20-3757

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

JAMES W. GIDDENS, AS TRUSTEE FOR
THE SIPA LIQUIDATION OF LEHMAN BROTHERS INC.,

Petitioner-Appellee,

—against—

THE LEHMAN BROTHERS INC. DEFERRED COMPENSATION DEFENSE STEERING COMMITTEE, AS ATTORNEY IN FACT FOR THOSE SPECIFIED HEREIN,

Respondent-Appellant.

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF AND SPECIAL APPENDIX FOR RESPONDENT-APPELLANT

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Rules

Regulations

Other Authorities

The Lehman Brothers Inc. Deferred Compensation Defense Steering Committee as Attorney-in-Fact for Those Specified in the Complaint in this proceeding below ("Appellants"), by their counsel, Scarola Zubatov Schaffzin PLLC, submit this Brief in support of their appeal of the Bankruptcy Court's grant of the motion of Appellee the Trustee in the bankruptcy of Lehman Brothers Inc. ("LBI") (the "Trustee") to dismiss Appellants' adversary proceeding to have their pension funds determined to be property outside the LBI bankruptcy estate under 11 U.S.C. §541(b)(7).

Statement of Subject Matter and Appellate Jurisdiction

This Court has jurisdiction over this appeal pursuant to 28 U.S.C. §158(d)(2), based upon its grant, on November 4, 2020 (*see* Doc. 2 in this case), of the Trustee's motion for a direct appeal to this Court from the final decision in the Memorandum Opinion and Order of the Bankruptcy Court of June 15, 2020 [A-397], and Appellants' timely Notice of Appeal of June 29, 2020. [A-425] The Bankruptcy Court had subject matter jurisdiction over this dispute pursuant to 28 U.S.C. §1334 and 28 U.S.C. §157.

Statement of the Standard of Review and of the Issues Presented

This appeal presents the following issues, each of which requires *de novo* review. *See In re Weber*, 719 F.3d 72, 75 (2d Cir. 2013) ("[W]e review de novo the bankruptcy court's legal conclusions"):

1. Whether, in light of the plain language of 11 U.S.C. §541(b)(7) providing that Appellants' pensions — which are part of an employee benefit plan subject to Title I of the Employee Retirement Income Security Act of 1974 ("ERISA") — are not part of the LBI bankruptcy estate, the Bankruptcy Court erred in deciding, contrary to the statute's clear and explicit language, and applying extraneous and subjective (and also baseless) policy considerations, that §541(b)(7) is inapplicable to Appellants' pensions at issue.

2. Whether the Bankruptcy Court erred in holding, contrary to all on-point and analogous precedent, that the catch-all general federal statute of limitations in 28 U.S.C. §1658(a) enacted in 1990 and applicable to ordinary claims in civil actions in Article III courts applies to the bankruptcy-specific determination here — the first time §1658(a) has been applied in any bankruptcy matter whatsoever in its 30 years, whether addressing if given property is part of a bankruptcy estate under 11 U.S.C. §541 or otherwise.

3. Whether the Bankruptcy Court erred in holding, on a pre-discovery motion to dismiss, that the doctrine of laches bars Appellants from seeking

determination of their rights under 11 U.S.C. §541(b)(7), when the Trustee itself inexplicably delayed the resolution of this issue since Proofs of Claim raising the issue were filed soon after the LBI bankruptcy filing, in 2009, and where it was aware from the virtual outset of this 2008 bankruptcy, when those Proofs of Claim were filed, that this 11 U.S.C. §541(b)(7) issue would need to be litigated before this dispute was concluded. The facts that the Bankruptcy Court made its laches finding on a motion to dismiss and without engaging in any fact-finding, and also its legal error in failing to address in any respect *at all* the "knowledge" element of the defense (§III.C below), require that the *de novo* standard of review applicable to a motion to dismiss be applied here. *See, e.g., Zuckerman v. Metro. Museum of Art*, 928 F.3d 186, 192 (2d Cir. 2019), *cert. denied*, 140 S. Ct. 1269 (2020) (reviewing laches determination *de novo* because made on a 12(b)(6) motion).

Appellants contend that the answer to each question is "yes," the Bankruptcy Court erred and should be reversed on each issue.

Statement of the Case and Statement of Facts

This is a direct appeal of the Bankruptcy Court's (Chapman, J.) dismissal of Appellants' proceeding pursuant to 11 U.S.C. §541(b)(7) for a determination that their pension funds are property outside the LBI bankruptcy estate. It presents an issue of first impression for this or any other circuit court (or any district court): whether §541(b)(7), enacted in 2005, protects, as outside the bankruptcy estate in

the event of bankruptcy, unfunded deferred compensation pension plans, sometimes called "Top Hat" plans, such as the plan that Appellants funded by deferring their earned income in the 1980s.

Appellants are 344 individuals who had been senior employees at Shearson Lehman Brothers Inc. (predecessor to LBI) in the 1980s. [A-179-96; Dkt. 8281[1]] They agreed to defer significant portions of their earned, non-discretionary, compensation in exchange for retirement benefits that would accrue and be paid by Shearson/LBI upon retirement — earned benefits that would be the principal source of retirement income for most. [*Id*.] Deferred compensation totaling more than $260 million, accrued to the time of the LBI bankruptcy in 2008, is at stake (far more was lost by these individuals in the way of now-extinguished additional future benefits). [*Id*.]

The pension plan involved is known as the Executive and Select Employees Plan ("ESEP") and was fully funded by Appellants' own money. [*Id*.] The features of ESEP relevant here are that it was, as noted, a Top Hat Plan in which senior executives defer their compensation, the funds are not segregated when they do (the employer becomes obligated to pay the pensions as a general obligation)

[1] All references to "Dkt. ___" are to the S.D.N.Y. Bankruptcy Court docket in Case 08-1420, the LBI bankruptcy proceeding from which the adversary proceeding below arises.

and taxes are not payable by the employees on the earned income at the time of deferral, but instead, only upon the future receipt of pension payments. [A-179-96]

When LBI filed for bankruptcy, Appellants and some others joined together to retain counsel, who in 2009 filed Proofs of Claim on behalf of each of them, which, among other things, asserted that Appellants' pension rights were protected by §541(b)(7) and hence outside the LBI bankruptcy estate. *See* Dkt. 12655 at Ex. B, Addendum. No action was taken by the Trustee as to that issue until six years later, in 2015, when the Trustee, without challenging the validity of the substance of Appellants' assertion that §541(b)(7) applied to their pensions, raised a different, procedural challenge to the Proofs of Claim (to their treatment of §541(b)(7) as equivalent to secured status). *See* Dkt. 12655. The Trustee prevailed on that issue in the Bankruptcy Court, *see* Dkt. 13053, and Appellants, also in 2015, then appealed to the District Court on that procedural issue. *See* S.D.N.Y. No. 15 CV 9670 ("Companion Appeal Dist. Ct."). The District Court did not decide that appeal until September 30, 2019, almost four years after it was filed. *See* Companion Appeal Dist. Ct. Dkt. 18. Appellants appealed that decision, and that appeal has been consolidated by this Court with this appeal by Order dated November 4, 2020. *See* Doc. 2 in this case. (That appeal being heard contemporaneously is referred to here as the "Companion Appeal.")

Appellants, before the District Court's decision eventually issued, determined to move forward, in light of the long wait (and the passage of time without their pensions), to obtain determination of the §541(b)(7) issue in the proceeding below, and, after discussions with the Trustee's counsel about the form in which to do that, filed a bankruptcy court adversary proceeding to obtain that determination. [A-8-13, 222] Prior to that time, the Trustee had plainly been aware of the §541 issue now presented and had never asserted in any sense whatsoever that it was too "late" for the issue to be determined (or that it should be raised in a different way). [A-131-32; *see also* §III.B. below] The Trustee moved to dismiss under FRCP 12(b)(6) (and FRBP 7012) — on the merits and also on assertions of a time-bar under 28 U.S.C. §1658(a) and laches [A-23-62] — and the Bankruptcy Court granted that motion on all three bases by its decision dated June 15, 2020 (the "Decision"). [A-397-423] Appellants filed their Notice of Appeal to the District Court on June 29, 2020. [A-424-25] The Trustee then moved to the Bankruptcy Court for certification of a direct appeal to this Court, and the Bankruptcy Court granted that motion by order dated July 20, 2020. *See* S.D.N.Y. Bankr. No. 19-01368, Dkt. 36 & 48. The Trustee then moved in this Court for permission for such direct appeal, *see* Case No. 20-2358, and this Court granted that motion by Order dated November 4, 2020 (directing in the same Order that the Companion Appeal be heard in tandem with this appeal). *See* Doc. 2 in this case.

Summary of Argument

Appellants' pension rights are not property of this bankruptcy estate in accordance with 11 U.S.C. §541(b)(7). That outside-the-bankruptcy estate status was determined in unequivocal and unambiguous language by Congress in 2005 amendments to the Bankruptcy Code adopted in §541(b)(7). (§I.A below) The Bankruptcy Court did not even attempt to explain in any way why the 2005 statutory amendment's text does not require that result. (§I.B below) Instead, it sets forth a discursive discussion of the so-called "Top Hat" features of pension plans such as ESEP and then abruptly concluded that the statute cannot be construed as Appellants contend — construed exactly as it unambiguously reads — because of perceived conflicts with other statutes applicable to unfunded Top Hat deferred compensation plans. The plain text, other provisions of the 2005 amendment explicitly covering plans exactly like Appellants' ESEP plan and §541(b)(7)'s legislative history all make clear, however, that §541(b)(7) applies to pension plans like ESEP. (§I.B.1) More, while the Bankruptcy Court held that it perceived a conflict between other, earlier, law and the 2005 amendment, it is beyond question that no court may ignore or effectively rewrite and reform clear statutory language because it believes Congress got it wrong. (§I.B.2) More still, once examined, the Bankruptcy Court's discursive discussion of the features of unfunded Top Hat deferred compensation plans such as Appellants' ESEP plan

does not even support a conclusion of actual conflict with other, earlier law — there is no such conflict. (§I.B.3) If there were, the conflict would still not permit a court to ignore the later statute and effectively rewrite it; but in fact, the asserted conflicts are illusory. For all these reasons, the Decision must be reversed.

On reversal of the Decision with regard to §541(b)(7), this Court must then consider and, Appellants contend also, reverse findings by the Bankruptcy Court that Appellants cannot prevail based upon a statute of limitations or laches. Both of those findings are erroneous.

The Bankruptcy Court incorrectly invoked a general federal catch-all statute of limitations enacted in 1990. (§II) That statute, 28 U.S.C. §1658(a), does not apply to a §541 determination as to what is and what is not bankruptcy estate property. In fact, *no case in the statute's 30 years has ever held* that §1658(a) applies to any bankruptcy court issue at all, much less to this *or any* subpart of §541. (§II) That statute does not apply, by its terms or its nature, to the necessary determination, in the administration of a bankruptcy, of the status of property — what is, or is not, property of a bankruptcy estate. Indeed, courts have uniformly held that both §541 and other closely related sections of the Bankruptcy Code *are subject to no statute of limitations*. (§II.A) The Bankruptcy Court ignored that caselaw — and common sense and logic. Additionally and separately, §1658(a) is, by its clear terms, applicable only to "civil actions" — a term of art that, consistent

with abundant statutory authority and caselaw, refers only to civil litigation in the commonly understood sense of disputes between plaintiffs and defendants in Article III courts and similar state courts. (§II.B) It does not apply at all to any proceeding in a bankruptcy court. The unprecedented and clearly incorrect application of §1658(a) to the assessment of what is, and is not, bankruptcy estate property must, therefore, be reversed.

The Decision must also be reversed in finding laches. (§III) Laches is a fact-intensive inquiry requiring proof, as an affirmative defense, of all three of its elements: (i) the movant's lack of knowledge as to the issue allegedly asserted late; (ii) undue delay by the party raising that issue; and (iii) actual material prejudice from the alleged delay. Because it requires that fact-intensive inquiry, laches generally may not be determined on a Rule 12(b)(6) motion addressed to a pleading (§III.A.1), but below, the Bankruptcy Court not only did exactly that (ruled based upon a pleading), but worse, affirmatively refused even to allow a factual record, expressly stating that it would not consider facts proffered by Appellants outside their pleading (§III.A.2). In itself, those are reasons for reversal. In fact, Appellants' proffer, together with whatever other evidence is available — including the public records in the court docket of the larger LBI bankruptcy to which the proceeding below was attached — establish that the Trustee did not and could not make a laches showing. (III.B) First, it is clear the

Trustee had knowledge of the pending §541(b)(7) issue — knowledge that precludes laches under settled Second Circuit decisions — as early as 2009, in 2015 as well, and even up to the time the proceeding below was filed after discussion with the Trustee about its form, all while never even suggesting delay on Appellants' part in any way whatsoever prior to the proceeding below arising. (§III.C) Second, there was no undue delay. Quite to the contrary, Appellants raised the issue diligently, and continued to do so at each turn, while the Trustee, for its part, (i) did nothing for six years in response to Appellants raising the issue in 2009, and (ii) even then avoided confronting the merits of §541(b)(7)'s applicability (raising only a *pro forma*, technical/procedural objection). (§III.D) Third, the Trustee not only failed to show actual material prejudice, but in fact, all available information shows that the Trustee could not identify any laches-cognizable prejudice at all. (§III.E) Finally, in light of the overriding equitable principle in laches jurisprudence that a laches finding must accomplish equity rather than its opposite, both the record presented as well as the record Appellants would create if they were allowed to have a factual evaluation would make abundantly clear that, where, as here, it is the Trustee rather than Appellants who controlled the process at every stage and who inexcusably delayed in bringing the §541(b)(7) issue to a head, it would be inequitable to deny Appellants — elderly

retirees who have been denied their principal, self-funded pensions since 2008 — the statutory rights given to them in 2005 in §541(b)(7).

Argument

I.

SECTION 541(b)(7) APPLIES TO THE ESEP PLAN

A. *The Plain Terms of the 2005 Amendment to the Bankruptcy Code's Estate Property Definition Provisions, 11 U.S.C. §§541(b)(7)(A) & (B), Apply Clearly and Unequivocally to Appellants' ESEP Pension Plan Rights and Provide that Those Rights as of 2005 Would Not Be Bankruptcy Estate Property in the Event of a Bankruptcy.*

The effect of Congress's 2005 amendment to 11 U.S.C. §541 — the bankruptcy statute titled "Property of the estate" that defines comprehensively and at length what is and is not part of a bankruptcy estate — was that pension rights such as those of Appellants were added to the list of assets that would not become bankruptcy estate property in the event of bankruptcy and would not become subject to bankruptcy court jurisdiction. The amendment is set forth in §541(b)(7)(A) & (B) and the relevant portion provides:

> "(b) Property of the estate does not include …
>
> > "(7) any amount —
> >
> > > "(A) withheld by an employer from the wages of employees for payment as contributions —
> > >
> > > > "(i) to —

> "(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 …."
>
> "or
>
> "(B) received by an employer from employees for payment as contributions —
>
> "(i) to —
>
> "(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 …."[2]

Appellants' deferred compensation in connection with the ESEP pension plan falls squarely within this definition.

Section 541(b)(7) states the simple, new rule as of 2005 that bankruptcy estates do not include pension plan funds of "an employee benefit plan that is

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[2] Section 541(b)(7)(A)(i) and (B)(i) each read in full (identically):

> "(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;
>
> "(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or
>
> "(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;
>
> "except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2) …."

subject to title I of [ERISA]." Congress stated no exclusion for Top Hat deferred compensation plans, though it, of course, would have done so in explicit and clear language had it intended to exclude them from the 2005 amendment.

Deferred compensation plans such as ESEP are without question subject to Title I of ERISA. In fact, ERISA's Title I contains a "Definitions" section specific to Title I (beginning: "For purposes of this subchapter"), and the definitions expressly include coverage of deferred compensation plans like ESEP in ERISA's Title I:

> "the terms 'employee pension benefit plan' and 'pension plan' mean any plan … to the extent [it]—
>
> (i) provides retirement income to employees, or
>
> (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond…."

29 US.C. §1002(2)(A).[3]

[3] Relatedly, the following sub-section, 29 U.S.C. §1002(3), provides: "The term 'employee benefit plan' [the precise term used in §541(b)(7)] or 'plan' means an employee welfare benefit plan *or an employee pension benefit plan* or a plan which is both an employee welfare benefit plan and an employee pension benefit plan." (Emphases added.)

ERISA's other three Titles are not germane. Title II amends the IRS Code in tandem with implementation of ERISA. *See* 26 U.S.C. §410 *et. seq*. Title III allocates jurisdiction and enforcement functions to the IRS and Department of Labor, *see* 29 U.S.C. §1201 *et seq.*, and Title IV deals with "defined benefit plans" (a different kind of pension plan) and the role of the Pension Benefit Guaranty Corporation with such plans. 29 U.S.C. §1301 *et seq*.

