Swint*, 456 U.S. 273, 288 (1982), appellate courts have reviewed arm's-length determinations for clear error both within and outside the bankruptcy context.

The court of appeals correctly articulated the applicable standards of review in this case. It first reviewed "de novo" the bankruptcy court's "definition of non-statutory insider status." Pet. App. 8a. The court of appeals concluded that, notwithstanding the bankruptcy "court's failure to use the words 'arm's length transaction,'" the bankruptcy court had properly analyzed whether the transaction was "conducted at arm's length." *Id.* at 17a n.15. Next, the court of appeals reviewed the factual record that the bankruptcy court had considered, *id.* at 16a-18a, and held that the bankruptcy court had not clearly erred in finding that Rabkin was not a non-statutory insider, *id.* at 18a. Whatever the merits of its view of the record, the court of appeals applied the correct standard of review to each question.

ARGUMENT

A BANKRUPTCY COURT'S ARTICULATION OF THE LEGAL STANDARD FOR ASSESSING "INSIDER" STATUS IS REVIEWED DE NOVO, BUT THE COURT'S FACTUAL FINDINGS ARE REVIEWED FOR CLEAR ERROR

A. Where Possible, Appellate Courts Should Distinguish Overarching Legal Questions From Subsidiary Factual Questions

1. "Traditionally, decisions on 'questions of law' are 'reviewable *de novo*,' [and] decisions on 'questions of fact' are 'reviewable for clear error.'" *Highmark Inc.* v. *Allcare Health Mgmt. Sys., Inc.*, 134 S. Ct. 1744, 1748

(2014) (quoting *Pierce* v. *Underwood*, 487 U.S. 552, 558 (1988)). Determining the proper standard of review thus requires precise identification of the particular question raised on appeal. Where "statutory terms are at issue, their interpretation is a question of law" that must be reviewed de novo. *Chandris, Inc.* v. *Latsis*, 515 U.S. 347, 369 (1995). But where the application of a statute turns on the underlying facts, a trial court's factual findings, "like all other factual determinations, must be reviewed for clear error." *Teva Pharm. USA, Inc.* v. *Sandoz, Inc.*, 135 S. Ct. 831, 838 (2015).

Rule 52(a)(6) of the Federal Rules of Civil Procedure, which applies in many bankruptcy proceedings, provides without exception that "[f]indings of fact * * * must not be set aside unless clearly erroneous, and the reviewing court must give due regard to the trial court's opportunity to judge the witnesses' credibility." Fed. R. Civ. P. 52(a)(6); see Fed. R. Bankr. P. 7052 (applying Federal Rule of Civil Procedure 52 to adversary proceedings in bankruptcy); Fed. R. Bankr. P. 9014(c) (applying Federal Rule of Bankruptcy Procedure 7052 to motions in contested matters, except where otherwise provided). Thus, across a variety of contexts, "review of factual findings under the clearly-erroneous standard —with its deference to the trier of fact—is the rule, not the exception." *Anderson* v. *City of Bessemer*, 470 U.S. 564, 575 (1985); see *Teva Pharm.*, 135 S. Ct. at 837 (explaining that, when they review the findings of a "district court sitting without a jury, appellate courts must constantly have in mind that their function is not to decide factual issues *de novo*") (citation omitted).

2. Petitioner asserts (Br. 29-34) that "insider" status under the Bankruptcy Code is a single mixed question of law and fact and is thus reviewed de novo. The need

for courts to define and apply a legal standard as part of their analysis, however, does not transform all subsidiary factual findings into legal conclusions. Nor does it require that the entire dispute be reviewed de novo. To the contrary, "[c]ourts of appeals have long found it possible to separate factual from legal matters." *Teva Pharm.*, 135 S. Ct. at 839.

This Court has taken care to distinguish overarching legal questions from subsidiary factual ones, particularly when an appeal focuses on only one type of question. The Court recently determined, for example, that a dispute about the meaning of a patent claim raises a question of law that an appellate court reviews de novo, while any subsidiary factual questions that may arise during claim construction are reviewed for clear error. See *Teva Pharm.*, 135 S. Ct. at 837-838. Similarly, to borrow petitioner's example (Br. 40-41), the Court has held that the definition of the Jones Act term "seaman," 46 U.S.C. 30104, is a legal question, but subsidiary questions such as whether a vessel is "in navigation" are factual. *Chandris*, 515 U.S. at 369, 373. In reaching that conclusion, the Court emphasized that "it is the court's duty to define the appropriate standard," but that a jury could find the facts relevant under that standard. *Id.* at 369.