It has long been recognized and understood, since well before the 2005 amendment to §541, that Top Hat unfunded deferred compensation plans like ESEP are covered by ERISA generally and its Title I in particular. ERISA Title I's reporting and disclosure regulations, 29 U.S.C. §1021 *et seq*. and ERISA Title I's administration and enforcement provisions, including criminal penalties, civil enforcement and ERISA's preemption provision, 29 U.S.C. §1131 *et seq*., all unquestionably apply to deferred compensation plans like ESEP. Numerous cases have made clear as early as the mid-1990s, well before §541(b)(7) was enacted, that Top Hat plans are covered by ERISA and its Title I. *See, e.g., In re New Valley Corp.*, 89 F.3d 143, 148 (3d Cir. 1996) (addressing a Top Hat deferred compensation plan: "As a threshold matter, we have little difficulty concluding that ERISA provides the framework for our analysis. ERISA's coverage extends broadly to include all employee benefit plans"); *Paneccasio v. Unisource Worldwide, Inc.*, 532 F.3d 101, 113 (2d Cir. 2008) (holding as to a deferred compensation plan that "[p]reemption [of state law] thus applies to every plan covered by ERISA, which necessarily includes top hat plans"); *Guiragoss v. Khoury*, 444 F. Supp. 2d 649, 656 (E.D. Va. 2006) ("the Plan, which by its terms is a deferred compensation agreement, falls squarely within the definition of an ERISA employee pension benefit plan"); *Bruno v. Hershey Foods Corp.*, 964 F. Supp. 159, 163 (D.N.J. 1997) ("In this case, the parties do not dispute that both of

the plans at issue — i.e., the [Deferred] Compensation Plan and the Pension Plan — are employee pension plans covered by ERISA").[4]

As to the remainder of the text of §541(b)(7), it states that the pension funds must have been "withheld" by an employer from wages for payment as

[4] To avoid doubt, when Congress enacted the 2005 amendment, it had been long-settled that plans such as ESEP fall within that definition, as is clear in the cases discussed above. If Congress had intended §541(b)(7) to have a more narrow or limited application, it would not have described plans covered by the new statutory provision, as it did, to include "an employee benefit plan that is subject to title I [ERISA]," because it knew that that description had long-included plans such as ESEP, *see, e.g., Lorillard v. Pons*, 434 U.S. 575, 581 (1978) ("where, as here, Congress adopts a new law incorporating sections of a prior law, Congress normally can be presumed to have had knowledge of the interpretation given to the incorporated law, at least insofar as it affects the new statute"), and also knew how to use other descriptive words if that had been its intent. *See Caminetti v. United States*, 242 U.S. 470, 485-86 (1917) ("Statutory words are uniformly presumed, unless the contrary appears, to be used in their ordinary and usual sense, and with the meaning commonly attributed to them"). If exclusion of Top Hat plans such as ESEP had been Congress's intent, it would have said so by mentioning and excluding them explicitly. More still, any possible doubt is negated by the fact that Congress did not write on a blank slate in enacting the 2005 amendments in other respects, as well. Rather, it wrote the 2005 amendments in the wake of a long-standing Supreme Court judicial construction as to so-called "funded" plans — holding that *those* plans' assets are not part of employer bankruptcy estates. *See Patterson v. Shumate*, 504 U.S. 753, 759-60 (1992). *Patterson* held that "funded" retirement plans" (or non-Top Hat deferred compensation) were *already* not property of the employer bankruptcy estates and already covered by a *different* subsection of 11 U.S.C. §541, *viz*., subsection (c)(2), for reasons found in ERISA, as ERISA had been enacted in 1974. *Id*. at 759. Because *Patterson* made clear in 1992 that assets of *funded*, non-Top Hat plans, are not part of an employer/plan sponsor bankruptcy estate, there would have been no need for Congress to enact the new §541(b)(7) language if its intent were merely to do the same thing *Patterson* did 13 years earlier, limited to funded plans. Nothing in the text or legislative history suggests Congress intended to accomplish only such a narrow purpose. This makes even clearer that §541(b)(7) applies to plans like ESEP.

contributions to the employee benefit plan and/or "received" by the employer for payment as contributions to the plan. There is no serious question that the amounts voluntarily deferred by Appellants from their earned income in the late 1980s — income they were otherwise entitled to receive at that time — were withheld and received by the employer as Appellants' contributions to the pension plan. For the avoidance of any possible doubt, Appellants point out that the ESEP Agreements [A-179] expressly provide, at ¶1, that "[c]ertain compensation … shall be deferred according to the terms and conditions of this agreement," and in subsequent paragraphs setting forth such terms and conditions, repeatedly refer to such "deferral" as synonymous with compensation being "withheld."[5]

Section 541(b)(7)(A) & (B) applies as Congress wrote and enacted it, and as Appellants contend it applies here. The statute mandates, without qualification or ambiguity: "Property of the estate does not include … any amount … withheld [or received] by an employer from the wages of employees for payment as contributions … to … an employee benefit plan that is subject to title I of the

[5] *See also id*. at ¶3 (referring to "subsequent deferrals and withholdings of compensation provided for in paragraph 1" and to "the amount of compensation theretofore deferred and/or withheld as provided in paragraph 1"), ¶4 (referring to "the amount of compensation theretofore deferred and/or withheld as provided in paragraph 1") & ¶5(f) (stating that "[t]he deferral and withholding of compensation provided for herein are irrevocable unless the Administrative Committee otherwise consents").

Employee Retirement Income Security Act of 1974….” The statute unambiguously applies to Appellants’ deferred compensation pension entitlements.

B. *The Decision Below Ignores the Plain Text of §541(b)(7) and Must Be Reversed.*

The Decision below all but ignores, and certainly elides, the text of §541(b)(7) to reach its conclusion that §541(b)(7) does not apply to the ESEP Top Hat plan deferred compensation funds.[6] The Decision begins [A-407-09] with a discursive review of characteristics of such Top Hat deferred compensation plans, such as the fact that they are “unfunded” when created — in other words, not maintained in a segregated fund — and that they are afforded favorable tax treatment (taxation is deferred until pension payments are released).

There is no controversy about those basic characteristics of such Top Hat deferred compensation plans. But those characteristics do not in any way, by the plain terms of §541(b)(7), exclude such plans from §541(b)(7)’s clearly stated coverage of them. Those characteristics are irrelevant to the text.

[6] The issue presented has never been reached by any district or circuit court. Only a few other bankruptcy court decisions address the issue, all in the 2008-2010 time period. As discussed in §I.C, where all of those cases are addressed, none is binding, none has been reviewed on appeal and some disagree with one another while others simply adopt each other’s holdings without analysis.

Indeed, the Bankruptcy Court does not even attempt to state a rationale or conclusion that the clearly stated text of §541(b)(7) does not apply to a plan such as ESEP — as, in fact, it could not plausibly do so.

Instead, avoiding any discussion of the statute's actual text, and without attempt at reconciling that text with its ultimate holding that §541(b)(7) does not apply to ESEP despite its plain meaning, the Bankruptcy Court gets to its result by concluding that — statutory text aside — it sees §541(b)(7) conflicting with other statutes, and based solely on its view of that perceived conflict, it resolves the conflict in favor of negating what §541(b)(7) states:

> "Were the ESEP Committee's interpretation of section 541(b)(7) correct, it would create a conflict between the Bankruptcy Code, on the one hand, and federal tax and ERISA law, on the other hand. Stated differently, applying section 541(b)(7) to an unfunded top hat plan like the ESEP would, as the Trustee correctly points out, 'nullify the ERISA and tax code provisions that make top hat plans possible.' ([Trustee's] Motion to Dismiss, p. 22.) …."
>
> "If section 541(b)(7) did in fact remove the contributions to unfunded top hat plans from the reach of creditors, it would effectively undo the tax-exempt status of such contributions, upsetting the function and tax structure of top hat plans."

[A-410-11]

As discussed in §I.B.3, below, there is no such conflict. But if there were, the Bankruptcy Court does not have the power to resolve it as it sees fit. The Decision below itself states:

> "As the Supreme Court has directed, 'when two statutes are capable of co-existence, *it is the duty of the courts*, absent a clearly expressed

> congressional intention to the contrary, *to regard each as effective*.' *Morton v. Mancari*, 417 U.S. 535, 551 (1974)."

[A-411 (emphasis added)] That is in fact so. But the Decision below did not follow that mandate to regard each law as effective and instead simply nullified §541(b)(7)'s application to deferred compensation plans.

In the sections that follow, Appellants first demonstrate the unquestionable clarity of the application of §541(b)(7) to plans like ESEP (§I.B.1) and discuss the duty courts have to enforce such clear language (§I.B.2). Then, for the avoidance of any possible doubt, Appellants explain why the Bankruptcy Court was in any event simply incorrect in perceiving conflicts among statutes, much less a conflict such that §541(b)(7) could or should not be given effect. (§I.B.3) At bottom, the Bankruptcy Court impermissibly substituted its view of what Congress *should have* done for what it in fact *did* do.

1. *Section 541(b)(7)* Explicitly *Covers Unfunded Deferred Compensation Plans Such as ESEP and the Statute's Legislative History Confirms the Intention of Congress to Do So.*

As discussed above, employee benefit plans like ESEP — unfunded deferred compensation Top Hat plans — are unquestionably covered by the statutory language of the 2005 amendment. Appellants discuss here the most striking and direct contradiction to the Decision's stated basis for overriding that language. The Decision rests on the premise that §541(b)(7)'s exclusion from bankruptcy estates

cannot be reconciled with or applied to a deferred compensation "unfunded top hat plan like the ESEP" because characteristics of those deferred compensation plans are incompatible with other laws [A-410], but §541(b)(7) *actually explicitly includes such deferred compensation unfunded Top Hat plans in the list of plans it covers.* The Bankruptcy Court's rationale thus simply cannot be right. As also discussed here, the legislative history of §541(b)(7) confirms Congress's intent to cover and protect such plans. The Bankruptcy Court ignored these facts — inexplicably.

a. *Deferred compensation plans are covered explicitly by §541(b)(7).*

Dispositively for Appellants, the Decision's very premise — that Congress could not possibly have meant for unfunded Top Hat deferred compensation plans to be exempted from bankruptcy estates — is contradicted and defeated by §§541(b)(7)(A)(i)(II) & (B)(i)(II) *in which unfunded Top Hat deferred compensation plans are described and included expressly in the exclusion from bankruptcy estates, using the very words* "*deferred compensation plan*" (referring, in that provision, to not-for-profit and governmental plans deferred compensation plans):

> "(II) a *deferred compensation plan* under section 457 of the Internal Revenue Code of 1986…."

(Emphasis added.)

Such §541(b)(7)(A)(i)(II) & (B)(i)(II) deferred compensation plans have the same characteristics as the ESEP plan that the Bankruptcy Court held were reason to disqualify such plans from §541 exclusion for a bankruptcy estate — *viz.*, not being maintained in a segregated fund and deferred tax treatment. [A-410-11]; *see* 26 U.S.C. §457(b)(6), (e)(1)(B).[7] Because Congress, in the §547(b)(7) amendment in 2005, provided for coverage explicitly and precisely for plans with those very

[7] To avoid possible doubt, numerous decisions recognize the obvious and uncontroversial point that the deferred compensation plans expressly described in §541(b)(7)(A)(i)(II) & (B)(i)(II) necessarily include *unfunded* Top Hat deferred compensation plans, the same kind of plan as ESEP. Internal Revenue Code §457 — and, therefore, §541(b)(7) — covers a number of unfunded deferred compensation plans, including, in particular, innumerable plans of not-for-profit organizations ("any other organization … exempt from tax under this subtitle"), 26 U.S.C. §457(b)(6) & (e)(1)(B) (specifically stating, at §457(b)(6)(C), that §457 applies to deferred compensation plans where all income "remain[s] … solely the property … of the employer … subject only to the claims of the employer's general creditors"). *See In re Twin City Hosp.*, No. 10-64360, 2011 WL 2946172, at *2-3 (Bankr. N.D. Ohio July 21, 2011) (quoting language from the employer's letter to pension plan participants that "Section 457 of the Code requires that the 457(b) Plan must be 'unfunded' and plan assets must not be set aside for participants or beneficiaries" and noting that the language of the plan itself stated that it "is an unfunded plan and all Deferred Compensation, property and rights to property purchased by Deferred Compensation and all income attributable thereto remain, until paid or made available under the Plan, the sole property and rights of the Employer, subject only to the claims of the Employer's general creditors"); *see also Roundy v. C.I.R.*, 70 T.C.M. (CCH) 6, 1995 WL 394378, at *4 (1995), *aff'd,* 122 F.3d 835 (9th Cir. 1997) ("Congress specifically exempted amounts distributed from *unfunded deferred compensation plans* of tax-exempt organizations … (sec. 457 plans)" (emphasis added)); *Foil v. C.I.R.*, 920 F.2d 1196, n.33 (5th Cir. 1990) (concluding that §457 covers both unfunded and funded plans, but is primarily concerned with unfunded plans, and noting that "numerous tax texts treat §457 as related only to unfunded plans" (citations omitted)).

characteristics, the conclusion of the Court below that such plans may *never* under any circumstance result in plan funds being outside a bankruptcy estate if there were to be a bankruptcy is simply wrong and cannot stand.

The Bankruptcy Court makes no effort to address that fatal flaw in its reasoning (pointed out by Appellants below [A-103-05]). But the Decision's viability evaporates with its premise for that single, simple reason: Congress expressly included such plans in the new 2005 protection.

The Bankruptcy Court's exact proposition was, in fact, squarely rejected by one bankruptcy court, *In re Twin City Hosp.*, No. 10-64360, 2011 WL 2946172 (Bankr. N.D. Ohio July 21, 2011). There, the premise that §541(b)(7) must exclude unfunded Top Hat deferred compensation plans was also asserted. In rejecting that premise and holding that assets of an IRS Code §457 unfunded Top Hat deferred compensation plan were not part of the bankruptcy estate in that case, the court: (i) considered an unfunded not-for-profit §457(b) plan, *see id*. at *3 ("Section 457 of the Code requires that the 457(b) Plan [of the particular variety at issue in *Twin City*] must be 'unfunded' and plan assets must not be set aside for participants or beneficiaries"); (ii) recognized the plan to be a Top Hat plan, *see id*. at *4; and (iii) noted that the language of the plan itself stated that it "is an unfunded plan and all Deferred Compensation, property and rights to property purchased by Deferred Compensation and all income attributable thereto remain,

until paid or made available under the Plan, the sole property and rights of the Employer, subject only to the claims of the Employer's general creditors." *See id.* at *2. Faced with those facts — facts that the Decision below would hold to be dispositive that §541(b)(7) does *not* apply to determine that pension amounts are outside the bankruptcy estate in the event of bankruptcy — *Twin City* squarely rejected an argument precisely like the holding in the Decision below. The *Twin City* court rejected the argument because, just as the Appellants here contend, all other considerations aside, the unambiguous language of the statute simply contains no such exception for unfunded/Top Hat deferred compensation plans:

> "It is irrelevant that the 457(b) Plan may be characterized as a top hat plan or anything else. The statute excludes 457(b) plan funds from the estate…. *No case cited by the parties squarely addresses the issue, perhaps because the application of the law to the facts is obvious*…. Section 541(b)(7)(A)(i)(II) excludes all 457 plans from the estate without qualification."

Id. at *4 (emphasis added).

Bizarrely, the Decision [A-412] sought to distinguish *Twin City* for the very reason §457 defeats its reasoning. The Decision asserts that because §541(b)(7)…(II) does not mention unfunded Top Hat plans, the provision is not relevant, but in fact, the point is precisely that §457 *does in fact expressly* cover unfunded Top Hat deferred compensation plans. *See id.* & 26 U.S.C. §457(b)(6) & (e)(1)(B) (requiring unfunded status for covered deferred compensation plans). The Decision's distinction makes no sense.

It could not be simpler — in Appellant's favor. Congress expressly included unfunded Top Hat deferred compensation pension plans in the §541(b)(7) exclusion from bankruptcy estate assets as of 2005. For that reason alone, the Decision's invention of a rule, rather than reliance on anything in the statutory language, to hold that Congress did not include in §541(b)(7) *any* unfunded deferred compensation plans — whether unfunded plans such as ESEP or any others — is squarely contradicted by the statute's express language and flatly wrong, requiring reversal.

b. *Legislative history reveals Congress's intent to protect plans like ESEP.*

To round out the picture, the legislative history of §541(b)(7) offers no support to the Decision and actually contradicts it. Section 541(b)(7)(A) & (B) was added to §541(b) in 2005 as part of "The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005" ("BAPCPA"), enacted on April 20, 2005. *See* Pub.L. 109–8, 119 Stat. 23, enacted April 20, 2005. Nothing in the extensive legislative history of the 2005 amendments states or even suggests remotely that the deferred compensation and pension entitlements at issue are, despite being expressly described as covered by §541(b)(7)(A) & (B) in so many words, nonetheless *not* in fact covered by the statute. The statute must, of course, be construed exactly as it was written, but if, as the Bankruptcy Court may have

believed, it were Congress's intent to have it read in a different way, then surely there would have been some specific Congressional comment to that effect. Yet there is no such comment at all (and certainly no such legislative history identified in the Decision or by the Trustee below). As such, there is no conceivable reason for any court to do anything other than enforce the Congressional mandate by its plain terms.

More than that, the legislative history leading to the 2005 legislative amendments further confirms that §541(b)(7)(A) & (B), especially in their sub-sections (i)(I), mean what they say and say what they mean in excluding deferred compensation rights from employer bankruptcy estates. The legislative history concerning this section of BAPCPA (numbered §323 in the enacting legislation) titled this section "Excluding Employee Benefit Plan Participant Contributions and Other Property from the Estate," and stated, *inter alia*, that "Section 323 of the Act amends section 541(b) of the Bankruptcy Code to exclude as property of the estate funds withheld or received by an employer from its employees' wages for payment as contributions to specified employee retirement plans, *deferred compensation plans*, and tax-deferred annuities." H.R. 109-31 (emphasis added). ESEP is, of course, not disputed to be a deferred compensation plan. When Congress wrote that the new sub-sections of §541 would cover "an employee benefit plan that is

subject to title I of the Employee Retirement Income Security Act of 1974," it plainly included deferred compensation plans such as ESEP.

2. *It Is Well-Settled that Courts May Not Correct What They Might See as Errors by Congress.*

The Supreme Court has often stated the rule that courts may not supplant the express directives of Congress's statutes even though a court sees concerns outside the statute's text, such as the perceived conflicts with other laws on which the Bankruptcy Court based the Decision.[8]

> "[T]he limits of the drafters' imagination supply no reason to ignore the law's demands. When the express terms of a statute give us one answer and extratextual considerations suggest another, it's no contest. Only the written word is the law, and all persons are entitled to its benefit."

Bostock v. Clayton County, Georgia, 140 S. Ct. 1731, 1737 (2020) (Gorsuch, J., writing for the Court); *see also John Hancock Mut. Life Ins. Co. v. Harris Trust and Sav. Bank*, 510 U.S. 86, 110 (1993) (Ginsburg, J., writing for the Court and recognizing that while Congress's plain language in a statute as plainly read by the Court gave rise to "*substantial concerns*" about "*significant*" expected "*disruptions and costs*" in the insurance industry identified by the Department of Labor, holding nonetheless that "we cannot give [these concerns] dispositive weight. The

[8] As discussed in §I.B.3 below, in fact, the ostensible conflicts discussed by the Bankruptcy Court do not exist. There are no such conflicts. But as discussed here, even if there were conflicts, it is for Congress, not the courts, to address them.

insurers' views have been presented to Congress and that body can adjust the statute" (emphases added)).

In light of that well-settled rule, the Decision must be reversed. As demonstrated in §I.A above, the ESEP pension plan and other Top Hat deferred compensation plans are excluded from bankruptcy estate assets by §541(b)(7)(A) & (B) in plain and unequivocal language. Even the Decision does not assert otherwise.

Of course, if Congress had intended to exclude from §541(b)(7)(A) & (B) all unfunded Top Hat deferred compensation employee benefit plans, then it would have written the statute to say so explicitly, instead of writing the exact opposite. Significantly, Congress did not write on a blank slate. To the contrary, as discussed in §I.A above, the words used in §541(b)(70 had clear and settled meaning. Thus, even leaving aside the plain language of §541(b)(7)(A) & (B), in light of the existing jurisprudence in 2005 as to deferred compensation plans, it is unthinkable Congress would have used words plainly *inclusive* of plans like ESEP if it intended to *exclude* such plans.

Against this background, the Decision below is an impermissible substitution of what a court believes Congress *should have* done for a statute's *actual* text. That remedy for a court's perception of a Congressional error is too far a reach. Courts simply may not rewrite clearly stated legislative language. *See*,

e.g., *Puerto Rico v. Franklin California Tax-Free Tr.*, 136 S. Ct. 1938, 1949 (2016) ("[O]ur constitutional structure does not permit this Court to 'rewrite the statute that Congress has enacted'"); *Connecticut Nat. Bank v. Germain*, 503 U.S. 249, 253-54 (1992) ("We 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: 'judicial inquiry is complete'" (citations omitted)); *U.S. v. Kozeny*, 541 F.3d 166, 171 (2d Cir. 2008) ("Statutory construction '"must begin with the language employed by Congress and the assumption that the ordinary meaning of that language accurately expresses the legislative purpose"'" (citations omitted)).

As the bankruptcy court held in *Twin City*, discussing that part of §541(b)(7) addressed to §457 deferred compensation plans:

> "It is irrelevant that the 457(b) Plan may be characterized as a top hat plan or anything else. The statute excludes 457(b) plan funds from the estate. Put differently, it is irrelevant if there is boundless precedent on rectangles if a statute excludes squares and the subject property is a square."

In re Twin City, 2011 WL 2946172, at *4 (emphasis added). Here, there is not even such boundless precedent on metaphorical rectangles to support the Decision. There is only the Bankruptcy Court's subjective view, at its bottom, that §541(b)(7) simply should have been drafted differently. But it says what it says, and the Bankruptcy Court did not have the power to rewrite it to achieve what it believed would be a better policy outcome.

3. *The Perceived Conflicts with Other Statutes Are, in All Events, Illusory and Not Grounded in Reality.*

The Decision's conclusion that there is conflict between §541(b)(7) and pre-2005 amendment ERISA and other (tax) law governing unfunded deferred compensation pension plans is, in all events, incorrect. Indeed, the *Twin City* decision applied §541(b)(7) in 2011 exactly as Appellants request that it be applied here — to an unfunded Top Hat deferred compensation plan 100% identical to Appellants' ESEP plan in the characteristics the Decision identifies as causing conflict — with none of the shattering consequences forecast in the Decision from doing so. For the reasons above, even actual conflict would not permit a court to rewrite the 2005 amendment (if there were such conflict, Congress's plain language in an amendment would control, per the authorities discussed above in §I.B.2). But as belt and suspenders, it is demonstrated here that the ostensible conflicts mentioned in the Decision are not conflicts at all — just as *Twin City* reflects.

Rather, as discussed below, the 2005 amendment in §541(b)(7) coexists seamlessly with prior law. And as directed in the Supreme Court authority the Bankruptcy Court cited for its holding, *Morton v. Mancari*, even where there is any perceived conflict, the courts' duty is to "regard each [statute] as effective" where the two statutes "are capable of coexistence." 417 U.S. 535, 551 (1974). As the Court explained:

> "Where there is no clear intention otherwise, a specific statute will not be controlled or nullified by a general one, regardless of the priority of enactment…. The courts are not at liberty to pick and choose among congressional enactments, and when two statutes are capable of coexistence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective."

Id. at 550-51. The Decision refused to apply §541(b)(7) to unfunded Top Hat deferred compensation plans because it perceived doing so would create irreconcilable conflict with prior law in three respects: (i) the regulatory scheme for such pension plans under ERISA; (ii) the tax treatment for such plans; and (iii) the characteristic of such plans as being unfunded. None reveals any actual "conflict," much less conflict to the extent it could create judicial authority to overrule and judicially reform and rewrite §541(b)(7), rather than to allow §541(b)(7) and all of the other statutory law identified by the Bankruptcy Court to "coexist" and "be effective."

a. *There is no conflict with ERISA's regulatory scheme for Top Hat plans.*

The 2005 amendment's exclusion from potential bankruptcy estate assets of deferred compensation in connection with plans such as ESEP does not conflict with the regulatory scheme created for such Top Hat plans. Those ERISA regulations and §541(b)(7) do not even intersect at all.

The regulatory scheme, as the Bankruptcy Court notes [A-409], is reduced for Top Hat plans as compared to some other ERISA-covered pension plans. But

nothing about the §541(b)(7) protection/exclusion from bankruptcy estates has anything whatsoever to do with this regulatory treatment. The Decision identifies no interplay of one issue with the other whatsoever. In fact, there is an altered regulatory scheme for so-called Top Hat plans for the reason, wholly irrelevant here, that Top Hat plans' participants are typically sophisticated and highly placed employees who can, in substance, protect themselves in lieu of certain protections ERISA would otherwise impose in the design and operation of an ongoing plan. This has nothing to do with treatment of pension rights in bankruptcy. The Department of Labor makes this clear in language actually quoted by the Bankruptcy Court:

> "[I]n providing relief for 'top-hat' plans from the broad remedial provisions of ERISA, Congress recognized that *certain individuals, by virtue of their position or compensation level, have the ability to affect or substantially influence, through negotiation or otherwise, the design and operation of their deferred compensation plan, taking into consideration any risks attendant thereto, and, therefore, would not need the substantive rights and protections of Title I*."

U.S. Dep't of Labor, Office of Pension & Welfare Benefit Programs (ERISA), Op. 90-14A, 1990 WL 123933, at *1 (May 8, 1990) (emphasis added); quoted at A-409.

That all is so, but has no bearing at all on Congress's decision to exclude certain funds from bankruptcy estates in §541(b)(7). It creates no conflict between laws to reconcile. The bottom line is that nothing in that regulatory regime was

changed or affected by Congress in 2005, and nothing in that regulatory scheme — implemented because Top Hat plan participants are generally seen as senior and sophisticated professionals and less in need of regulatory protections in the design and management of ongoing plans — is needed to change as a consequence of the §541(b)(7) 2005 amendment's protection in the event of bankruptcy. The perceived conflict noted in the Decision does not exist.

b. *There is no conflict with tax law for Top Hat plans.*

The Bankruptcy Court also perceives conflict with tax law for unfunded Top Hat plans. [A-410][9] But again, there is no conflict, per the terms of the tax law that governs. The Bankruptcy Court notes correctly that the compensation that is deferred into a Top Hat plan is not taxed at the time of earning and deferral, but rather, is taxed when the deferred compensation is paid at a later time (typically, retirement years). [A-410] Again, nothing relevant to taxation of plans such as the ESEP plan changed in 2005 with the addition of §541(b)(7).

The issue is risk of loss, which Appellants continued to face after 2005, even with Congress's adoption of the bankruptcy-scenario protection in §541(b)(7).

[9] Significantly, the Decision relies heavily not on actual tax law but on descriptions of holdings in mostly pre-2005 cases describing tax treatment of unfunded plans. Those descriptions do not reveal conflict among statutes. The decisions themselves do not address §541(b)(7) and/or do no more than note that, prior to 2005 and §541(b)(7), some deferred compensation plans would have been treated as part of a bankruptcy estate. Section 541(b)(7) changed that.

The Decision correctly states that "the Internal Revenue Code explicitly excludes from the definition of property for purposes of assessing taxable income 'an unfunded and unsecured promise to pay money or property in the future,'" such as the ESEP pension rights, and correctly cites and quotes 26 C.F.R. §1.83-3. [A-410] Section 1.83-3 is the provision that implements the tax treatment of unfunded Top Hat deferred compensation plans — deferral until later payment. As it states, the deferral of taxation rule applies to "unfunded and unsecured" promises to pay in the future.

The policy rationale for this rule is obviously that there be risk of loss until ultimate receipt of payment. Section 541(b)(7) does not remove that risk. Section 541(b)(7) notwithstanding, Top Hat deferred compensation plans did not become "[]funded" or "[]secured" in 2005 by reason of §541(b)(7), and the employee participants remained exposed to total loss of their pension rights in myriad scenarios. Section 541(b)(7) does not negate the possibility that the employee participants would ultimately find no funds available — whether in a bankruptcy or otherwise. Total loss can occur, for example, through defalcation, corporate mismanagement, the effects on a business of a pandemic or innumerable other causes. Complete loss of that sort has always been common and occurs frequently — and the risk of such loss was in no way negated by §541(b)(7).

Thus, the same rationale for the tax treatment of plans such as ESEP that was in place before 2005 did not change when the partial protection from loss was enacted in the 2005 amendment. Once again, it is stressed that Congress could have made a different rule, but it did not, and hence, having made the new rule in §541(b)(7), there is no possible basis for a court to override that Congressional choice. But because employees in plans such as ESEP remained subject to complete loss, 26 C.F.R. §1.83-3 continued to provide for the same tax deferral as existed before 2005 for such plans.

The Bankruptcy Court discussed none of these considerations (though they were briefed by Appellants below [A-108-09]). In fact, the Decision's undeveloped/unexplained conclusion that application of §541(b)(7) to ESEP would destroy Top Hat plans is simply unsupportable. The purported statutory conflict to which the Decision points simply does not exist.

c. *There is no conflict merely because Top Hat plans are unfunded.*

Finally, the Decision [A-410] posits that Top Hat plans are understood to be unfunded as its final perceived conflict between application of §541(b)(7) to plans like ESEP and other, pre-2005 law (and cases describing that law). But as explained in the preceding section, §541(b)(7) in no way changes anything — it does not require that Top Hat plans be funded or magically turn them into funded

plans. Such plans, even with what protection §541(b)(7) provides, in no way requires that segregated funds be established or created, and such plans remain as they were prior to the amendment.

***

Had Congress intended a change or intended a different meaning for §541(b)(7) from the plain words applicable to Top Hat plans, Congress would have written the statute to deal with it expressly. It did not. The amended statutory language controls today.

The foregoing discussion establishes that there is, in any event, no conflict with other law. But to the extent conflict — or even policy inconsistency — were perceived, then *Morton v. Mancari*, as the Bankruptcy Court quoted it, directs that "[t]he courts are not at liberty to pick and choose among congressional enactments, and when two statutes are capable of coexistence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." 417 U.S.at 551. The foregoing discussion demonstrates that in keeping with that rule, §541(b)(7) must be implemented as written, just as Appellants contend.

C. *Other Decisions Mentioned, but Not Relied upon, in the Decision Do Not Change the Result that §541(b)(7) Applies to Deferred Compensation Plans Like ESEP.*

Finally, the Bankruptcy Court made positive reference to two earlier bankruptcy court decisions that declined, on different grounds, to apply §541(b)(7) to a Top Hat deferred compensation plan — *In re The Colonial BancGroup, Inc.*, 436 B.R. 695 (Bankr. M.D. Ala. 2010), and *In re New Cent. Holdings, Inc.*, 387 B.R. 95 (Bankr. D. Del. 2008), *as amended* (June 17, 2008). Significantly, the Bankruptcy Court did not endorse or adopt their reasoning as its holding. In fact, the point of mentioning those decisions seemed to be no more than that a few other bankruptcy courts had tried to get to the same result, by whatever rationale they could think of — while at the same time tacitly recognizing that the reasoning of those two decisions is unsupportable. For the sake of completeness, those two decisions are discussed here.

One, *Colonial*, expressly recognized that the plain language of §541(b)(7) includes unfunded deferred compensation plans, but held that the language should be ignored because of a perception, similar to that of the Court below, as to conflicts with other statutes. But *Colonial* went much further than the Decision below did, at least than the Decision did overtly, by holding expressly — though incorrectly — that that court had power to nullify Congress's language and would do so. The other case, *New Century*, relied on an effort to distinguish deferred

compensation plans from those covered by §541(b)(7) through a conclusion that deferred compensation is neither "withheld" nor "received" within the meaning of the 2005 amendment. But that distinction has been thoroughly discredited in other cases, including in the *Colonial* decision, as well as in *Twin City*. Deferred compensation is by its nature withheld from employees and received by their employers. More, while *New Century* holds that *no* deferred compensation plans are covered, as discussed above (§I.B.1.a), deferred compensation plans are expressly covered by the 2005 amendment. As noted, the Decision mentioned both *New Century* and *Colonial* with favor, yet it did not adopt the reasoning of either as a holding. The reasons each case fails as a rationale for the Decision — presumably the reasons the Bankruptcy Court did not follow them — are discussed here.

1. *The* Colonial *Decision Stakes Out Impermissible Territory in Concluding It May Nullify Congress's Chosen Language.*

The rationale of *Colonial* is the impermissible rationale that courts may substitute their belief as to what Congress should have written despite clear and to-the-contrary statutory language. Like the Decision below, the *Colonial* court stated the belief that §541(b)(7) is at odds with ERISA and the nature of Top Hat plans: "To exclude the assets of an unfunded plan from property of the estate … would …

fly in the face of the very purpose, structure and function of a top hat plan …. [and] place 11 U.S.C. § 541(b)(7) at odds with ERISA." *Id.* at 712.

But unlike the Decision below, *Colonial* candidly recognized that there is no plausible way to read §541(b)(7)'s text except to do exactly what it says — exclude from bankruptcy estates the assets of deferred compensation plans such as ESEP. Specifically, *Colonial* acknowledges, in a way the Decision below elides expressing clearly, that §541(b)(7)'s "plain meaning" is to include unfunded Top Hat deferred compensation plans — *viz.*, to exclude them from bankruptcy estates. *Id.* It then incorrectly, though at least forthrightly, went on to hold that it would override the plain meaning of the 2005 amendment and supplant Congress's words with a rewrite of the statutory language:

> "'*The plain meaning of legislation should be conclusive, except in the "rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters.*"' *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 242, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989) (citation omitted). '*In such cases, the intention of the drafters, rather than the strict language, controls.*' *Id.* at 242, 109 S.Ct. 1026.
>
> "The court concludes that the plan assets are not excluded from property of the estate under 11 U.S.C. § 541(b)(7)."

Id. (emphasis added).

This is an extraordinary, drastic and dangerous holding: that courts may generally override "the plain meaning of legislation" when they decide "literal application of a statute" would be "at odds with" Congress's "intentions." The

Decision below did not even go so far, leaving its reasoning to the oblique statements discussed above in §I.B that it was merely reconciling perceived conflicts, while leaving unsaid that it could not reconcile its reconciling with the "plain meaning" of the statutory language. But in fact, as discussed in §I.B.2 above, courts do *not* have that broad latitude to override and effectively revise clear statutory language even where the court perceives a need in policy or in Congress's choice of words. As Justice Ginsburg explained: if there are "substantial concerns" about the effects of a clear statute, the issue must be "presented to Congress and that body can adjust the statute." *John Hancock*, 510 U.S. at 110.

The one case cited by *Colonial* as support for its overreach is *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 242 (1989), but the *Ron Pair* decision allows no such drastic judicial revision of Congress's words. That case did, in fact, consider an argument for supplanting "literal application of the statute" where that literal application would "produce a result demonstrably at odds with the intention of its drafters," *id*. at 242 (citation omitted), but *Ron Pair* did not take, or broadly authorize, the extraordinary step of nullifying the statutory language it construed. *It actually rejected the argument for doing so.* In fact, the very limited room a court has for statutory nullification is illuminated further by the case *Ron Pair* cites, the Supreme Court's decision in *Griffin v. Oceanic Contractors, Inc.*, 458

U.S. 564 (1982), which also declined to ignore and rewrite the statutory language before it. *Ron Pair* went on to address the unique and narrowly circumscribed context before it — the overhaul of United States bankruptcy law in 1978 — and noted that Congress might in that context not have explained in detail each change in the law being made amidst that large task, leading to a presumption that courts should not attempt to "inquire beyond the plain language of the statute" just because a court perceives some error. *Ron Pair*, 489 U.S. at 240-41. *See also Life Receivables Tr. v. Syndicate 102 at Lloyd's of London*, 549 F.3d 210, 216 (2d Cir. 2008) ("[W]e must interpret a statute as it is, not as it might be, since 'courts must presume that a legislature says in a statute what it means and means in a statute what it says....' A statute's clear language does not morph into something more just because courts think it makes sense for it to do so" (citation omitted)); *Arciniaga v. Gen. Motors Corp.*, 460 F.3d 231, 236 (2d Cir. 2006) ("When a statute's language is clear, our only role is to enforce that language '"according to its terms"'" (citation omitted)).

As discussed above, if Congress had meant anything other than what it wrote, it knew how to write it, and would have. *See Ron Pair*, at 245 ("There is no reason to suspect that Congress did not mean what the language of the statute says"). In the 2005 BAPCPA amendment, Congress meant to enact and enacted new protections for unfunded pension funds, such as ESEP, in the event of

employer bankruptcy. A court may not pronounce the equivalent of "we cannot believe it," pronouncing what is in substance no more than the view of a court that it does not agree with what Congress's words plainly stated — and then act on that view to displace a statute with that court's perception of a preferred policy result.

2. *The* New Century *Decision Is Predicated upon an Unsupportable, Indeed, Tortured, Reading of the Words "Withheld" and "Received."*

Finally, the Decision gives a passing positive mention to the discredited "withheld/received" distinction first discussed in *New Century* (but again, without going so far as to adopt its discredited reasoning; indeed the decision does not even cite *New Century* for this proposition, but it is, in fact, the first case to articulate the "withheld/received" distinction and the only one to give it substantive discussion).[10] [A-411-12] In brief, *New Century* concluded that the §541(b)(7) references to funds "withheld" and/or "received" are not satisfied by *any* deferred compensation plans whatsoever, engaging in a tortured analysis of language to conclude that funds deferred from employee earnings to fund a pension are not actually "withheld" or "received" by anyone. *New Century*, 387 B.R. at 114. *New Century* reflects an unsupportable misreading of those words. It ignores the plain

[10] The Decision below cites the *Bill Heard* and *Downey* decisions mentioned above as adopting the same withheld/received analysis as in *New Century*, but each merely adopted *New Century*'s analysis of the withheld/received language without meaningful further analysis or support. *See In re Bill Heard Enterprises, Inc.*, 419 B.R. 858, 868-69 (Bankr. N.D. Ala. 2009); *In re Downey Regl. Med. Ctr.-Hosp., Inc.*, 441 B.R. 120, 131 (Bankr. App. 9th Cir. 2010).

meaning of the statute and the explicit text of agreements, such as the ESEP Agreements, and worse, ignores the fact that §541(b)(7) actually expressly covers certain unfunded deferred compensation plans — the IRS §457 plans discussed in §I.B.1.a above — within the exact, same "withheld" and/or "received" provision, while *New Century* nonetheless holds that such expressly *included* plans are nonetheless 100% *excluded*. These conclusions make no sense.

Even the *Colonial* decision discussed above — the case on which the Trustee relied most heavily below and which sought to negate §541(b)(7) by simply overriding the Congressional language — has fully analyzed and squarely rejected *New Century*'s withheld/received conclusion. Decisively rejecting and critiquing *New Century*, *Colonial* explained both the fact that §541's specific inclusion of IRS §457 deferred compensation plans (§I.B.1.a) defeats the withheld/received argument and also the fact that the withheld/received analysis in *New Century* is simply incorrect in light of the nature of deferred compensation as deferral of earned income:

> "But there are two weaknesses with [the *New Century*] view. First, 11 U.S.C. § 541(b)(7) expressly embraces certain deferred compensation plans. 11 U.S.C. § 541(b)(7)(A)(II) and (B)(II) [IRS §457 plans]. In addition, except for the voluntary election by the employees to make a contribution to the plan, they had a present entitlement to the income. The amounts deferred had been fully earned at the time the contributions were made"

Colonial, *436* B.R. at 712. These flaws in the withheld/received analysis were also identified in *Twin City*, 2011 WL 2946172, at *4–5 ("Any other linguistic machinations would serve to frustrate the clear intent of Congress").

To be clear, as explained in §I.A above, Appellants' deferred compensation was, in fact, "withheld" from them and "received" by Shearson. The *New Century* notion that deferred compensation is not "withheld" or "received" is contrary to the express language of the ESEP Agreements, which refer in numerous provisions to the deferred compensation being "withheld" and treat the withholding as synonymous with a "deferral."[11] All else aside, this glaring fact is, in itself, sufficient to reject the *New Century* distinction as to Appellants.

Notably, although citing *Colonial* in other respects, the Decision did not even mention *Colonial*'s dismantling of the logic of *New Century*. [A-411-12] The Decision's notable failure to discuss this argument, even while otherwise citing *Colonial* with favor, bespeaks the Decision's general lack of merit.