The bankruptcy context is no different. In a variety of circumstances, resolution of an overarching legal question—including resolution of a dispute about the meaning of an undefined or partially defined statutory term—may demand subsidiary factual findings. When reviewing those subsidiary findings, an appellate court should apply the same deferential standard of review that it would apply to any other trial-court factual find-

ing. For example, numerous provisions of the Bankruptcy Code authorize dismissal of a case for "cause," a term for which the Code provides illustrative examples but which it does not exhaustively define. 11 U.S.C. 707(a), 1112(b)(4), 1307(c). Several courts of appeals have explained that a trial court's definition of "cause" is a legal conclusion that is reviewed de novo. See, *e.g.*, *In re Krueger*, 812 F.3d 365, 369-373 (5th Cir.), cert. denied, 137 S. Ct. 314 (2016); *In re Piazza*, 719 F.3d 1253, 1261-1262 (11th Cir. 2013); *In re Marsch*, 36 F.3d 825, 828 (9th Cir. 1994). But where a trial court has properly defined "cause" to include "bad faith," the trial court's finding of bad faith is reviewed deferentially on appeal. See *Krueger*, 812 F.3d at 374; *Piazza*, 519 F.3d at 1271-1274; *Marsch*, 36 F.3d at 828.

3. Petitioner suggests (Br. 52-53) that a factual finding is ineligible for deferential review if it represents the "ultimate issue" to be decided. That is incorrect. "[A]n issue does not lose its factual character merely because its resolution is dispositive of the ultimate * * * question." *Miller* v. *Fenton*, 474 U.S. 104, 113 (1985); see *Teva Pharm.*, 135 S. Ct. at 842 ("Simply because a factual finding may be nearly dispositive does not render the subsidiary question a legal one."); *Baumgartner* v. *United States*, 322 U.S. 665, 670 (1944) ("[A] 'finding of fact' may be the ultimate judgment on a mass of details involving not merely an assessment of the trustworthiness of witnesses but other appropriate inferences that may be drawn from living testimony which elude print."). And Federal Rule of Civil Procedure 52(a) "does not divide findings of fact into those that deal with 'ultimate' and those that deal with 'subsidiary' facts." *Pullman-Standard* v. *Swint*, 456 U.S. 273, 287 (1982).

B. A Trial Court's Determination Whether A Particular Person Has "Insider" Status Under The Bankruptcy Code Involves Both Legal And Factual Components, With Separate Standards Of Review For Each

The well-established principles described above govern the analysis of insider status under Section 1129(a)(10). When an appellate court reviews a trial court's determination concerning a creditor's insider status, the trial court's conclusions of law are reviewed de novo and its findings of fact are reviewed for clear error. The critical question is whether, on appeal, the trial court is "faulted for misunderstanding or applying an erroneous definition" or for "arriving at * * * an erroneous [factual] finding." *Pullman-Standard*, 456 U.S. at 287.

1. Petitioner is correct (Br. 19-22) that an appellate court should review de novo the legal test or standard that a trial court articulates for determining whether a particular person is a non-statutory insider.

The enumerated list of "insiders" set forth in Section 101(31) reflects that "[a]n insider is one who has a sufficiently close relationship with the debtor that his conduct is made subject to closer scrutiny than those dealing at arms length with the debtor." House Report 312; Senate Report 25. In determining whether a particular creditor is a non-statutory insider (*i.e.*, a person who should be treated as an insider even though he does not fall within the non-exhaustive list of examples contained in Section 101(31)), courts therefore have "focuse[d] on two factors: (1) the closeness of the relationship between the parties; and (2) whether the transaction was negotiated at arm's length." 5 *Collier* ¶ 547.03[6], at 547-36; see *In re U.S. Med., Inc.*, 531 F.3d 1272, 1277 (10th Cir. 2008) ("The inquiry then is whether there is a

close relationship and whether there is anything other than closeness to suggest that any transactions were not conducted at arm's length.") (emphasis omitted).