[11] *See* A-179 at ¶1 ("[c]ertain compensation … shall be deferred according to the terms and conditions of this agreement"), ¶3 (referring to "subsequent deferrals and withholdings of compensation provided for in paragraph 1" and to "the amount of compensation theretofore deferred and/or withheld as provided in paragraph 1"), ¶4 ("the amount of compensation theretofore deferred and/or withheld as provided in paragraph 1") & ¶5(f) ("[t]he deferral and withholding of compensation provided for herein are irrevocable unless the Administrative Committee otherwise consents").

D. *The Court Below Did Not Have Latitude to Rule Against Appellants for Other Reasons*.

Finally, the Bankruptcy Court, "observes that even if [Appellants] were to prevail" in arguing in arguing that §541(b)(7) removes their pension rights from the estate, that "does not create ownership rights" in and of itself. The Bankruptcy Court then states that because it "has already determined [that §541 does not apply] on the merits, the Court need not determine whether [Appellants] are correct regarding ownership" of their pension funds. [A-413-14] Thus, there was no determination of that issue, and it is not at issue here.

Appellants agree, as the Bankruptcy Court recognized, first and foremost, that the Bankruptcy Court may not make such a determination, but it may not do so precisely because of the §541(b)(7) mandate that the funds are not part of the bankruptcy estate. They are, as a consequence, not subject to Bankruptcy Court jurisdiction.

Upon reversal of the Decision based upon §541(b)(7), Appellants (and any other party claiming an interest in the funds) would, if there were any dispute, resolve it in an Article III court or some other manner to which they might agree. Today, there is no such dispute, and the possibility that there might be one cannot be addressed here in a vacuum.

Appellants note that the Bankruptcy Court makes reference in closing comments that the 1980s ESEP agreements have language to subordinate

Appellants to Bankruptcy Court creditors, but as the Bankruptcy Court tacitly recognizes by making these remarks only in *dicta*, any possible claims of others were not represented, considered, litigated or decided in the proceeding below.

But to be clear, §541 does protect Appellants' pensions. As countless authorities have recognized, the principal purpose of BAPCPA's §541(b)(7) in particular was to encourage and protect retirement savings. *See, e.g.*, 5 Collier on Bankruptcy ¶541.23 (16th Ed. 2019) (Section 541(b)(7), "which appears to apply in bankruptcy proceedings of the employee and the employer, seems intended to protect amounts withheld by employers from employees or paid by employees that are in the employer's hands at the time of filing bankruptcy" (footnotes omitted)).[12] Obviously, if Appellants' pension funds are not held to be outside the estate under §541(b)(7), the very purpose of the amendment to protect retirement savings would be defeated. If there is any issue to be litigated as to Appellants' pension funds

[12] *See In re Sibila*, Bky. No. 09–64754, 2010 WL 4365741, at *5 (Bankr. N.D. Oh. Oct. 28, 2010) ("By passing section 541(b)(7), Congress elevated the public policy in favor of retirement savings above the bankruptcy policy that favors maximum repayment to unsecured creditors"); *In re Smith*, No. 09–64409, 2010 WL 2400065, at *3 (Bankr. N.D. Oh. Jun. 15, 2010) ("the enactment of section 541(b)(7) injected a policy favoring retirement savings into the bankruptcy code"); *In re Seafort*, 669 F.3d 662, 670, 674 (6th Cir. 2012) ("It is true, as Debtors assert, that BAPCPA added new protections for retirement funds that did not exist under pre-BAPCPA law, namely … § 541(b)(7)"); *In re Vanlandingham*, 516 B.R. 628, 636-37 (Bankr. D. Kan. 2014) ("When Congress enacted BAPCPA, it sought to protect debtors' retirement resources and to encourage them to voluntarily save for retirement"); *In re Overby*, No. 10–20602–drd13, 2010 WL 3834647, at *4 (Bankr. W.D. Mo. Sept. 24, 2010) ("Congress protected retirement plans (by excluding contributions to such plans from property of the estate in § 541(b)(7)").

outside the bankruptcy estate, Appellants have ample argument that §541(b)(7), once enacted in 2005, protects them.

Judge Gardephe, in the decision being appealed in the Companion Appeal, held that if there is a finding that property is outside the estate, as Appellants contend here, then that would give Appellants *more* rights to their pensions than even a secured claim of a bankruptcy creditor:

> "[E]ven if Claimants are correct that the Lehman estate is currently holding property of Claimants that is not part of the estate under Section 541, Claimants would not have a secured claim. *See, e.g., In re Kornblum & Co., Inc.*[,] 81 F.3d 280, 284 (2d Cir. 1996) ('A PACA trust beneficiary [whose property is outside the debtor's estate by virtue of 11 U.S.C. § 54l(d)] is thereby entitled to claim trust property ahead of even creditors holding security interests in the property.') *Rather, Claimants would hold an interest in the property at issue that is superior to a secured claim*. *See id*."

Companion Appeal Dist. Ct. Dkt. 18, at 11-12. But Appellants' "superior" rights would not be honored if they were to prevail on §541(b)(7) and yet their pension funds nonetheless were to go elsewhere.

Plainly, as the Decision recognized, these issues were not litigated or decided below and are not litigated here. But if any party were to contest Appellants' rights to their pensions after reversal here, Appellants should and would prevail.

II.

NO STATUTE OF LIMITATIONS APPLIES TO A BANKRUPTCY PROCEEDING THAT WILL DETERMINE WHETHER OF NOT CERTAIN ASSETS ARE IN FACT ASSETS OF A BANKRUPTCY ESTATE, OR ELSE OUTSIDE THE ESTATE, IN ACCORDANCE WITH 11 U.S.C. §541

The Trustee moved to dismiss the proceedings below under a general federal catch-all, non-bankruptcy, statute of limitations enacted in 1990 in 28 U.S.C. §1658(a) — a statute never once applied to a bankruptcy proceeding in its 30 years. It states:

> "Except as otherwise provided by law, a civil action arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues."

As discussed herein, §1658(a) does not apply to the determinations in the administration of a bankruptcy of what belongs to the bankruptcy estate and what does not. (§A below) As well, separately, the proceeding below is not a "civil action" and does not involve determination of a "cause of action." (§B below) The §541 determination is not what §1658(a) addresses.

As discussed in §A, a bankruptcy proceeding to determine what assets are, and are not, part of a bankruptcy estate is a bankruptcy-specific matter. Section 1658(a) only applies "[e]xcept as otherwise provided by law" such as bankruptcy law governing estate property determinations. And that bankruptcy law has long been settled and consistent on this point — as common sense dictates, this essential threshold determination in a bankruptcy case of what property belongs in the

bankruptcy is not an "action" and is not a question that can be extinguished by the passage of time under *any* time limitations rule. Extensive bankruptcy caselaw establishes that this determination of the status of property — the subject of 11 U.S.C. §541 generally — is by law, and by its nature, not a cause of action subject to any statute of limitations, whether in §1658(a) or otherwise.

In addition, as discussed in §B. below, §1658(a) could not be applied here for the separate and discrete reason that, by the plain text of §1658(a) itself, it applies only to "civil actions," while the matter below was not a civil action, but a bankruptcy court proceeding unique to the bankruptcy process. Extensive case law makes clear it is not within the category of matters included within the term of art, "a civil action," to which §1658(a) applies.

Without addressing Appellants' principal caselaw or citing a single decision that has applied any statute of limitations to a determination of whether or not property belonged to a bankruptcy estate, the Bankruptcy Court became the first court ever to do so, and the first to do so under *any subpart of 11 U.S.C. §541*, much less §541(b)(7) in particular. Settled law holds that no statute of limitations applies a §541 determination. The Decision should be reversed.

A. *Section 541(b) Creates Rights Not Subject to Any Statute of Limitation.*

Contrary to the Bankruptcy Court's unprecedented holding, all other courts to consider this and any similar issue have held that the determination of whether

property is or is not part of a bankruptcy estate under §541 does not and should not have any statute of limitations. This is because the determination of property rights under §541, as under many other bankruptcy provisions, does not determine an "action" in any sense to which a statute of limitations might apply. Rather, a §541 determination is a bankruptcy-specific, statutory status to be determined in the context of bankruptcy proceedings. Indeed, in a bankruptcy, the so-called automatic stay, 11 U.S.C. §362(a)(3), prohibits any acts or claims against the bankruptcy estate/its trustee by a "civil action." The determination of the status of property within a bankruptcy — whether, when and how it is or is not part of the estate — is made as part of the bankruptcy administration process, subject to *sui generis* bankruptcy law and procedures, and by nature not subject to §1658(a)'s general federal catch-all limitations period "for a civil action arising under an Act of Congress."

1. *Caselaw Is Clear that No Statute of Limitation Applies to §541 Determinations.*

Numerous cases have confirmed this, and no limitations period has ever been held to apply to determining estate property status — not §1658(a) and not any other limitations statute. None of these authorities, which were cited below by Appellants, are mentioned at all in the Decision.

This rule that estate property determinations are not time-limited was explained, for example, in *In re Wiggins*, 220 B.R. 262 (Bankr. D.S.C. 1998). Considering expressly whether a determination that property is or is not part of a bankruptcy estate under §541 is subject to any statute of limitations — §1658 or any other — *Wiggins* held it is not. The court addressed an attempt by a trustee to challenge the claiming of certain exemptions from property by the debtor under §522(b).[13] The court approached the issue as "entail[ing] a two step process," in which, the court had to determine, first, whether the property at issue was part of the estate under §541 at all before ever needing to consider the §522(b) issues — because those issues would only be relevant if the property were held to be estate property. *Id*. at 270; *see also In re Parrish*, 02-10613C-7G, 2002 WL 31474172, at *2 (Bankr. M.D.N.C. Nov. 3, 2002) ("The property of the estate, including property added to the estate after commencement of the proceeding under subsections 541(a)(3) through (a)(7) is 'property of the estate' and can be claimed by the debtor as exempt under section 522(b)"). The *Wiggins* court then analyzed the applicable time considerations under each of these sections, holding expressly that "[a] determination of whether property is property of the estate [under §541]

[13] The debtor was arguing both that (i) certain IRA pension funds were outside the bankruptcy estate (per §541(b)), and (ii) that even if not outside the bankruptcy estate, the debtor had taken proper steps to elect to exempt them from estate property, as permitted under 11 U.S.C. §522(b), with the trustee having failed to challenge that claimed exemption in a timely fashion under FRBP 4003(b)(1). *See id*. at 269-70.

or not is the logical first step, *but it is one which has no time limit*." *Id.* (emphasis added).

The same conclusion was reached with respect to the same issue in *In re Fontaine*, ADV.LA 08-01994-BR, 2010 WL 6259993, at *7 (Bankr. App. 9th Cir. Nov. 26, 2010), *aff'd,* 472 Fed. Appx. 738 (9th Cir. 2012), where the court specified that before proceeding to consider whether a trustee had raised a timely challenge, under FRBP 4003(b)(1), to a debtor's claimed exemption under §522(b), the court had to make a *prior* determination of whether the property at issue was property of the debtor's estate *at all* under §541(a) — and, thus, subject to any claim of exemption under §522(b). *See id.* at *7. Critical to its decision was the fact that, unlike the expressly time-limited challenge to a claim of an exemption under §522, "whether a debtor or the bankruptcy estate has any interest [under §541(a)] in property claimed as exempt is one of several threshold issues" that "'has no time limit.'" *Id*. (quoting *Wiggins*).

This settled law is also found in the settled jurisprudence of the Bankruptcy Code's turnover remedy in §542, which in turn hinges on a threshold, predicate determination under §541 of whether property is or is not part of a bankruptcy estate. In other words, for a trustee to seek turnover, under §542, of estate property in third-party hands, the property must first be determined *actually to be* property of the estate under §541. *See, e.g., U.S. v. Whiting Pools, Inc.*, 462 U.S. 198, 204-

05 (1983) ("Section 542(a) is such a provision" that provides for turnover to the estate of property that "§541(a)(1) is intended to include in the estate"; *In re Norris*, 183 B.R. 437, 463 (Bankr. W.D. La. 1995) ("the property [of which the court can order turnover pursuant to §542] must be property of the estate as defined in 11 U.S.C. §541").

Critically, court after court has held that "turnover" under §542 — dependent on this §541 determination that property is or is not part of the estate — *is subject to no statute of limitations. See, e.g., In re Mushroom Transp. Co., Inc.*, 382 F.3d 325, 336-37, 343 (3d Cir. 2004) ("The turnover claim … arises under 11 U.S.C. §§542 and 543. The Bankruptcy Code does not impose a statute of limitations on turnover claims arising under these provisions" (collecting cases)); *In re Yerushalmi*, 487 B.R. 98, 107-08 (Bankr. E.D.N.Y. 2012) ("Court agrees with the Trustee that there is no statute of limitations or reach back period imposed on a trustee's cause of action to recover property of the estate under section 542 of the Bankruptcy Code…. The consequence of such a determination would be that the Trustee is entitled to demand turnover of the assets held by the QPRT because those assets are property of the estate under section 541"); *In re De Berry*, 59 B.R. 891, 898 (Bankr. E.D.N.Y. 1986) ("Undeniably, Section 542(a) has no express period of limitation within which one must sue for a turnover"); *In re Midway Airlines, Inc.*, 221 B.R. 411, 458 (Bankr. N.D. Ill. 1998) (holding that "American

recognizes that the Bankruptcy Code does not contain a statute of limitations for turnover actions pursuant to §542"); *In re Bookout Holsteins, Inc.*, 100 B.R. 427, 432 (Bankr. N.D. Ind. 1989) ("Although Congress specifically limited the time within which certain rights given by the Code must be exercised, it did not impose a statute of limitations with regard to actions under §542"). These and many other cases recognize the obvious principle that a statute of limitations is inapposite and not imposed — and serves no purpose — where the issue is bankruptcy estate property status. No party has a natural or otherwise superior right to the property which could or should vest with the passage of time.

As the varied cases above illustrate, and as the many more that frequently arise further confirm, the property in question might be in the physical possession of (i) the debtor, (ii) the bankruptcy trustee or (iii) a third party (as is often the case in turnover issues), and the question of its character and status does and should not depend upon a free-for-all, a race or a possession-as-9/10ths of the law rule.[14] The required process is correct determination of property's character and status as (possible) estate property, and the bankruptcy administration process determines that — what belongs to whom — on the timelines for any particular bankruptcy's administration; it is not subject to a default schedule set by a general federal catch-

[14] By contrast, other determinations where a *trustee* may elect to take steps based upon choices available to it, such as various avoidance rights a trustee may choose to exercise, do establish express time limitations for a trustee to take those steps. *See, e.g.*, §§544, 545, 547, 548, 549 and 553.

all limitations period that applies only "[e]xcept as otherwise provided by law," such as the ample law described here governing the time for §541 determinations, and only to "a civil action," which a §541 determination plainly is not.

2. *The Bankruptcy Court Ignored the Cases Cited as Well as Logic and Common Sense.*

Despite Appellants citing the authorities discussed in §A.1, making clear that the determination of whether property is or is not part of a bankruptcy estate "is one which has no time limit," *Wiggins*, 220 B.R at 270, the Bankruptcy Court simply ignored them. While ignoring them, it observed that Appellants "have not cited to any case addressing section 541(b)(7)," in particular. [A-417] This, of course, is because no such case exists — *no party has previously attempted an argument such as made by the Trustee here for the good reason that it would be a baseless argument*. And, of course, neither the Trustee nor the Bankruptcy Court cited any case specifically discussing §541(b)(7) and reaching a different result. There is none. It is settled law that all §541 determinations of what is or is not part of an estate has no statute of limitations. This is so for the common-sense reason that this essential determination of what property belongs to a bankruptcy estate is not a cause of action or a question that can be extinguished by the passage of time. Rather, it is a determination of the *status* of property (regardless of who holds it)

and is determined as part of the bankruptcy administration process under bankruptcy law, procedures and *sui generis* timelines.

Indeed, illustrating the non-fit of the Bankruptcy Court's holding, the Bankruptcy Court ruled that the four-year statute of limitations in §1658(a) would have established a September 2012 cut-off date (four years after the date LBI's bankruptcy commenced) [A-417-18] for Appellants' position as to §541(b)(7) — a position that had already been raised in 2009 in Appellants' Proofs of Claim — to have been raised, again, by the different procedure used below, or else be time-barred. [A-417-18] (Appellants, of course, pursued that different procedure after they had waited four years for the District Court to act in the Companion Appeal. *See* Companion Appeal Dist. Ct. Dkt. 13 & 18.) Yet, the Trustee itself chose not to address the §541 issue or Appellants' Proofs of Claim *until 2015*, *well after* the putative September 2012 deadline the Bankruptcy Court Decision applied. In fact, the Trustee itself *did not do a single thing as to Appellants' assertion of rights under §541(b)(7) until September 2015*, in the motion giving rise to the issues in the Companion Appeal. *See* Dkt. 12655. The import of the Bankruptcy Court's holding, therefore, would be that Appellants' ability to assert rights under §541(b)(7) had expired in 2012, while the Trustee did not have to reach those or many similar issues until 2015 or even later.

Compounding the absurdity, based on where matters stood in 2012, and at least through 2015, Appellants had no reason to know the Trustee would challenge their Proofs of Claim or §541 right on any ground; and if the Trustee later never did, Appellants would have received their pension funds under their unchallenged Proofs of Claim. As of 2012, they had done what was needed as of 2009 and had heard no objection from the Trustee. Retroactively applying a statute of limitations as of 2012 is thus plainly inconsistent with the *sui generis* timelines of bankruptcy proceedings generally and the specific timelines in this one in particular. This underscores the reasons the caselaw discussed in §II.A.1 above is clear that no statute of limitations, neither §1658(a) nor any other, applies to §541 determinations — not to raising, arguing or determining the §541 issues.

B. *Section 1658(a) Applies to "Civil Actions," Not Bankruptcy Proceedings Like This One.*

There is a separate and discrete reason the statute of limitations in §1658(a) does not apply here: §1658(a) applies only to "civil actions" and "causes of action" asserted in them, while a bankruptcy proceeding such as the proceeding below is not a "civil action." No decision has applied the §1658(a) limitation to *any* bankruptcy matter whatsoever since it was enacted more than 30 years ago. As explained further below, a "civil action" is a term of art that is limited to, in substance, lawsuits ("causes of action") in Article III courts (and similar state

courts) presenting such courts with litigation between a plaintiff and defendant in the commonplace, commonly understood and traditional sense. Section 1658(a)'s text, the common meaning of "civil action" in jurisprudence and the legislative history confirm that §1658(a)does not apply in bankruptcy proceedings.

Section 1658(a) states this clearly: "[e]xcept as otherwise provided by law, a *civil action* arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues." (Emphasis added.) A §541 estate property determination is not a "civil action" among litigants disputing a "cause of action," but rather, requires a unique proceeding exclusive to bankruptcy courts and law in which a bankruptcy court decides what is in the pot of assets available to pay creditors — the bankruptcy estate — and what may be retained by the bankrupt debtor (or belongs to others). These unique proceedings, often initiated by bankruptcy trustees seeking turnover, generally take the form of "adversary proceedings," the bankruptcy term of art for the proceeding below, or "contested matters," initiated through a motion in the bankruptcy case (a form in which Appellants could also have proceeded).[15] They are bankruptcy-specific processes trustees and others use

[15] Instead of the §541(b)(7) issue being addressed through a separately initiated "adversary proceeding," the parties, under FRBP 4001(a)(1), could have addressed it to the Bankruptcy Court through a form of motion known in bankruptcy as a "contested matter." *See* FRBP 9014. Appellants' motion would have been even far less similar to a "civil action;" thus, any claim that §1658 applied to it would

in myriad scenarios where bankruptcy-specific determinations are needed. They are different in kind from civil actions in Article III courts, to which §1658(a), with its statutory language — a "civil action" — was expressly directed.[16] No case has held that the term "civil action" in §1658(a) should apply to such a bankruptcy proceeding.