Courts' emphasis on the presence or absence of an arm's-length relationship is consistent with the purpose of Section 1129(a)(10). A creditor who is also an insider often has a substantial interest, not necessarily shared by other creditors, in ensuring that a debtor business continues to operate rather than liquidating. As a result, an insider may be willing to accept impairment under a plan of reorganization so that the insider can continue to benefit from the debtor's ongoing operation. Because an insider is in a position to advance its own interests by influencing the drafting of a proposed plan, the degree of impairment it is willing to accept may not reflect the type of arm's-length bargaining that would be reflected in the acceptance of impairment by a non-insider creditor. Excluding an insider's vote ensures that "some disinterested creditors have approved the plan" and limits the "risk of collusion between an insider creditor and the debtor at the expense of other creditors." *In re South Beach Sec., Inc.*, 606 F.3d 366, 378 (7th Cir. 2010); see *U.S. Med.*, 531 F.3d at 1280 ("[I]nsiders do not have interests 'independent' of their debtors whereas parties held to be operating at arm's length necessarily do.") (citation omitted).

How courts frame the legal standard to best capture those conflicted insiders is a question of statutory interpretation and thus a pure question of law. See, *e.g.*, *Chandris*, 515 U.S. at 369. As petitioner correctly observes (Br. 47), "appellate courts are much better situated to decide norms and standards that give meaning and limits for open-ended statutory terms." Thus, when the appellant in a bankruptcy case challenges the legal

test or standard that the trial court applied to determine non-statutory insider status, that challenge should be reviewed de novo on appeal. See Pet. Br. 22; Resp. Br. 30 n.12.[3]

2. At the present stage of the case, the parties' primary disagreement concerns the standard of review to be applied to a subsidiary question: whether the sale of MBP's claim to Rabkin "was negotiated at arm's length." 5 *Collier* ¶ 547.03[6], at 547-36. The bankruptcy court's resolution of that factual question, which depends in part on the parties' intent at the time they consummated the transaction, should be reviewed for clear error. Deferential review is also consistent with the "history of appellate practice," "the sound administration of justice," and other provisions of the Bankruptcy Code. *McLane Co.* v. *EEOC,* 137 S. Ct. 1159, 1166 (2017) (citation omitted).

a. The basic nature of the arm's-length inquiry counsels in favor of clear-error review. An arm's-length transaction is "[a] transaction between two parties, however closely related they may be, conducted as if the parties were strangers, so that no conflict of interest arises." *Black's Law Dictionary* 1726 (10th ed. 2014); see *U.S. Med.*, 531 F.3d at 1277 n.4 ("An arm's-length transaction is a transaction in good faith in the ordinary

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[3] The petition for a writ of certiorari in this case raised two legal challenges, which were reviewable de novo on appeal, to the court of appeals' determination that Rabkin was not an insider for purposes of the Bankruptcy Code's cramdown provisions. First, petitioner argued that a person who acquires a claim from an insider automatically takes on insider status. See Pet. 7-19. Second, petitioner argued that the court had applied an incorrect legal test for determining insider status. See Pet. 24-28. This Court denied review on those questions. See J.A. 161.

course of business by parties with independent interests.") (citation, brackets, and internal quotation marks omitted). For purposes of insider status under the Bankruptcy Code, the determination whether two parties bargained at arm's length turns on the parties' *motivations*: Did (and would) the creditor act solely in his own interests, or did (and would) he account for the interests of the debtor? Cf. *Commissioner* v. *Wemyss*, 324 U.S. 303, 306 (1945) (explaining that, for purposes of the gift tax, a transaction "at arm's length" is "free from any donative intent") (citation omitted); see *In re Holloway*, 955 F.2d 1008, 1014 (5th Cir. 1992) (concluding that ex-wife was an insider because her transactions with her ex-husband "were not commercially motivated" and thus "were not conducted at arm's length"). Questions concerning the parties' motives in negotiating a transaction, like other questions of intent, are factual. See, *e.g.*, *Merck & Co.* v. *Reynolds*, 559 U.S. 633, 648 (2010) (explaining that the "state of a man's mind is as much a fact as the state of his digestion") (citations omitted); *Pullman-Standard*, 456 U.S. at 288 ("Treating issues of intent as factual matters for the trier of fact is commonplace.").