The limited meaning given to the term "civil action" is well-recognized in federal and state jurisprudence, confirming that §1658(a) does not apply here. By way of example, the Federal Rules of Civil Procedure, and cases construing those rules, recognize this narrow meaning. *See, e.g., Oppenheim v. Campbell*, 571 F.2d 660, 663 (D.C. Cir. 1978) ("we reaffirm the longstanding proposition that the term '"civil action" as used in s 2401(a) [containing a federal statute of limitation for suits against the United States] is a term of art judicially and statutorily defined as one "commenced by filing a complaint with (a) court," not an executive board'").[17]

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have been still more obviously untenable. This further demonstrates that §1658's "civil action" language is simply a mismatch with the bankruptcy-specific determinations uniquely needed in bankruptcy-specific proceedings.

[16] The remainder of §1658 similarly has no intersection with bankruptcy. Section 1658(b) is addressed exclusively to limitations for federal securities law fraud cases.

[17] The Bankruptcy Court tried to distinguish this and certain other cases cited herein by doing no more than reciting their general facts, apparently to make the point that they do not consider and reject application of §1658(a) to a bankruptcy matter, without any further comment. [A-417 at n.10] But, of course, there are no cases applying §1658(a) in the bankruptcy context. The point of these cases, of

FRCP 2 states that "[t]here is one form of action — the civil action," and FRCP 3 states that "[a] civil action is commenced by filing a complaint with the court."[18] These provisions plainly refer to actions initiated in district courts, not bankruptcy court determinations necessary to a bankruptcy's administration. Other subsections within 28 U.S.C. use that term in the same way. *See, e.g.*, 28 U.S.C. §1441, Revision Notes and Legislative Reports ("[p]hrases such as 'in suits of a civil nature, at law or in equity,' the words 'case,' 'cause,' 'suit,' and the like have been omitted and the words 'civil action' substituted in harmony with Rules 2 and 81(c) of the Federal Rules of Civil Procedure"). Along the same lines, the venue provisions in 28 U.S.C. §1391 have been expressly interpreted *not to include a bankruptcy adversary proceeding* when they employ the term "civil action;" bankruptcies have their own venue provisions. *See In re Enron Corp.*, 317 B.R. 701, 704 (Bankr. S.D. Tex. 2004) ("28 U.S.C. §1391(b) applies only to a 'civil action,' and does not create an independent basis for venue in an adversary proceeding; rather, 'nonbankruptcy venue statutes are available in bankruptcy only to the extent provided by the bankruptcy venue statutes themselves'").

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course — one that the Bankruptcy Court ignored — is that the term "civil action" is widely recognized to have a limited meaning.

[18] As noted above, a contested matter in a bankruptcy proceeding is initiated by filing a motion, not a complaint.

This limited meaning of the term "civil action" is widely understood in other areas of law. As a further example, state statutes of limitations referring to a "civil action" or an "action" are construed *not* to present a time bar to a claim in an *arbitration* which would be time-barred if there were no arbitration clause and it were brought in a court. *See, e.g.,* Craig P. Miller, Laura Danysh, *The Enforceability and Applicability of A Statute of Limitations in Arbitration*, 32 Franchise L.J. 26, 29 (2012) ("Numerous courts across the country have concluded that arbitrations are not 'actions'").[19]

The legislative history of §1658 further confirms this reading of the statute's limited scope. First, the legislative history explains that §1658(a) had a very specific purpose for civil actions in Article III courts, which purpose is entirely unrelated to bankruptcy matters — *viz.*, to do away with the messiness previously existing in scenarios where, for example, Article III courts "borrowed" the most

[19] *See Gannett Fleming, Inc. v. Corman Constr., Inc.*, 243 Md. App. 376, 397-99 (Md. Spec. App. 2019) ("On its face, CJP § 5-101 applies only to 'civil action[s] at law.' And arbitration proceedings are not civil actions at law…. [O]ur holding aligns with the majority view of other jurisdictions"); *Har-Mar, Inc. v. Thorsen & Thorshov, Inc.*, 300 Minn. 149, 155 (Minn. 1974) ("Based upon the special nature of arbitration proceedings and both the statutory and common-law meaning of the term 'action,' we feel compelled to hold that s 541.05(1) was not intended to bar arbitration"); *Carpenter v. Pomerantz*, 36 Mass. App. Ct. 627, 631 (Mass. App. 1994) ("As used in statutes of limitation, the word 'action' has been consistently construed to pertain to court proceedings"); *Broom v. Morgan Stanley DW Inc.*, 169 Wash.2d 231 (Wash. 2010) ("[W]e ... read the statutory language and our own precedent to conclude that arbitration is not an 'action' subject to state statutes of limitations").

analogous state or federal statute of limitations, with inconsistent results (of course), when addressing a claim under a federal law that had no limitations period. *See Jones v. R.R. Donnelley & Sons Co.*, 541 U.S. 369, 377 (2004) (citing Memorandum from R. Marcus, Assoc. Reporter to Workload Subcommittee (Sept. 1, 1989), reprinted in App. to Vol. 1 Federal Courts Study Committee, Working Papers and Subcommittee Reports (1990), Doc. No. 5, p. 10). There is obviously no similar concern in §541 bankruptcy matters, in which no such "borrowing" of limitations periods ever occurs.

Further, the legislative history does not say a word about bankruptcy matters at all, and it advises that "[s]ection [1658] provides a fall-back statute of limitations … for *federal civil actions*." 136 CONG. REC. S17, 581 (daily ed. Oct. 27, 1990) (emphasis added). More, it was enacted as part of a broader suite of revisions to various aspects of civil procedure, as part of PL 101-650, 104 Stat 5089 (1990). The term "civil action" is also used in other parts of the Bill in a manner demonstrating that it is used only in its conventional sense as a term of art, with only its limited, commonplace scope. For example, it is used in §113 to amend the language of 28 U.S.C §636 concerning "CONSENT TO TRIAL IN CIVIL ACTIONS" by magistrate judges and in §114 of the bill to add the supplemental jurisdiction language of 28 U.S.C. §1367 and refer to "any civil action of which the district courts have original jurisdiction" and "any civil action

of which the districts courts have [diversity jurisdiction]." Clearly, the meaning of "civil action" in these provisions is specifically the FRCP 2 and 3 civil action in a district court.[20]

Seeking to avoid the result that §1658(a) does not apply here, the Bankruptcy Court takes a deep, hair-splitting dive into ways that bankruptcy procedures borrow in some instances from the Federal Rules of Civil Procedure as an analog to be used where a bankruptcy procedure has similarities to an FRCP subject. But drill deeply as it may, the fact that bankruptcy procedure sometimes borrows from general FRCP rules does not bootstrap a bankruptcy proceeding into being the "civil actions" that they are not and does not extend §1658(a) beyond its more limited intended reach. The Bankruptcy Court [A-416] found it significant that the Federal Rules of Bankruptcy Procedure, which adopt some parts of the Federal Rules of Civil Procedure, use the words "civil action" in FRBP 9002(1), which addresses and implements the FRBP's adoption by reference of certain FRCP rules. But this merely refers to the occasional borrowing for some bankruptcy proceedings of the FRCP rules that apply to actual civil actions. FRBP

[20] *See also Crown Coat Front Co. v. U.S.*, 386 U.S. 503, 510-11 (1967) ("We start with the obvious: Section 2401(a) provides a time limit upon bringing civil actions against the United States. The 'civil action' referred to is a civil action in a court of competent jurisdiction…. Our initial inquiry is, therefore, when the right of the contractor in this case to bring suit in the District Court first accrued…. But, as we have said, the 'right of action' of which s 2401(a) speaks is not the right to administrative action but the right to file a civil action in the courts against the United States").

9002(1) does nothing to broaden the native meaning, scope and reach of §1658(a), and of course makes no reference to similarly borrowing §1658(a) at all. Rather, it merely implements the Bankruptcy Rules' use of certain FRCP rules by proxy in some instances. To that end, FRBP 9002(1) states the words "'[a]ction' or 'civil action' [as used in the rules] means an adversary proceeding or, when appropriate, a contested petition, or proceeding to vacate an order for relief or to determine any other contested matter" as proxies in those matters where the bankruptcy rules (FRBP) borrow from the general federal rules (FRCP). This does not turn a bankruptcy proceeding *into* a civil action.

FRBP 9002(1)'s title confirms this: it is, in fact, entitled "Meanings of Words in the *Federal Rules of Civil Procedure* When Applicable to Cases Under the [Bankruptcy] Code," and begins by stating that "[t]he following words and phrases *used in the Federal Rules of Civil Procedure* made applicable to cases under the Code by these rules have the meanings indicated *unless they are inconsistent with the context.*" FRBP 9002 (emphases added). FRBP 9002(1) provides only that, nothing more. It is by its design a bankruptcy procedural borrowing rule only — confined to the FRBP — and does not change the meaning of §1658(a) or tacitly or implicitly adopt the non-FRCP statutory provision of 28 U.S.C. §1658(a) into bankruptcy "adversary proceedings" or a bankruptcy "contested matters." It is here merely to permit FRCP terms, including "civil

action," to have an unconfusing meaning to the extent the FRBP borrows FRCP provisions that use that term. Nothing, however, turns a bankruptcy proceeding that *is not* a "civil action" into one by proxy. FRBP 9002(1) does not have that effect any more than FRBP 9002(3) — which clarifies the meaning of "clerk" where there is FRCP borrowing — would turn the clerk of the bankruptcy court into the "clerk of the district court."[21]

Numerous cases confirm that "civil actions" and bankruptcy court "adversary proceedings" are not the same thing (despite some broadly similar characteristics). The First Circuit's decision in *In re Harrington*, 992 F.2d 3 (1st Cir. 1993), illuminates the rubric set up by the bankruptcy rules and makes clear that an adversary proceeding is not a civil action:

> "An important purpose of the Bankruptcy Reform Act of 1978 *was to conform the practice and procedure* in Bankruptcy Code cases *as near as may be to ordinary civil actions*. *See, e.g.*, 28 U.S.C. § 158(c); Fed. R. Bankr. P. 7054(a), 8002 & 9002. With that aim in mind, most Federal Rules of Civil Procedure are made directly applicable in certain proceedings in bankruptcy. *See, e.g.*, Fed. R. Bankr. P. 7001-7071 (adversary proceedings), 9014 (contested matters). The Bankruptcy Rules recognize three distinct types of proceedings within a bankruptcy case: adversary proceedings,

[21] The Trustee made numerous other non-fit arguments in its effort to improperly import §1658(a) here. One example is worth noting because it is so wrong. It will occasionally occur in bankruptcy that a cause of action that arose pre-bankruptcy, and would have been time-barred before the bankruptcy, is nonetheless later proposed for resurrection in the bankruptcy. A bankruptcy court would, of course, recognize the time-bar that arose pre-bankruptcy. That in no way is reliance on §1658(a), though the Trustee bizarrely argued below that that scenario is reason to believe §1658(a) applies here, citing, for example, *In re Dunn*, 50 B.R. 664 (Bankr. W.D.N.Y. 1985). The argument was another nonstarter.

> administrative proceedings, and contested matters. *Adversary proceedings are most like ordinary civil actions*; contested matters are substantially similar; whereas most administrative proceedings are quite dissimilar to ordinary civil actions."

Id. at 6 (emphases added). "Most like" a "civil action" is not the same as "*is*" a civil action. Being "like" something is by definition not being the same thing. S*ee also In re Sun Healthcare Group, Inc.*, 2004 WL 941190, at *1 (Bankr. D. Del. Apr. 30, 2004) ("Adversary proceedings in bankruptcy cases are *procedurally analogous* to civil actions filed in district courts") (emphases added); *In re New Cent. TRS Holdings, Inc*, 07-10416 KJC, 2011 WL 1811050, at *2, n.4 (Bankr. D. Del. May 10, 2011) (same); *In re Gens*, 15-BK-53562, 2018 WL 4353086, at *1 (N.D. Cal. Sept. 12, 2018) (distinguishing bankruptcy adversary proceedings from ordinary civil actions in federal district court: "The dispute has spawned multiple bankruptcy proceedings and civil actions in which Ms. Gens has challenged Wells Fargo's rights to collect payments on the loan or foreclose on the Property").

Other courts have expressly recognized the distinction between adversary proceedings and "civil actions" for purposes of service of process. *See, e.g., In re Salau*, CV 1:15-11080, 2016 WL 183704, at *2 (S.D.W. Va. Jan. 14, 2016) ("As noted above, the service of process at issue relates to an adversary proceeding, rather than a [non-adversary] bankruptcy proceeding or a civil action. An adversary proceeding filed in bankruptcy court is governed by Part VII of the Federal Rules of Bankruptcy Procedure…. As a result, 'the provisions on service

of summonses and complaints by a United States marshal apply to civil actions filed in District Court, not to adversary proceedings filed in Bankruptcy Court'"); *In re Lindsey*, 177 B.R. 748, 749 (Bankr. N.D. Ga. 1995) ("The provisions on service of summonses and complaints by a United States marshal apply to civil actions filed in District Court, not to adversary proceedings filed in Bankruptcy Court").

At bottom, §1658(a) is not one of the Federal Rules of Civil Procedure at all, much less one of those rules specifically borrowed into bankruptcy proceedings by FRBP 9002 as convenient analogs. No case (except the Decision below) has mistakenly used FRBP 9002 to extend the reach of §1658 or any similar statute to bankruptcy court adversary cases or contested matters.[22]

[22] The Bankruptcy Court [A-416] also misplaces reliance for a similar reason on *In re Yelverton*, No. 09-00414, 2014 WL 7212967 (Bankr. D.D.C. Dec. 17, 2014), *as amended* (Dec. 19, 2014), *subsequently aff'd sub nom. U.S. ex rel. Yelverton v. Fed. Ins. Co.*, 831 F.3d 585 (D.C. Cir. 2016). The case stated the uncontroversial proposition, in a factual context with no relevance to this one, that "[t]he 'adversary proceeding' label the civil action carries in the bankruptcy court is of no import, as it merely distinguishes the civil action from a "contested matter" (the other category of civil proceedings tried in the bankruptcy court, and as to which less formal procedures apply)." *Id*. at *1. The case merely addresses differences in bankruptcy between two bankruptcy processes: the adversary proceeding and the contested matter. Nothing in that statement extends the federal catch-all limitations statute in §1658(a) to anything in bankruptcy. The words quoted are nothing more than a loose formulation unrelated to the question presented here. Notably, the *Yelverton* case, goes on to confirm this point. (contrasting adversary proceedings and contested matters):

III.

THE COURT BELOW ERRED IN INVOKING THE DOCTRINE OF LACHES

Finding laches requires a fact-intensive inquiry — an affirmative defense with movant satisfying a burden of persuasion on three elements. *See, e.g.*, *Pecorino v. Vutec Corp.*, 6 F. Supp. 3d 217 (E.D.N.Y. 2013) ("Because laches is an affirmative defense, a defendant asserting laches bears the ultimate burden of persuasion, even where a presumption of laches may apply"); *Masterson v. NY Fusion Merchandise, LLC*, 300 F.R.D. 201, 206 (S.D.N.Y. 2014) ("In order to succeed on a defense of laches, a defendant has the burden" of proving its elements). Specifically,

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> "In this instance, Federal Rule of Bankruptcy Procedure 7001 required that the civil proceeding be treated as an adversary proceeding in which the bulk of the Federal Rules of Civil Procedure applicable to a civil action are made applicable (including the requirement of filing a complaint). In other words, an adversary proceeding *is the analog of a civil action in the District Court*. In contrast, contested matters are governed by Federal Rule of Bankruptcy Procedure 9014 (which, for example, dispenses with the requirement of filing a complaint). A contested matter is a civil proceeding, but is generally not viewed as the equivalent of a civil action with all of the pleading requirements a civil action entails."

Id. at *1, n.4 (emphasis added). An "analog" of something is merely that — an "analog," not the thing itself. As such, the Bankruptcy Court's citation to *Yelverton* makes Appellants' point: an "adversary proceeding" may be a bankruptcy-specific "analog" of a civil action, within the confines of bankruptcy cases, but it is *not itself a civil action*. FRBP 9002 does not extend §1658(a)'s reach into bankruptcy cases where nothing indicates it was meant to apply.

> "[a]n equitable action is barred by laches under New York law where the following exist: (1) proof of delay in asserting a claim despite the opportunity to do so; (2) lack of knowledge on the defendant's part that a claim would be asserted; and (3) prejudice to the defendant by the allowance of the claim…. Moreover, '[i]n order to show that he has been prejudiced, a defendant must show reliance and change of position resulting from the delay.'"

Rapf v. Suffolk County of New York, 755 F.2d 282, 292 (2d Cir. 1985). Not one of these three elements is established on the record below.

Moreover,

> "[a]s laches is an equitable doctrine, it is not established by undue delay and prejudice, which 'merely lay the foundation for the trial court's exercise of discretion.' *A.C. Aukerman Co.*, 960 F.2d at 1036. The defense may be denied when there is evidence of other factors which would make it inequitable to recognize the defense. *Id."*

Masterson, 300 F.R.D. at 206; *see also Hoehn v. Crews*, 144 F.2d 665, 671 (10th Cir. 1944), *aff'd sub nom. Garber v. Crews*, 324 U.S. 200 (1945) ("Since laches is an equitable doctrine, its application is controlled by equitable considerations. It cannot be invoked to defeat justice and will be applied as a defense only where the enforcement of the asserted right would work injustice"). Equitable considerations, explained below, also preclude a laches holding here.

But even before reviewing those three elements and general equitable considerations, the laches inquiry should end quickly in Appellants' favor because laches was found in the extraordinary circumstance of a motion to dismiss with no

factual record permitted by the Bankruptcy Court. As discussed in §A, that is contrary to the law of laches.

Disregarding this body of law entirely, the Bankruptcy Court in this case made an extraordinary laches determination on a motion to dismiss and *expressly refused* to consider the facts offered by Appellants, as discussed at §A.1 and A.2. [A-386] More, it did so in circumstances where it had expressed a clear *ex parte* predetermination of the merits and a stated intention to close out this case in 2020, as Appellants discussed in a now moot motion to recuse and as is explained at §A.3. Those *ex parte* remarks cast a harsh light on the Bankruptcy Court's refusal to allow a factual showing. That refusal was *especially* inappropriate given the byzantine, fact-intensive path along which this issue has unfolded — a long story involving the Trustee's knowledge and control and own choices and the resulting equities (and inequities) precluding laches.

The facts proffered (those ignored by the Bankruptcy Court) are summarized in §B. Turning to the three elements of laches discussed by courts, including this Court, in cases like *Rapf, supra*, as discussed at §C, the Bankruptcy Court inexplicably disregarded entirely — and did not discuss in the Decision — the critical element of the Trustee's clear knowledge that the substance of the §541(b)(7) issue would need to be addressed and resolved. That element of the

laches defense — lack of such knowledge, which the Trustee could not possibly satisfy — squarely precludes its laches defense.