Petitioner contends that de novo review is nevertheless justified because "the historical facts are admitted or established, the rule of law is undisputed, and the issue is whether the facts satisfy the statutory standard." Pet. Br. 26 (quoting *Pullman-Standard*, 456 U.S. at 289 n.19). But *Pullman-Standard* distinguished that sort of mixed question of law and fact from factual questions of intent. The Court explained that, even where the historical facts regarding the discriminatory effect of a seniority system had been established, the question "whether the differential impact of the seniority system

reflected an intent to discriminate on account of race" remained "a pure question of fact." *Pullman-Standard*, 456 U.S. at 287-288. So too here. Whether a transaction was conducted at arm's length is a *factual* inference drawn from various historical facts, whether or not those historical facts are themselves disputed. Deferential review is particularly appropriate where (as here) the trial court's conclusions as to intent are based in part on live testimony concerning the witnesses' reasons for acting as they did. See Pet. App. 16a n.14 (explaining that the dissenting judge "did not preside over the evidentiary hearing and did not hear the evidence in person").

b. The limited history of relevant appellate practice also supports a deferential standard of review. See *McLane*, 137 S. Ct. at 1167. In deciding whether claimants were non-statutory insiders under the Bankruptcy Code, courts of appeals have treated determinations regarding the arm's-length character of particular transactions as determinations of fact, in the few cases where the issue has arisen. See *In re Winstar Commc'ns, Inc.*, 554 F.3d 382, 399-400 (3d Cir. 2009) (declining to "conclude that the Bankruptcy Court's finding that the parties did not deal at arm's length was clearly erroneous"); *In re Florida Fund of Coral Gables, Ltd.*, 144 Fed. Appx. 72, 76 (11th Cir. 2005) (holding that the bankruptcy court did not "clearly err[] in finding that the transactions between the Florida Fund and the Police Fund were not at arm's length"); cf. *U.S. Med.*, 531 F.3d at 1280 (concluding that, "where the bankruptcy court considered a variety of factors and found that all relations between Creditor and Debtor were at arm's length, a ruling that Creditor is a non-statutory insider does not follow") (citation omitted). Although petitioner

points to those decisions and others that describe insider status as a mixed question of law and fact to be reviewed de novo (Br. 31-32), petitioner does not identify any decision that has applied de novo review to the subsidiary question whether a transaction was conducted at arm's length.

Those few examples applying Section 1129(a)(10) are consistent with appellate courts' general approach. In a variety of contexts, courts of appeals have long accorded deference to trial-court findings about the arm's-length nature of a transaction. See, *e.g.*, *Lardas* v. *Grcic*, 847 F.3d 561, 568 (7th Cir. 2017) (explaining that bankruptcy court's determination that a sale was conducted at arm's length was "reviewable only for clear error"), petition for cert. pending, No. 16-1508 (filed June 19, 2017); *D'Amato* v. *Deutsche Bank*, 236 F.3d 78, 86 (2d Cir. 2001) (holding that district court's determination that settlement was the product of arm's-length negotiations "was not clearly erroneous"); *In re O'Connor*, 153 F.3d 258, 261 (5th Cir. 1998) (holding that bankruptcy court's arm's-length determination about an option contract was not "clear error"); *Ford* v. *Allied Mut. Ins. Co.*, 72 F.3d 836, 840 (10th Cir. 1996) (describing a "major issue of fact as to whether" an individual "was in an arm's length relationship" with his insurer); *Allen* v. *Commissioner*, 925 F.2d 348, 352 (9th Cir. 1991) (concluding that "it was not clear error to find the three organizations were not at arm's length for purposes of the transaction in question") (citation and internal quotation marks omitted); *United States* v. *Seetapun*, 750 F.2d 601, 605 (7th Cir. 1984) (concluding that a husband and wife were "plainly not dealing at arm's length

in this matter, and the district court committed clear error in failing to recognize that fact"). Petitioner does not identify any contrary examples.

c. The "basic principles of institutional capacity" likewise "counsel in favor of deferential review." *McLane*, 137 S. Ct. at 1167. The fact-intensive determination that a transaction was conducted at arm's length turns in part on historical facts (the terms of the deal, the relationship between the parties, and so on) and in part on the credibility of the witnesses who testify as to their motives and reasoning. The resulting decision "must be based ultimately on the application of the fact-finding tribunal's experience with the mainsprings of human conduct to the totality of the facts of each case." *Commissioner* v. *Duberstein*, 363 U.S. 278, 289 (1960). The court that hears the live testimony of the relevant witnesses is best positioned to make that decision. See, *e.g.*, *Cooper* v. *Harris*, 137 S. Ct. 1455, 1474 (2017) ("[T]he various cues that bear so heavily on the listener's understanding of and belief in what is said are lost on an appellate court later sifting through a paper record.") (citation and internal quotation marks omitted); *Miller*, 474 U.S. at 114 (noting that there are "compelling and familiar justifications" for applying deferential review when "the issue involves the credibility of witnesses and therefore turns largely on an evaluation of demeanor").

In addition, de novo appellate review would provide few "law-clarifying benefits" in this context. *Pierce*, 487 U.S. at 561. Although the Bankruptcy Code enumerates 20 categories of persons and entities that qualify as insiders, 11 U.S.C. 101(31), Congress did not attempt to define the full range of covered entities because "the term ['insider'] is not susceptible of precise

specification." House Report 314. Non-statutory insiders represent the residual category that Congress deemed incapable of comprehensive definition. As a result, the range of potential non-statutory insiders will vary significantly, and the determination whether a transaction was conducted at arm's length will "generally not [be] amenable to broad *per se* rules." *McLane*, 137 S. Ct. at 1168 (citation omitted). Rather, trial courts are likely to confront "multifarious, fleeting, special, narrow facts that utterly resist generalization." *Pierce*, 487 U.S. at 561-562 (citation omitted). Searching appellate review of such case-specific decisions would add only modest value.

d. Other Bankruptcy Code provisions reinforce the conclusion that deferential review is appropriate. See *Pierce*, 487 U.S. at 558. As this case illustrates, an assertion that an individual is an insider under 11 U.S.C. 1129(a)(10) may often accompany an assertion that he voted to confirm a plan in bad faith, see 11 U.S.C. 1126(e), or that a plan was proposed in bad faith, see 11 U.S.C. 1129(a)(3). See J.A. 73-74. Petitioner acknowledges (Br. 51) that a trial court's bad-faith analysis involves an assessment of "individualized subjective factors" that is subject to deferential review. See *In re W.R. Grace & Co.*, 475 B.R. 34, 87 (D. Del. 2012) (noting that bankruptcy courts have "considerable discretion in finding good faith") (citation omitted). Much of the same evidence that informs the court's determination whether a person voted his claim in good faith, consistent with his commercial interests, may also inform the determination whether a person acquired that claim at arm's length, consistent with his commercial interests. Trial courts equipped to distinguish between good-faith and bad-faith voting are similarly equipped

to distinguish between independent and biased decisionmaking. See *McLane*, 137 S. Ct. at 1163 (noting that trial courts' "considerable experience in making similar decisions in other contexts gives them the institutional advantage") (brackets, citation, and internal quotation marks omitted).

In addition to the provisions that restrict insiders' role in the plan-confirmation process, the Bankruptcy Code contains several independent safeguards against approval of plans that are substantially unfair to creditors. All plans must be proposed in good faith, must provide objecting creditors with at least the value that they would receive if the debtor were liquidated, and must be feasible. 11 U.S.C. 1129(a)(3), (7) and (11). In addition, cramdown plans must "not discriminate unfairly" and must be "fair and equitable," as further defined for a variety of scenarios, "with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." 11 U.S.C. 1129(b)(1); see *RadLAX Gateway Hotel, LLC* v. *Amalgamated Bank*, 566 U.S. 639, 643 (2012) (explaining that "[a] Chapter 11 plan confirmed over the objection of a class of secured claims must meet one of three requirements in order to be deemed fair and equitable") (internal quotation marks omitted). Those other prerequisites to plan confirmation mitigate petitioner's concern that deferential appellate review of a bankruptcy court's determination regarding a particular creditor's arm's-length status will result in "an unfair advantage" for debtors at the expense of creditors. Pet. Br. 55 (citation omitted).