The Trustee also did not meet his burden of persuasion on the elements of undue delay (§D) or material prejudice (§E). As to undue delay, the undisputed procedural history, including filings in the main LBI bankruptcy case, show that, if anyone, it is *the Trustee*, not the elderly retirees who are Appellants here, who inexcusably delayed in raising any issue as to §541(b)(7) protection. Appellants' Proofs of Claim filed in 2009 would, in accordance with 11 U.S.C. §502(a), have entitled Appellants to their full pension payments based on §541(b)(7) unless and until the Trustee raised an objection — which it did not do until *six years later*, in 2015. For this and many other reasons, resolution was delayed as a direct result of the Trustee's own deliberate litigation choices. As to material prejudice, the Trustee made no showing of prejudice in the sense the term is used in laches jurisprudence, such as lost evidence or adverse, irreversible choices made in ignorance of the issue later raised in a surprise. There is no such prejudice — on this record or otherwise. Further, the Trustee did not even attempt to make a showing that its two proffered bases for claimed prejudice — allegedly increased litigation costs from *seriatim* rather than in-tandem litigation and alleged delay in the closeout of this bankruptcy — are, in fact, real. Indeed, as discussed at §E, the Trustee's own filings in the record in this case show they are not.

Finally, as discussed in §F, "other factors" make any application of laches to preclude Appellants from having determination of their §541(b)(7) protection "inequitable." If they are correct on the merits, as §I shows they are, the circumstances overall do not warrant the unconscionable result sought by the Trustee — that the issue not even be determined. It is they, not the Trustee, who have suffered gravely from the 12+-year delay in the payment of their earned pensions. The Trustee and its experienced bankruptcy counsel delayed for of over six years, until 2015, in challenging the Proofs of Claim assertion of §541 protection in any respect, and even then did so only on a procedural ground rather than the merits. The Trustee controlled the schedule. Finding laches in these circumstances is grossly inequitable.

A. *The Bankruptcy Court's Finding of Laches Should Never Have Been Made in the Absence of a Full Record Involving Fact-Finding as to the Kinds of Facts Summarized Here.*

1. *Laches Cannot Be Found Where Consideration of Facts Was Required, but Not Permitted, by the Court.*

As noted above, laches is a fact-intensive affirmative defense almost invariably not amenable to resolution on a pre-discovery motion to dismiss. Under FRCP 8(c), applicable below per FRBP 7008, "laches is an affirmative defense … and properly should be raised in the defendant's answer and not upon a motion to dismiss." *Karlen v. New York U.*, 464 F. Supp. 704, 708 (S.D.N.Y. 1979). The

affirmative defense requires evidentiary proof by a movant, which an opponent can contest. "[A] determination that a claim is barred by laches requires a factual inquiry into the reasons for plaintiff's delay and the extent and nature of the prejudice suffered by defendant as a result …. [T]his inquiry is inappropriate on a motion to dismiss." *Deere & Co. v. MTD Products, Inc.*, 00 CIV 5936 LMM, 2001 WL 435613, at *2 (S.D.N.Y. Apr. 30, 2001); *see also Broad. Music, Inc. v. Liberman Broad., Inc.*, 16 CIV. 2266 (LLS), 2016 WL 3919654, at *2 (S.D.N.Y. July 14, 2016) ("Dismissing on the grounds of laches pursuant to Fed. R. Civ. P. 12(b)(6) is anomalous because: 'a ruling on the defendant's defense of laches would necessarily involve a fact-intensive analysis and balancing of equities that would require the Court to consider matters outside of the pleadings that are in dispute'"). Even a "multi-year delay" is not "*per se* unreasonable and inexcusable," and where "[t]o determine whether plaintiffs' delay in initiating this action was unreasonable and whether defendant was prejudiced by this delay would necessitate the consideration of factual circumstances beyond the Complaint, [this is] an improper action at this stage of the litigation." *Alston v. 1749-1753 First Ave. Garage Corp.*, 12 CV 2676 DRH GRB, 2013 WL 3340484, at *4 (E.D.N.Y. July 2, 2013).

In this largest bankruptcy in U.S. history, where the path the Trustee and Appellants took to get to this point is byzantine, starting with the filing of the

Proofs of Claims in 2009, 11 years ago, and involving many intervening motions, appeals and much communication between them, it is gross understatement to say that *this* particular assertion of laches by the Trustee involves circumstances that are fact-intensive. They cry out for discovery and a factual record if there were not outright reversal of the Decision based upon Appellants' other arguments.

2. *The Bankruptcy Court Erred in Expressly Refusing to Allow a Factual Record, Even Though Appellants Made an Extensive Proffer of Relevant Facts.*

The Bankruptcy Court committed reversible error per the authorities discussed above because it refused to consider any factual development, despite Appellants' proffer of a record of pertinent facts made to the Bankruptcy Court in briefing. Faced with the inability to present facts on a 12(b)(6) motion, Appellants, opposing the motion below, presented a 20-page, necessarily partial-only, proffer of what the facts, if adduced on a proper record, would show. [A-129-49] The Bankruptcy Court ignored this proffer entirely and, at oral argument, pointedly stated that it would not accept anything "in the nature of a proffer" because "[t]his is a motion to dismiss." [A-386]

Despite there being certain narrow exceptions to the general rule, "when the defense of laches is clear on the face of the complaint" so that "a court may consider the defense on a motion to dismiss," *Lennon v. Seaman*, 63 F. Supp. 2d 428, 439 (S.D.N.Y. 1999), this case presents no such exception. Appellants'

proffer describes facts outside their pleading which, together with the Trustee's own discussion of the circumstances at issue [A-36-39, 43-47], confirms that there are myriad facts to be considered here. The Bankruptcy Court's refusal to consider those facts requires reversal. *See, e.g., Deere & Co.*, 2001 WL 435613, at *2.

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For purposes of this appeal, the evidence proffered by Appellants, including references to the docket in the LBI bankruptcy to which the proceeding below is attached, is discussed generally in §III.B and also in the remaining arguments in §III.

3. *The Bankruptcy Court's Refusal to Recuse After Making* Ex Parte *Comments Reflecting Predetermination of the Motion Against Appellants Should Be Weighed by this Court in Reviewing the Decision.*

Before turning to Appellants' proffer and their reasons the Trustee did not satisfy the three *Rapf* elements of laches, Appellants note they also appealed [A-425] denial of a motion for the Bankruptcy Judge to recuse [A-304] — a motion made after the Bankruptcy Court had an *ex parte* colloquy, on the record, with Trustee's counsel. The Court's statements showed predetermination of the issues below, *before they were briefed or submitted*, in favor of the swiftest possible expungement of Appellants' §541 rights.

To be clear, recusal is, of course, now moot as a practical matter given this Court's acceptance of this appeal for direct appeal. To be clear on a separate issue, Appellants did not assert personal malice or improper motive, but rather, improper predetermination informed by extraneous considerations — here, expediency — to reach a result, even if contrary to the merits.[23] While recusal as such is now moot, Appellants submit the issue informs this Court's review of the laches holding.

The comments at issue were made at a hearing on December 17, 2019, on an attorneys' fees application in the LBI bankruptcy for the Trustee, with Appellants' counsel neither present nor expected. [A-221] The Bankruptcy Court, *sua sponte*, initiated discussion with the Trustee's counsel concerning the merits of Appellants' §541 position [A-231-235], in which the Court expressed its views that Appellants were wrong, would lose before the Court and should lose quickly:

> "I mean, if this were any other situation — and I'm not sure why it doesn't pertain in this situation, but I defer to you — this would be a situation where it might be appropriate to talk about sanctions. This has now become, in my view — subject to someone telling me something else — this is frivolous litigation…. And it's costing the estate a lot of money. And it's costing the

[23] *See* 28 U.S.C. §455, which governs recusal issues — providing for recusal where there is a basis to conclude "the judge's impartiality might reasonably be questioned," §455(a), and a basis to conclude the judge harbors "prejudice or bias concerning a party," §455(b). *See, e.g., U.S. v. Antar*, 53 F.3d 568, 575-76 (3d Cir. 1995), *overruled on other grounds*, *Smith v. Berg*, 247 F.3d 532, 534 (3d Cir. 2001) (recusal required based upon a showing of predetermination, where trial court stated, *post-jury trial and post-criminal convictions*, it had the motive of reaching a result to benefit parties allegedly defrauded by the moving defendants with appearance of partiality contrary to the interests of the moving defendants).

> legitimate creditors money…. I would like to be able to close the case in 2020. There is no impediment to that, as far as I can tell."

[A-234-35] It is manifest that *ex parte* statements to Appellants' adversary, when the Trustee's motion to dismiss had not yet been submitted or read, reveal an improper predetermination, based upon: (i) the reference to the Court viewing this unbriefed issue as "frivolous litigation," (ii) the suggestion that "it might be appropriate to talk about sanctions," (iii) the reference to Appellants — *LBI retirees being threatened with the loss of their fully earned pensions* — as something other than "legitimate creditors" and (iv) the stated desire to "close the case in 2020," to which the Court saw "no impediment." The Court even went on to speculate with Trustee's counsel how the District Court appeal of the certain-to-come dismissal order could be resolved more quickly than other appeals had been [A-234] and told the Trustee that "we share the same goal" in a quick wrap-up to the issue. [A-236] Such comments are chilling to other parties, grossly improper and above all reflect, at a minimum, a very "reasonable question" as to "impartiality" under §455(a).

The Bankruptcy Court's refusal to recuse, and its appeal by Appellants, became moot upon direct appeal to this Court. But for present purposes, that Court's *ex parte* comments, expressing certain predetermination and intention to close out the case in 2020, weigh heavily in discrediting the Bankruptcy Court's laches determination.

B. *The Relevant Facts, to the Extent Known to Appellants on this Pre-Discovery Motion to Dismiss, Preclude Any Finding of Laches.*

The space limitation of appellate briefing and the lack of a true record preclude full discussion of relevant facts. Appellants, therefore, refer the Court to their discussion in their proffer in the Bankruptcy Court [A-129-49], but present a summary here of their proffer and the kinds of facts that a full laches analysis would have needed to consider (including matters on the LBI bankruptcy docket):

- As described above, Appellants are hundreds of elderly retirees. At the beginning of this bankruptcy, they faced the obstacle of identifying and tracking each other down in order to organize to retain counsel and file claims. But the Trustee began its over-a-decade-long process of obstruction, first by even refusing to let them know each other's contact information (Judge Peck (originally presiding) ordered disclosure). *See* Dkt. 353 at 3, 4 & 8.
- Once a group had organized, it retained prominent bankruptcy attorney Bruce Bennett and his firm, Hennigan Bennett & Dorman. Mr. Bennett filed essentially identical Proofs of Claim on behalf of the group members in May 2009. *See, e.g.*, Dkt. 12655, Ex. B.
- Consistent with authority that permits property outside a bankruptcy estate to be treated as equivalent to secured property, discussed in the Companion

Appeal Dkt. 36, at 18-23, the Proofs of Claim identified secured status as to the ESEP entitlements because §541(b)(7) placed such assets outside the bankruptcy estate.[24] That procedure is at issue in the Companion Appeal.

- No action whatsoever was taken on these Proofs of Claim until the Trustee sought subordination in the bankruptcy of these claims *four+ years later*, in summer 2013.
- As of that time, the §541(b)(7) issue raised by the Proofs of Claim, and whether these assets were in the bankruptcy estate at all, was not mentioned by the Trustee.
- By 2013, Mr. Bennett had left his firm for another, his old firm merged or disbanded and neither he nor anyone else was acting as counsel.
- A new group had to be organized, which retained Appellants' present counsel "for the limited purpose of opposing the efforts of the Trustee to subordinate their certain claims," Dkt. 8234 — a different issue from that here, and an alternative ground for recovery as secured creditors.

[24] The claims were filed as secured, with an express statement that "the amounts [at issue were] contributed to the [ESEP] Plan by … [claimant] and/or withheld from … [claimant's] compensation pursuant to the Plan" and that, *inter alia*, "sections 541(b)(7) and/or (8) of the Bankruptcy Code apply to the amounts withheld by the Debtor or contributed by the … [claimant] to the Debtor under the [ESEP] Plan." Dkt. 12655, Ex. B. It also stated that "[m]any of the facts necessary to determine whether this is a secured claim are in the possession of the Debtor and/or its predecessors or successors in interest and are not currently known to [claimant]." *Id.*

- The ESEP agreements contained an arbitration clause targeted specifically at subordination disputes. [A-184] The group sought arbitration as the quickest path to a resolution, but the Trustee opposed it, *see* Dkt. 9287, with the result that the litigation of the subordination issue, with its multiple levels of appeals, took until October 2019 to resolve. The Bankruptcy Court exercised discretion to negate the bankruptcy-specific arbitration clause, *see* Dkt. 9617, and this Court ultimately upheld that discretionary act. *See In re Lehman Brothers Holdings Inc.*, 663 Fed. Appx. 65 (2d Cir. 2016) (unpublished).
- While that dispute was pending, the Trustee's attorney called the group's counsel informally in April 2015, seeking to have the claims reclassified from secured to unsecured. That issue was beyond the scope of Appellants' counsel's limited notice of appearance and retention and came out of the blue. *Notably, this was the first time since the Proofs of Claim were filed in 2009 that the Trustee sought to raise the issue of the claims' proper classification — the issue implicating §541(b)(7) — or anything else about them at all.* Even so, in that discussion, the Trustee made no mention of §541(b)(7). [A-142]
- Later that year, the Trustee moved formally "for reclassification," but on purely procedural grounds that the §541 issue ostensibly did not lead to

proof of claim secured status. The Trustee did not address the ultimate issue asserted, *viz.*, §541(b)(7)'s applicability on the merits. *See* Dkt. 12656. (This motion is the subject of Companion Appeal, and the nuances of the procedural issue are addressed there.) Although it quoted the language from the Proofs of Claim expressly invoking §541(b)(7), *see* Dkt. 12656 at ¶13, it pointedly took pains not to address the merits of §541's application, making, instead no more than a statement that "[b]ased on analysis by the Trustee's counsel …, the Trustee has determined that the Claims … should be reclassified." *Id*. at ¶21.

- When Appellants asked for that analysis, the Trustee refused to provide it. *See* Dkt. 12833, at ¶4.
- In its reply brief on the reclassification motion, the Trustee actually expressly acknowledged that it was aware of, but had made the deliberate choice *not to address*, the substance of the §541(b) issue, and, of course, it understood the issue in need of resolution:

> "It is true that the Trustee did not directly address in his Motions the assertion in the proofs of claim that the Claims were secured … if it is determined that wages withheld by LBI or contributed to LBI or life insurance policies are not part of the estate due to the provisions of ERISA or sections 541(b)(7) and/or (8)."

Dkt. 12942, ¶2, n.4.

- The Bankruptcy Court granted the Trustee's reclassification motion, *see* Dkt. 13053, and on appeal to the District Court, Appellants again made the substantive §541(b)(7) issue clear: "[I]f the property at issue, *viz.*, the … Claimants' earned compensation that was transformed into contributions toward deferred retirement benefits per the applicable plan, is held to be outside the debtor's estate per 11 U.S.C. §541…." Companion Appeal Dist. Ct. Dkt. 13, at 4.
- Thus, the merits of §541(b)(7) were plainly recognized by both sides to be in need of resolution in their respective court papers.
- As to the procedural issue on appeal, marshalling caselaw, Appellants argued: "[m]any reported decisions discuss that a secured claim may, in various circumstances, be treated as equivalent to property in which an estate holds, similarly, only a legal but not an equitable interest pursuant to §541." *Id*. at 4-5, n.1 (collecting cases).
- The appeal was fully briefed by February 2016, *see* Companion Appeal Dist. Ct. Dkt. 13, but Judge Gardephe's decision did not come until September 30, 2019, *an almost four-year wait*. *See* Companion Appeal Dist. Ct. Dkt. 18.
- That timing, of course, was beyond the control of either party. It was clear, however, that the next step for both parties was bound up with the issue before Judge Gardephe. If he had held (and were to have been affirmed on

appeal) that §541(b)(7) can give rise to the equivalent of a secured claim, then the §541 claims would proceed as secured, and it would have then been incumbent upon the Trustee at that point, if it wished to contest Appellants further, to dispute, finally, the substantive issue of whether §541(b)(7) covered these claims. If, on the other hand, Judge Gardephe had held, as he, in fact, did (and were to be affirmed on appeal), that §541(b)(7) does not give rise to the equivalent of a secured claim but only a claim that property was outside the estate, then the substantive issue would be determined under different bankruptcy procedures, *i.e.*, in a contested matter or an adversary proceeding.

- Either way, it was self-evident in 2015 that the issue would need to be determined either under the Proofs of Claim or under other procedures.
- The parties simply — and perfectly reasonably — had no inkling they would be facing a nearly four-year wait for Judge Gardephe's decision. Had his decision been issued within a year rather than four, surely no laches defense would have even been asserted.
- As the four-year wait continued, Appellants, then 10+ years with no pensions, reached out to the Trustee in the summer of 2019 to break the logjam. They suggested going forward with a proceeding finally to address §541's merits without waiting for Judge Gardephe's decision. Both counsel

negotiated about the form such a proceeding would take. [A-222] Up to this time, *there had never been any suggestion that the long-pending issue should be raised in a different way, much less any mention that, if it were not, there would be a claim of delay or laches*. [A-131-32]

- Judge Gardephe's decision was issued soon after, coincidentally, while Appellants were preparing the pleading for the proceeding below, so that Appellants filed the proceeding shortly after receiving that decision.
- Judge Gardephe held that if §541(b)(7) applied, it would not give rise to a secured claim, but it *would* create "an interest in the property at issue that is superior to a secured claim" of a bankruptcy creditor. *See* Companion Appeal Dist. Ct. Dkt. 18 at 11-12. The District Court in no way stated or suggested that the substantive §541 rights to that "superior" position had lapsed while its decision was pending.

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It is clear from these facts that during this many-years-long bankruptcy in which the Trustee was in control of *what* would happen and *when*, despite the fact Appellants had raised the applicability of §541(b)(7) to their pensions from the very outset, the Trustee inexplicably did not take up the issue *at all* until 2015, and even then pointedly refused to address the substance at every opportunity. It knew the issue would need to be determined. But throughout these many years, the

Trustee not only did not act to resolve it but also did not at any point state or suggest, directly or obliquely, that it would raise a laches defense if Appellants did not act in some different way.

Those facts show that the Trustee could not carry its burden to prove any of the three elements of laches — lack of knowledge, undue delay or material prejudice — discussed in turn below.

C. *The "Knowledge" Element of the Laches Doctrine Squarely Forecloses Any Finding of Laches on this Record.*

The Court must reverse the laches holding for one single, very simple reason, without needing to reach the case's long and complex procedural history — the Trustee had knowledge the issue was in play and needed determination. This Circuit Court has a bright line rule that if a party knew or should have known that an issue would be asserted, it has no laches defense.