C. The Court Of Appeals Articulated And Applied The Correct Standard Of Review In This Case

1. The court of appeals correctly explained that, when an appellate court reviews a trial court's determination concerning a creditor's insider status, it reviews the trial court's conclusions of law de novo and the trial court's findings of fact for clear error. Pet. App. 8a. In applying that approach, the court of appeals first reviewed the bankruptcy court's articulation of the criteria used to determine whether a particular creditor is a non-statutory insider. The court of appeals recognized that "[e]stablishing the definition of non-statutory insider status is * * * a purely legal inquiry" that an appellate court reviews "de novo." *Ibid.* The court further explained that an entity is a non-statutory insider if "(1) the closeness of [the creditor's] relationship with the debtor is comparable to that of the enumerated insider classifications in § 101(31), and (2) the relevant transaction is negotiated at less than arm's length." *Id.* at 13a.

The court of appeals evidently viewed the bankruptcy court as having applied the proper legal test for determining non-statutory insider status, as it emphasized that it had "reviewed de novo the bankruptcy court's definition of non-statutory insider status." Pet. App. 15a n.13. The court of appeals then stated that it would next "analyze whether the facts of this case are such that Rabkin met that definition, which is a purely factual inquiry and properly left to clear error review." *Ibid.* The court described the course of dealing among Rabkin, Bartlett, and MBP, see *id.* at 16a-18a, and concluded that "[t]hese facts do not leave us with a 'definite and firm conviction that a mistake has been committed,'" *id.* at 18a (citation omitted). The court's overall

approach was thus consistent with the principles described above, under which a trial court determination as to insider status may rest on distinct legal and factual components, and an appellate court should apply the standard of review that is appropriate for each aspect of the trial court's analysis.

To be sure, the court of appeals' opinion includes some imprecise language. The court stated, for example, that "[t]he bankruptcy court's finding that Rabkin does not qualify as a non-statutory insider is not clearly erroneous," Pet. App. 16a—a statement that elides the separate legal and factual components of the bankruptcy court's ultimate conclusion as to Rabkin's insider status. But the court of appeals elsewhere made clear that it was applying "a different standard of review" to the "two distinct issues in question," *i.e.*, de novo review to the bankruptcy court's articulation of the legal standard and clear-error review to the bankruptcy court's factual findings. *Id.* at 15a n.13.

2. Petitioner contends (Br. 26-28) that the court of appeals in fact deferred to the bankruptcy court's *legal* conclusions. That contention rests on petitioner's view that the bankruptcy court adopted a strict five-factor test for determining non-statutory insider status, rather than properly assessing whether MBP had sold its claim to Rabkin at arm's length.[4]

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[4] Petitioner elsewhere faults the bankruptcy court for failing to recite any specific test for determining whether the sale was conducted at arm's length. Pet. Br. 28-29 (citing Pet. App. 24a). But an arm's-length transaction is a familiar concept that this Court has often applied without further embellishment. See, *e.g.*, *Jones* v. *Harris Assocs. L. P.*, 559 U.S. 335, 346 (2010); *Pepper* v. *Litton*, 308 U.S. 295, 306-307 (1939). The bankruptcy court did not commit legal error in failing to recite explicitly the definition discussed above. See pp. 17-18, *supra*.

If the bankruptcy court had articulated and applied the wrong test for determining whether a particular creditor is a non-statutory insider, that would have been a legal error, reviewable de novo. See, *e.g.*, *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 43-44 (1960). But while the bankruptcy court did not find in so many words that Rabkin had purchased MBP's claim in an "arm's-length transaction," it cited an array of facts supporting that conclusion: that Rabkin did not control Bartlett, or vice versa; that Rabkin's and Bartlett's finances were not intertwined; that MBP's "insider claim was not assigned to Dr. Rabkin in bad faith to create an impaired, consenting class";[5] and that Rabkin had made "a speculative investment" with reasonable due diligence "under the circumstances." Pet. App. 66a-67a;

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[5] In the proceedings below, petitioner argued that MBP had assigned its claim to Rabkin in order "to artificially create an impaired consenting class," J.A. 74; see Pet. App. 62a, and that Rabkin's acceptance of the plan therefore should be disallowed under 11 U.S.C. 1126(e), which authorizes the court to "designate any entity whose acceptance or rejection of [a proposed] plan was not in good faith, or was not solicited or procured in good faith." The bankruptcy court rejected that contention. Pet. App. 67a. The court found that MBP's "insider claim was not assigned to Dr. Rabkin in bad faith to create an impaired, consenting class for purposes of cramdown" because Rabkin "was not required to sell his claim to" petitioner; because Rabkin had exercised diligence that "was sufficient under the circumstances"; and because "Ms. Bartlett did not ask Dr. Rabkin to vote in favor of the" plan. *Ibid.* Although the parties' dispute over bad faith primarily related to Section 1126(e), the court's analysis of the Section 1126(e) issue also supports its finding that the transaction at issue here was conducted at arm's length—*i.e.*, that Rabkin had purchased (and MBP had sold) the claim in good faith, consistent with his own commercial interests. See *id.* at 42a; see also *U.S. Med.*, 531 F.3d at 1277 n.4.

see J.A. 153-155. Taken together, those various findings are properly understood as an implicit determination that the sale was made at arm's length.

In any event, in determining whether the court of appeals misstated the legal principles that govern appellate review, the salient point is that the court of appeals *understood* the bankruptcy court to have found that an arm's-length sale occurred. The court of appeals did not believe that the bankruptcy court had adopted the strict five-factor test that petitioner perceives (Br. 26-27). Rather, it concluded that "[t]he [bankruptcy] court's failure to use the words 'arm's length transaction' is irrelevant. The court's entire explanation is a description of why the transaction was conducted at arm's length and, hence, why Rabkin was not an insider." Pet. App. 17a n.15; see *id.* at 14a (noting that a trial court "must conduct a fact-intensive analysis to determine if a creditor and debtor * * * negotiated at less than arm's length"). The court of appeals' articulation of the applicable standard of review followed logically from its understanding of the rationale on which the bankruptcy court had decided the case.

3. The dissenting judge below offered two basic criticisms of the majority's analysis. The dissenting judge stated that "[a]t no point does the bankruptcy court mention or refer to an 'arm's length transaction' at all, let alone provide a sufficient basis for a finding that Rabkin and Bartlett were unrelated or dealt with each other as strangers." Pet. App. 23a. The majority acknowledged the bankruptcy court's "failure to use the words 'arm's length transaction'" but found that omission "irrelevant," explaining that "[t]he court's entire explanation is a description of why the transaction was

conducted at arm's length." *Id.* at 17a n.15. The majority understood the term "arm's length transaction" to mean either a "transaction between two unrelated and unaffiliated parties" or a transaction between related parties that is "conducted as if the parties were strangers." *Id.* at 13a-14a n.11 (citation omitted). The dissenting judge did not dispute that, if the bankruptcy court had made an explicit finding that the sale of MBP's claim was conducted "as if the parties were strangers," *id.* at 14a n.11, that finding would be reviewable on appeal only for clear error. See p. 18, *supra* (questions concerning individual's motive or intent are factual rather than legal).

The dissenting judge also stated that "the only logical explanation for Rabkin's actions here" was that Rabkin "did a favor for a friend." Pet. App. 21a. The phrase "only logical explanation" suggests that, even if the bankruptcy court had made an explicit finding that the sale was conducted as though the parties were strangers, the dissenting judge would have rejected the finding as clearly erroneous. *Ibid.*; see *id.* at 19a ("The facts make it clear that this transaction was negotiated at less than arm's length."). The majority noted the dissent's view but concluded that "the bankruptcy court's explanation that Rabkin made a speculative investment at a relatively low cost and with the potential for a big payoff is equally logical." *Id.* at 18a n.16. Under the clear-error standard of appellate review, the majority's conclusion that the two explanations were "equally logical" required sustaining the bankruptcy court's determination that Rabkin was not a non-statutory insider.

Petitioner, like the dissenting judge below, identifies substantial grounds for doubting the bankruptcy court's factual finding that Rabkin acquired MBP's

claim for legitimate investment purposes, rather than as a means of benefiting a statutory insider with whom he had a close personal relationship. Pet. Br. 54; Pet. App. 19a-22a. But those arguments relate to the distinct question whether the bankruptcy court clearly erred in finding that Rabkin had purchased MBP's claim at arm's length. Whatever the answer to that question, the court of appeals was correct in holding that the bankruptcy court's resolution of the parties' factual dispute was subject to clear-error review on appeal.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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