The Decision's laches discussion (and the Trustee's motion) inexplicably failed to address this rule at all,[25] but there is no dispute it bars a laches finding. Although not mentioned in the Decision, this factor of "knowledge," *i.e.*, the movant's lack of it, is an independent element of a laches defense as to which a showing must be made. *See, e.g., Rapf*, 755 F.2d at 292 ("An equitable action is

[25] The Trustee made a *pro forma* statement, in a reply brief with no submission of any sworn or other proof, denying knowledge. [A-278] That is neither evidence nor an explained, cogent evidentiary denial that could be credited and taken into account in a laches analysis.

barred by laches under New York law where the following exist: … *lack of knowledge on the defendant's part that a claim would be asserted* …. Moreover, '[i]n order to show that he has been prejudiced, a defendant must show reliance and change of position resulting from the delay'" (emphasis added)); *In re Drexel Burnham Lambert Group, Inc.*, 157 B.R. 532, 535 (S.D.N.Y. 1993) ("In the Second Circuit, the laches doctrine considers the following factors: … lack of knowledge on the defendant's part that a claim would be asserted"); *In re Schultz*, 250 B.R. 22, 38 (Bankr. E.D.N.Y. 2000) (recognizing "lack of knowledge" element of laches defense and refusing to apply laches where, *inter alia*, "the Debtor and his counsel were on notice that the Trustee was analyzing the value of the accounting practice as early as February 19, 1998, when a written demand was made for documents regarding the practice…," even though the trustee initiated an adversary proceeding as to the issue only substantially later).[26]

The Trustee knew at the virtual outset of the LBI bankruptcy in 2009, when Appellants filed Proofs of Claim, that Appellants contended that §541(b)(7) applied to their pension rights. This was just as clear in 2015, when the Trustee

[26] Even *imputed* knowledge is sufficient reason to reject a laches defense. *See, e.g., In re Dark Horse Tavern*, 189 B.R. 576, 581-82 (Bankr. N.D.N.Y. 1995) ("[I]n light of the fact that Frederick commenced a state court dissolution proceeding prior to the filing of the Petition, Debtor *knew, or should have known*, that Frederick would likely oppose a plan of reorganization. Debtor should also have become aware of Frederick's objections when he revoked the general power of attorney on June 17, 1993, shortly after the filing of the Petition" (emphasis added)).

first sought to challenge the Proofs of Claim, though solely on procedural grounds, as discussed in the Companion Appeal. As discussed above, it even explained in its reply brief on that motion that it had made a deliberate, conscious choice *not* to address the merits of the §541(b)(7) issue:

> "It is true that the Trustee did not directly address in his Motions the assertion in the proofs of claim that the Claims were secured … if it is determined that wages withheld by LBI or contributed to LBI or life insurance policies are not part of the estate due to the provisions of ERISA or sections 541(b)(7) and/or (8)."

Dkt. 12942, ¶2, n.4.

These facts are clear in public court documents cited below and need no proffer. They are also clear in myriad other facts in the proffer discussed above. Under this Court's law, they preclude laches. The §541 issue did not come out of the blue or as any sort of surprise to the Trustee. There is, for the reasons above, no question that the Trustee knew at every turn since 2009 that Appellants were asserting their §541 position and that estate property status would have to be determined. Neither the Decision, nor the Trustee, cite below to any caselaw addressed to the "lack of knowledge" element that both ignored — or any caselaw as to how there could be laches in the absence of proof of that element. Reversal is required for this reason alone.

D. *The Court Below Erred in Finding Undue Delay in These Circumstances.*

Based on the facts described at §B, Appellants did not act with undue delay. Quite the opposite: in their circumstances as individual retirees faced in 2008 with the loss of their pensions in the world's largest-ever bankruptcy, they organized as a group (over the Trustee's obstruction, *see* Dkt. 353 at 3, 4 & 8) to obtain counsel who prepared their Proofs of Claim asserting the §541 issue in 2009 addressed to issues in bankruptcy law which few laypersons would know exist. There was no delay.

But more than that, it also cannot be disputed that:

(i) Appellants asserted §541 protection in 2009;

(ii) that was sufficient to entitle Appellants to be receive their pension funds if the Trustee did not object, *see* 11 U.S.C. §502(a) ("[a] claim … is deemed allowed, unless a party in interest … objects");

(iii) the Trustee did not object in any way or even discuss or raise the issue until 2015;

(iv) even then, it only sought, on a procedural ground — an issue still being addressed in the Companion Appeal — to reclassify the claims as not "secured;"

(v) the Trustee, in briefing that motion, pointedly declined to address the substance of §541(b)(7)'s applicability;

(vi) appeal on that procedural issue took almost four years to decision in the District Court (something neither Appellants nor the Trustee could have anticipated or controlled);

(vii) even the District Court's decision stated that §541(b)(7) could give Appellants property outside the estate, rights "superior" to those of secured creditors in the bankruptcy (though not a secured claim);

(viii) Appellants (not the Trustee), prejudiced by the delay in the District Court in issuing the decision now in appeal in the Companion Appeal, sought in 2019 to break the logjam by reaching out to the Trustee to coordinate with it to file a proceeding below to move the issue toward determination; and

(ix) before then, there was not a single mention by the Trustee of laches or any form of waiver or anything of the kind.

These facts alone are sufficient to find that there was no undue delay on Appellants' part. But moreover, Appellants have actually pressed their §541 right at every point presented:

(i) as noted, Appellants' then-counsel filed Proofs of Claim invoking §541(b)(7) in 2009;

(ii) notably, §541(b)(7) had been enacted only some four years earlier and in 2009 was the subject of virtually no interpretation as to substance or procedures applicable to it;

(iii) as above, per 11 U.S.C. §502(a), the Proofs of Claim were in themselves sufficient for Appellants to obtain their rights if not challenged by the Trustee;

(iv) as also noted, the Trustee, for its part, did nothing on the subject until 2015;

(v) though Mr. Bennett had exited the picture by 2013, Appellants — hundreds of now-aging retirees —organized again, *ad hoc*, in response to the Trustee's 2013-raised subordination motion; and

(vi) Appellants objected in 2015 to the Trustee's non-substantive attack on their Proofs of Claim (as shown in the Companion Appeal) and appealed from the Bankruptcy Court in 2015.

Thus, in addition to general diligence beginning in 2009, Appellants took appropriate steps in litigation at each turn, *even though the Trustee did nothing until 2015 and the parties waited almost four years for a District Court appeal decision within that process until 2019.*

Laches requires not mere delay but "unreasonable lack of diligence under the circumstances" of a given case. *King v. Innovation Books, a Div. of Innovative*

Corp., 976 F.2d 824, 832 (2d Cir. 1992); *Lottie Joplin Thomas Tr. v. Crown Publishers, Inc.*, 592 F.2d 651, 655 & n.4 (2d Cir. 1978) (holding that "[i]n attempting to establish the defense of laches defendants failed to make the required showing that plaintiff (or her predecessors in interest) did not assert her or their rights diligently," and that a party's 16-year delay in challenging an assignment "was [not] unreasonable" where there was no reason to assume the costs of such litigation would have been worthwhile during much of that period); *Alston,* 2013 WL 3340484, at *4 (declining to find that a "multi-year delay" is "*per se* unreasonable and inexcusable," and requiring consideration of factual circumstances for any such determination of what was reasonable). The Trustee, on these facts and on this state of the record, cannot possibly show any "unreasonable lack of diligence under the circumstances" on Appellants' part.

More, if both parties are thought to have delayed — and in this scenario, based upon the Trustee's own delays and affirmative avoidance of the issue, that is the worst that could be said for Appellants on a laches analysis — courts will not allow one party to use the doctrine of laches as a sword against the other. *See In re Kelly*, 311 B.R. 341, 345 (Bankr. W.D.N.Y. 2004) ("Although the debtor may have neglected timely to move for the present relief, the respondents neglected to assert a secured status in their proofs of claim. Because all parties procrastinated in the assertion of rights, this court will not now apply laches"); *see also In re Dark*

Horse Tavern, 189 B.R. at 581-82 (declining to find laches and taking note of movant debtor's own delinquency in filing operating reports and holding: "In the matter *sub judice*, the Court cannot find that Debtor has acted in an equitable manner during the course of this bankruptcy case").

While acknowledging, as it had no choice but to do, that Appellants asserted §541(b)(7) protection from the virtual outset of this bankruptcy in 2009 [A-419-21], the Bankruptcy Court's finding of undue delay was premised on the fact that Appellants proceeded first through Mr. Bennett by their Proofs of Claim, rather than bringing a proceeding such as the one below sooner. The Bankruptcy Court simply ignores the actual procedural history of the issue and diligent steps taken by Appellants detailed above. But if it was not laches for the Trustee to wait until 2015, *i.e.*, *six years after claims had been filed invoking §541*, to even raise its procedural challenge, then it certainly was not laches for Appellants to raise their arguments in response to those objections, commencing in 2015, once the Trustee first objected.

Significantly, the Decision does not identify when laches arose. That is, in itself, a fatal flaw in the Decision. Certainly, it could not be said to have arisen before the Trustee was heard from at all in 2015. At that time, in the face of Trustee silence, Appellants would have needed to do nothing more to secure their §541 rights (which, per 11 U.S.C. §502(a), would have become absolute if the

Trustee had never raised objection). Similarly, having presented a well-stated motion opposing the Trustee's sole, procedural attack in 2015, laches could not be said to have arisen while Appellants awaited the result of their appeal to the District Court. And most certainly, there was no laches in Appellants' decision to move forward with the proceeding below while the appeal before Judge Gardephe remained *sub judice*, and, simply stated, they had grown more than 10 years older since the LBI bankruptcy with no pension payments.

More still, if Judge Gardephe had ruled in Appellants' favor, or if this Court does in the Companion Appeal, the very concept of laches becomes irrelevant because that still-to-be-made decision for Appellants would mean the issue was completely and fully in play in 2009 without even procedural objection available to the Trustee. In light of that question being open even today, it simply is not possible to find that there was laches at *any* prior time.

For all these reasons, the laches determination must be reversed because the Trustee did not establish its undue delay element.

E. *The Bankruptcy Court Erred in Finding Material Prejudice from Any Delay in this Case.*

The Trustee also cannot show "material prejudice" under laches jurisprudence — the third element of the required showing. Material prejudice is harm in the nature of changed position, lost evidence by the passage of time or

some similar, palpable harm in the way of changed or lost position. *See, e.g.*, *Hill v. W. Bruns & Co.*, 498 F.2d 565, 568 (2d Cir. 1974) ("Laches is a doctrine aimed at avoiding the commencement of stale claims in equity where it is impossible or difficult for a defendant to defend because evidence has been destroyed or lost and the defendant thereby prejudiced as a result of the delay in the institution of the action"); *Tri-Star Pictures, Inc. v. Unger*, 14 F. Supp. 2d 339, 361 (S.D.N.Y. 1998) ("Defendants laches argument also fails here because they have not satisfied their burden as to the second half of the laches inquiry which demands the showing of prejudice. In order to establish prejudice, Defendants must prove that they 'changed [their] position in a way that would not have occurred if the plaintiff had not delayed'"); *In re Francis*, 6:07-BK-73901, 2013 WL 773458, at *5 (W.D. Ark. Feb. 28, 2013), *aff'd,* 750 F.3d 754 (8th Cir. 2014) ("The bankruptcy court appears not to have discussed whether Summit and Southern State detrimentally changed their positions in reliance on GMAC's failure to correct its mortgage; instead it focused mostly on GMAC's lack of action by itself. 'Laches,' however, 'requires a demonstration of prejudice,' … which is another way of saying detrimental reliance").

All other bars to laches here aside, the Trustee has not shown and cannot make any showing that it changed its position to its detriment or was deprived of a

fair chance to present its §541 position by the passage of time because of anything Appellants did or did not do.

The Bankruptcy Court identified two ostensible elements of prejudice. First, it concluded, if Appellants had acted sooner to invoke §541(b)(7) in a proceeding like the one below, then the Trustee could have litigated this dispute "in tandem" with other issues rather than *seriatim*. [A-422 (discussed at §1 below)] Second, it contends that the Trustee cannot yet close out the estate bankruptcy because of this dispute. [A-422-23 (discussed at §2 below)]

Neither of these is cognizable as material prejudice under caselaw, such as cited above.[27]

But more, as discussed below, neither of these findings of purported prejudice withstands scrutiny as being true. First, as discussed above, there was nothing stopping the Trustee from litigating the merits sooner or "in tandem," and in any event, this record discloses no possible cost-efficiency from litigating these unique issues sooner with other unrelated issues. Second, the Trustee again establishes no actual delay or harm as to closing the bankruptcy estate because many other issues remain, and if the Trustee could close the estate but for this controversy, then it could likewise close the estate in the same way while this

[27] It is not cognizable above all because parties must be and are free generally to litigate as litigation unfolds in their interest so long as not acting in actual bad faith (never asserted here), need not be driven by a plan to achieve efficiencies for one's adversary, and certainly so when seeking $260+ million in earned pension funds.

controversy is being heard and determined. At the very least, the Trustee has not sustained its evidentiary burden of persuasion in showing prejudice on this pre-discovery motion.

1. *There is No Prejudice Because All Issues Were Not Litigated "in Tandem."*

First, the Trustee at all times had the ability to litigate "in tandem" but, for reasons of its own that it has not disclosed, it chose not to do so. As explained numerous times above, in 2015, in 2013 and at many other times, it chose, and in 2015 acknowledged openly, its deliberate choice of *refusing* to address the substance of §541(b)(7). It could have met the merits then or in tandem with any other litigation with Appellants on any other issue. It did not — because it *chose* not to. Laches law does not permit the Trustee, knowingly, to ignore the substance of a known issue while itself litigating other issues and then cry "laches" once the substantive issue is finally joined. *See, e.g., In re Kelly*, 311 B.R. at 345. Such gamesmanship is not allowed because it is itself inequitable. *See i.d.* ("As an equitable doctrine, laches must fulfill the principles of equity. Fundamental among these principles is the precept that one who seeks equity must do equity").

Second, no actual, much less material, prejudice is shown on this front in any way. The Trustee did not establish or even explain the purported efficiency it claims was lost and certainly did not document or particularize any costs. Of

course, it did not because it could not. All of its other issues with any of Appellants (such as arbitrability of subordination issues — itself an efficiency blocked by the Trustee, *see* Dkt. 9287) were disparate and discrete, wholly unrelated in their facts and governing law. The asserted lack of efficiency because there was no so-called "in tandem" litigation is a fiction.

As with so many other points, these were raised below, but not addressed in the Decision (or rebutted by the Trustee). Thus, even if this were a cognizable laches argument, it was not proven below

2. *There Is No Prejudice Concerning the Continued Pendency of the Bankruptcy.*

The Bankruptcy Court also found prejudice from the alleged fact the Trustee must keep the bankruptcy estate open due to this issue. [A-422-23] Again, that is not a cognizable basis for laches — if it were true that Appellants were the last to litigate, it would mean nothing. Some issue must inevitably come last, but the last does not lose merely because it is last.

But, above all, the assertion that this dispute is keeping the estate open is another fiction, wholly unsubstantiated on this record and contradicted by public records as to the LBI bankruptcy's status. Those records supply ample evidence that that is not the case because many other issues preclude closing the estate.

To begin with, the Trustee has often proposed, since at least April 2019, closing the estate and creating a "vehicle" to handle the many remaining estate matters. *See, e.g.*, Dkt. 14906, ¶34; Dkt. 15018, ¶22. If that is possible, the Trustee could do that now and include this controversy. The Trustee has never explained why it could not, despite Appellants pointing out this precise issue. [A-172-73]

But regardless of whether such a mystery-vehicle could have been created by April 2019 or now, the Trustee's semi-annual public reports disclose innumerable other matters that the Trustee would have had to include in that vehicle, then or now. Many are at least as complex as this case, many are no different in kind and many will outlast this controversy. Together, they show that "vehicle" or no, it is not *this* controversy keeping the estate open. As examples of matters that could fit in the vehicle if this one could and that will outlast this one (as of briefing in the Bankruptcy Court):

- the Trustee proposed its "vehicle" while litigating a $17 billion net operating loss calculation with New York State that it described as "complicated," such that its litigation would require extensive tax analysis "sufficiently complex so as to divert significant resources" from the estate, *see* Dkt.

15036, ¶¶3, 28; nonetheless, that dispute was among those eligible for the "vehicle;" and if that dispute was, this one would certainly be;[28]

- the Trustee is engaged in intensive litigation to recover a $230,000,000 judgment together with another Lehman affiliate, including litigation in Saudi Arabia; the Trustee has stated it might actually transfer *that* litigation to its proposed "vehicle" (again, if that litigation does not keep the estate open, this case certainly does not);
- the Trustee is still marshaling assets from Lehman counterparties, with a prospect of issuing new subpoenas for new efforts — again, there is no end in sight (and no difference from these matters);
- the Trustee is still identifying new defendants for new group antitrust litigation;
- the Trustee is pursuing a part of $4.275 billion recovery from antitrust and other financial industry misconduct; and
- the Trustee is pursuing ongoing securities litigation recoveries, including three possible new "class action" cases.

See Dkt. #15094, at 5-7.

With these numerous other open matters affecting the bankruptcy estate, some possibly to be open for a long time to come, it is simply false that this issue is

[28] Since the proposal, that dispute apparently settled.

the obstacle to closing the estate. The Trustee's assertion and Bankruptcy Court's holding to the contrary have never been examined, documented or even explained, and are, as above, contradicted by what is apparent on the face of the Bankruptcy Court docket. As such, this basis to find laches also fails, requiring reversal.

F. *A Finding of Laches Is Plainly Inequitable in this Case.*

As discussed above, in addition to being precluded by the Trustee's failure to make the requisite showing as to the more "formal" elements of the laches defense (knowledge, undue delay and material prejudice), "[t]he defense may be denied when there is evidence of other factors which would make it inequitable to recognize the defense." *Masterson*, 300 F.R.D. at 206. Such inequity is present here in spades.

It would be wholly inequitable to deny Appellants $260+ million in their earned and self-funded pensions based on laches against the background of this gargantuan and byzantine 12+-year bankruptcy for which the Trustee controlled the schedule. In the larger context of this bankruptcy and the real-world implications of what is at stake for Appellants, the Trustee's request that this Court apply the equitable doctrine of laches to prevent Appellants from having determination of §541(b)(7) protection for their pensions is, for numerous reasons, simply appalling on the most fundamental human level:

- As above, the Trustee, represented at all times by sophisticated expert bankruptcy counsel, offers no excuse for its six-year delay (until 2015) in even acknowledging or addressing the 2009 Proofs of Claim.
- It wishes to hold Appellants — a large group of elderly individual retirees — to a higher standard.
- The Trustee's assertion of prejudice from delay is more than ironic in light of the obvious fact that if anyone is being prejudiced by the long delay, it is Appellants, who already lost so much as a result of the LBI bankruptcy (having been deprived of their earned, owed pensions for 12+ years).
- The Trustee, as above, made conscious, strategic choices to litigate every issue to a final resolution, to opt for the longer path of litigation over contractual arbitration and to refuse, pointedly, to address the substance of the §541(b)(7), yet it now wishes this Court to impose a penalty for its choices on Appellants.
- Even while knowing all the while that the substance of the §541(b)(7) issue would need to be litigated before this dispute was concluded, the Trustee, at no point during the four-year-long wait for Judge Gardephe's decision (or before then), raised a prospective laches defense to Appellants. [A-131-32]
- If the Trustee were to prevail on its laches defense, the merits of this §541(b)(7) issue would, of course, not be reached, with the result that,

despite the merits favoring Appellants (*Argument* §I), what remains of their pensions would go as a windfall to the financial institutions that purchased more than 95% of the outstanding creditor claims. *See* Dkt. 14568, ¶20. Given these circumstances, finding laches is more than inequitable; it shocks the conscience. *See Masterson*, 300 F.R.D. at 206.

Conclusion

For the foregoing reasons, this Court should reverse the Decision in all respects.

Dated: New York, New York
December 18, 2020

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CERTIFICATE OF COMPLIANCE WITH
FEDERAL RULE OF APPELLATE PROCEDURE 32(a)

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B), as enlarged in this appeal in accordance with this Court's Order dated November 18, 2020, allowing the parties to file opening briefs of up to 25,000 words, because it contains 24,979 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f).

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(5) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word in Times New Roman 14-Point font.

Dated: New York, New York
December 18, 2020

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SPECIAL APPENDIX

TABLE OF CONTENTS

PAGE

FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	:	
LEHMAN BROTHERS INC.	:	Case No. 08-01420 (SCC) SIPA
THE LEHMAN BROTHERS INC. DEFERRED COMPENSATION DEFENSE STEERING COMMITTEE as Attorney in Fact for those Specified,	:	Adv. Pro. No. 19-01368 (SCC)
Plaintiffs,	:	
-- against --	:	
JAMES W. GIDDENS, as Trustee for the SIPA Liquidation of Lehman Brothers Inc.,	:	
Defendant.	:	

MEMORANDUM OPINION AND ORDER (I) GRANTING TRUSTEE'S MOTION TO DISMISS AND (II) DENYING ESEP COMMITTEE'S MOTION FOR SUMMARY JUDGMENT

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SHELLEY C. CHAPMAN
United States Bankruptcy Judge

Before the Court is the *Motion to Dismiss Adversary Proceeding*, dated November 6, 2019 ("Motion to Dismiss") (Doc. No. 5)[1] filed by the defendant, James W. Giddens, as Trustee for the liquidation of Lehman Brothers Inc. ("Trustee" or "Defendant") under the Securities Investor Protection Act of 1970 ("SIPA"), and the *Cross Motion for Summary Judgment and Opposition to Motion to Dismiss*, dated December 23, 2019 ("Motion for Summary Judgment") (Doc. No. 10) filed by the plaintiff, the Lehman Brothers Inc. Deferred Compensation Defense Steering Committee as Attorney-in-Fact for Those Specified ("ESEP Committee" or "Plaintiff").[2] A hearing was held on both motions on February 19, 2020, and the matter was taken under advisement.

Before diving into the legal issues presented by the Motion to Dismiss and the Motion for Summary Judgment, the Court believes it would be useful to describe in simple terms the history of the ESEP Committee's actions in the SIPA proceeding of Lehman Brothers Inc. ("LBI") over the last decade. With the goal of recovering approximately $270 million of deferred compensation directed to an unfunded "top hat" plan prepetition by the claimants who comprise the ESEP Committee (collectively, the "Claimants") and in an effort to recover such deferred compensation at a higher claim priority in the SIPA proceeding than that to which the Claimants would be legally entitled, the ESEP Committee has filed multiple motions in this Court, has

[1] Herein, "Doc. No." refers to documents filed in Adversary Proceeding No. 19-01368, and "Bankr. Doc. No." refers to documents filed in the Lehman Brothers Inc. SIPA liquidation proceeding, Case No. 08-01420.

[2] The Plaintiff has also filed its *Statement of Undisputed Facts*, dated December 23, 2019 ("Statement of Undisputed Facts") (Doc. No. 11) and the *Declaration of Richard J.J. Scarola in Opposition to the Trustee's Motion to Dismiss and in Support of Cross-Motion for Summary Judgment*, dated December 23, 2019 ("Scarola Decl.") (Doc. No. 10-2), in support of its Motion for Summary Judgment. The Defendant has also submitted the *Trustee's Reply in Support of His Motion to Dismiss and Opposition to Claimants' Cross-Motion for Summary Judgment*, dated January 21, 2020 ("Reply") (Doc. No. 17), and *Trustee's Response to Claimants' Local Bankruptcy Rule 7056-1 Statement of Facts as to Which There is No Dispute*, dated January 21, 2020 ("Response to Statement of Undisputed Facts") (Doc. No. 18).

failed to prevail on each motion, and has appealed each and every time it has not prevailed. Over the past six years, the ESEP Committee's litigation has garnered multiple decisions from this Court, from three District Court judges, and from two panels of judges on the United States Court of Appeals for the Second Circuit. Judges from all three courts have determined that the ESEP Agreements (as defined below) to which each of the Claimants is a party provide that the right to payment of the ESEP deferred compensation is subordinated to the claims of general unsecured creditors of the LBI estate.

Now, for the first time since the Claimants filed their claims against LBI over a decade ago, the ESEP Committee asserts a new and novel argument that is entirely at odds with every argument it has heretofore asserted: that section 541(b)(7) of the Bankruptcy Code excludes the ESEP deferred compensation from property of the LBI estate. The Complaint (as defined below) filed by the ESEP Committee in the instant Adversary Proceeding and its Motion for Summary Judgment are entirely without merit. It is time for this litigation odyssey to end. Simply put, enough is enough.

Even accepting as true all assertions set forth in the Complaint and drawing all reasonable inferences in the ESEP Committee's favor, the Court concludes that ESEP Committee has failed to state a claim upon which relief can be granted. For the reasons set forth herein, the Trustee's Motion to Dismiss is granted and the ESEP Committee's Motion for Summary Judgment is denied. The Court's decision follows.

BACKGROUND

The question before the Court is twofold. First, the Claimants seek a determination that ESEP funds that are part of the LBI estate are, in fact, not property of the estate, but property of the Claimants. As statutory support for their assertion in this regard, the Claimants cite to section 541(b)(7) of the Bankruptcy Code, which excludes from property of the estate funds that

are either "withheld by an employer from the wages of employees for payment as contribution" or "received by an employer from employees for payment as contributions" to "an employee benefit plan that is subject to title I" of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1001 et seq. ("ERISA"). Second, the Court must consider whether, even if Claimants' argument were to prevail, they are barred from bringing this proceeding due to the running of the applicable statute of limitations or by the equitable doctrine of laches.

In order to address the matters before the Court, it is necessary to review the lengthy history of the litigation between the Claimants and the Trustee.

I. The ESEP Agreements

The Claimants are certain former highly compensated executives and select employees who participated in a voluntary deferred compensation plan during the period of their employment by LBI and its predecessors, as applicable, prior to the commencement of LBI's SIPA proceeding on September 19, 2008. The deferred compensation plan, known as the Executive and Select Employee Plan (the "ESEP"), is governed by certain contracts (the "ESEP Agreements").[3]

The ESEP is what is known as a "top hat" plan, and as such, is exempt from many of the protections of ERISA.[4] The ESEP is an unfunded plan. The amounts directed by Claimants to the plan were, by agreement, not set aside in trust for the Claimants' sole benefit or kept separate from the assets of LBI. Instead, the ESEP Agreements specifically required that the amounts of

[3] A legible example can be found attached to the *Declaration of Richard J.J. Scarola in Support of Motion to Compel*, Ex. A, dated June 6, 2014 (Bankr. Doc. No. 9069), and it is from this document that the citations herein are taken. The ESEP Agreements are incorporated by reference into the Complaint (as defined below), and therefore may be considered when deciding the Motion to Dismiss. *See, e.g.*, *Int'l Audiotext Network, Inc. v. American Tel. & Tel. Co.*, 62 F.3d 69, 71–72 (2d Cir. 1995).

[4] *See* Appellant's Brief, ECF Doc. No. 11, p. 4, *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, No. 17 Civ. 06246 (AT) (S.D.N.Y.) (noting that the ESEP "did not have all of ERISA's protections . . . because it was what is known as a 'Top Hat' plan exempt from some of those protections").

compensation voluntarily deferred by Claimants be part of the capital of LBI and available to the creditors of LBI. The ESEP Agreements expressly state:

> The amounts credited to the deferred compensation account hereunder shall be dealt with in all respects as capital of [LBI], shall be subject to the risks of the business, and may be deposited in an account or accounts in [LBI]'s name in any bank or trust company.

(ESEP Agreements § 9(i).) Under the ESEP Agreements, the Claimants deferred compensation in exchange for a contractual right to receive future payments based on the deferred amounts. In so doing, Claimants were allowed to defer income tax that would otherwise be owed for the deferred amounts, and they received a guaranteed compound interest rate of approximately eleven percent, which accrued on a tax-deferred basis. (*Id*. § 2.)

This Court has previously found and determined that under the ESEP Agreements, Claimants' rights to payment are subordinate to the claims of general creditors of LBI. *See Giddens v. 344 Individuals (In re Lehman Bros. Inc.)*, 574 B.R. 52 (Bankr. S.D.N.Y. 2017), *aff'd*, No. 17 Civ. 6246 (AT), 2018 WL 10454936 (S.D.N.Y. Sept. 26, 2018), *aff'd sub nom.*, 792 F. App'x 16 (2d Cir. 2019). Section 9(d) of the ESEP Agreements provides that each of the Claimants:

> irrevocably agrees that the obligations of [LBI] hereunder with respect to the payment of the amounts credited to [Claimant's] deferred compensation account are and shall be subordinate in right of payment and subject to the prior payment or provision for payment in full of all claims of all other present and future creditors of [LBI] whose claims are not similarly subordinated . . . .

(*Id*. § 9(d).) Likewise, each of the Claimants agreed that in the event of a SIPA liquidation of LBI, the Claimant:

> shall not be entitled to participate or share, ratably or otherwise, in the distribution of the assets of [LBI] until all claims of all other present and future creditors of [LBI], whose claims are senior to

> claims arising under [the ESEP Agreements], have been fully satisfied or provision has been made therefor.

(*Id*.) Each Claimant also agreed that any payments made to him or her under the ESEP Agreements were "unsecured subordinated obligations of [LBI] only," and that he or she is "only a general subordinated creditor of [LBI] in that respect." (*Id*. § 5(d).)

II. The LBI SIPA Proceeding and the Claims

On September 19, 2008 (the "Filing Date"), the liquidation of LBI under SIPA was commenced, and the Trustee was appointed. On November 7, 2008, the Court entered an order establishing a claims bar date of June 1, 2009. (Bankr. Doc. No. 241.)

Each of the Claimants filed timely claims against LBI (the "Claims"). The large majority of the Claims asserted that they were secured based on, among other things, section 541(b)(7). (*See, e.g.*, Proof of Claim No. 7001872, Bankr. Doc. No. 14131, Ex. D.)

On November 15, 2012, the Court approved procedures for the Trustee to file omnibus objections to proofs of claim. (Bankr. Doc. No. 5441). Between July 19, 2013 and January 28, 2014, the Trustee filed omnibus objections to the Claims, seeking an order subordinating such claims to all general creditor claims of LBI (Bankr. Doc. Nos. 6847, 6865, 6866, 7264, 7388, 8153, collectively, the "Omnibus Objections.")

III. The Subordination Proceeding

Certain of the Claimants opposed the Omnibus Objections on procedural grounds, asserting that the relief sought required an adversary proceeding. On February 6, 2014, the Trustee filed a motion to convert the Omnibus Objections to a consolidated adversary proceeding. (Bankr. Doc. No. 8196.) Claimants opposed the motion, arguing that the Trustee was required to file a summons and complaint. (Bankr. Doc. Nos. 8280, 8282.) After a hearing held on February 27, 2014, this Court entered an order (Bankr. Doc. No. 8576) overruling

Claimants' objection and granting the motion to convert the Omnibus Objections to a single, consolidated adversary proceeding (the "Subordination Proceeding").

A. Motion to Compel Arbitration

On June 6, 2014, Claimants moved to compel arbitration of the Subordination Proceeding. (Bankr. Doc. No. 9068, the "Motion to Compel Arbitration.") On August 11, 2014, this Court entered an order denying the Motion to Compel Arbitration. (Bankr. Doc. No. 9617.) Claimants appealed.

On September 30, 2015, the District Court affirmed this Court's denial of the Motion to Compel Arbitration. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, No. 14 Civ. 7643 (ER), 2015 WL 5729645 (S.D.N.Y. Sept. 30, 2015). The Claimants further appealed, and, on October 6, 2016, the Second Circuit affirmed the decisions of the lower courts. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, 663 F. App'x 65 (2d Cir. 2016).

B. Motion to Withdraw the Reference

On November 6, 2014, while the appeal of the Motion to Compel Arbitration was pending, Claimants filed a motion to withdraw the reference. Motion to Withdraw the Reference, ECF Doc. No. 1, *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, No. 14 Civ. 8825 (ER) (S.D.N.Y.). The District Court denied the motion on December 1, 2016. (*Id.*, ECF Doc. No. 26.)

C. Cross-Motions for Summary Judgment

On January 13, 2017, the Trustee moved for summary judgment in the Subordination Proceeding. (Bankr. Doc. No. 14128.) Claimants opposed the Trustee's motion and cross-moved for summary judgment in their favor, seeking a determination that the Claims were not subordinated. (Bankr. Doc. Nos. 14192, 14196.) On July 13, 2017, this Court issued a decision, finding that the ESEP Agreements plainly and unambiguously provide that the Claims are

subordinate to claims of general creditors of LBI and therefore must be classified as subordinated claims. (*Giddens v. 344 Individuals (In re Lehman Bros. Inc.)*, 574 B.R. 52 (Bankr. S.D.N.Y. 2017) (the "Subordination Decision").

Claimants appealed from the Subordination Decision. The District Court affirmed on September 26, 2018, agreeing with this Court that the plain language of the ESEP Agreements requires the subordination of the Claimants' claims. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, No. 17 Civ. 6246 (AT), 2018 WL 10454936 (S.D.N.Y. Sept. 26, 2018).

Claimants further appealed to the Second Circuit. On November 1, 2019, the Second Circuit affirmed the judgment of the District Court, holding that it had properly affirmed the Subordination Decision's holding that the Claims are properly subordinated to the claims of LBI's general creditors. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, 792 F. App'x 16 (2d Cir. 2019).

IV. The Secured Classification Motion

On September 2, 2015, while the Subordination Proceeding was still in its early stages, the Trustee filed a separate objection to the Claims' assertion of secured status (Bankr. Doc. Nos. 12655, 12656, the "Secured Classification Motion.") The Claims were filed as secured claims, which required the Trustee to maintain a reserve for the Claims at 100 cents on the dollar, limiting the funds available for interim distributions to holders of allowed, undisputed claims while objections to the Claims remained pending. By the Secured Classification Motion, the Trustee sought a determination that the Claims were unsecured.

The ESEP Agreements expressly state that each Claimant's right to payment is "unsecured." (ESEP Agreement § 5(d).) By their response to the Secured Classification Motion (Bankr. Doc. No. 12832), Claimants argued that, notwithstanding this contractual agreement, the Claims were secured pursuant to section 541(b)(7), which excludes from property of the estate

funds that are either "withheld by an employer from the wages of employees for payment as contributions" or "received by an employer from employees for payment as contributions" to "an employee benefit plan that is subject to title I" of ERISA. 11 U.S.C. § 541(b)(7).

A hearing on the Secured Classification Motion was held on November 4, 2015. This Court granted the Trustee's objection to the Claimants' assertion of secured status, reclassified the Claims as general unsecured non-priority creditor claims, and preserved the Trustee's right to further object to the Claims. (Bankr. Doc. No. 13053, the "Reclassification Order.") In response to Claimants' argument that section 541(b)(7) gave their claims secured status, this Court noted that "[i]n order to have a secured claim, you have to have a security interest on property of the debtor's estate. . . . It therefore follows that it is impossible for the claims to be secured by having an interest in something that is not property of the estate. . . . [Claimants] have not asserted anything that comes close to establishing a *prima facie* case for these being secured claims." (Tr. of Nov. 4, 2015 Hr'g, 25:18-26:8, Bankr. Doc. No. 13064.)

Claimants appealed from the entry of the Reclassification Order. On September 30, 2019, the District Court affirmed this Court's ruling. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, No. 15 Civ. 09670 (PGG), 2019 U.S. Dist. LEXIS 170606 (S.D.N.Y. Sept. 29, 2019). The District Court specifically rejected Claimants' argument that their claims were entitled to secured status pursuant to section 541(b)(7). *Id.* at 11-12. The District Court stated that a finding that section 541(b)(7) applied would result in Claimants holding "an interest in the property at issue that is superior to a secured claim" and "a party cannot have a secured claim in property of the debtor if the property at issue is not the debtor's." *Id*. (internal citations omitted). Claimants appealed the District Court's decision to the Second Circuit. *344 Individuals v. Giddens (In re Lehman Bros. Inc.)*, Case No. 19-3245 (2d Cir.). No decision has yet been rendered.

V. The Adversary Proceeding

The ESEP Committee filed the complaint (the "Complaint") initiating this adversary proceeding on October 7, 2019. (Doc. No. 1.) The ESEP Committee seeks a declaratory judgment that 11 U.S.C. § 541(b)(7) removes "the deferred compensation [Claimants] were entitled to receive under the ESEP plan" from the LBI estate and asks this Court to award to Claimants "the amounts of the deferred compensation pension accruals in connection with the ESEP plan for each of the [Claimants] through the time of LBI's bankruptcy," together with interest, costs, and fees. (Complaint ¶¶ 11, 21)

On November 6, 2019, the Trustee filed the Motion to Dismiss, arguing that the Complaint should be dismissed as untimely under the applicable statute of limitations, barred under the equitable doctrine of laches, and dismissed on the merits for failure to state a claim. (Doc. No. 5.) The ESEP Committee filed the Motion for Summary Judgment on December 23, 2019, asserting that the claims stated in the Complaint were not subject to any statute of limitations and therefore were not barred; opposing the defense of laches and asserting that the Trustee's defense relies on facts outside the Complaint and therefore cannot be resolved on a motion to dismiss; and seeking summary judgment in its favor on the issue of section 541(b)(7)'s applicability to the Claimants' pre-petition contributions to the ESEP. (Doc. No. 10.) The ESEP Committee also filed its Statement of Undisputed Facts. (Doc. No. 11.) The Trustee filed its Reply on January 21, 2020, responding to the ESEP Committee's objection and opposing the Motion for Summary Judgment. (Doc. No. 17.) The Trustee also filed its Response to Statement of Undisputed Facts. (Doc. No. 18.)[5]

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[5] The parties agree on the following two statements:

"The Pension Parties are former Shearson Lehman Bros. Inc. ("Shearson") employees who participated in an Executive and Select Employees Deferred Compensation Plan. See ECF No. 14129, at ¶1."

On February 19, 2020, a hearing was held on the Trustee's Motion to Dismiss and the ESEP Committee's Motion for Summary Judgment, and the matter was taken under advisement. (Tr. of Feb. 19, 2020 Hr'g, Doc. No. 28.)

DISCUSSION

To survive a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), made applicable here through Federal Rule of Bankruptcy Procedure 7012, "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). A complaint may be dismissed under Rule 12(b)(6) because it is barred by an applicable statute of limitations, *Ghartey v. St. John's Queens Hosp.*, 869 F.2d 160, 162 (2d Cir. 1989) (holding that where "the dates in a complaint show that an action is barred by a statute of limitations, a defendant may raise the affirmative defense in a pre-answer motion to dismiss"), or on the basis of laches, *Zuckerman v. Metro. Museum of Art*, 928 F.3d 186, 193 (2d Cir. 2019) (holding that "laches may be decided as a matter of law when the [plaintiff's] lack of due diligence and prejudice to the [defendant] are apparent") (citation omitted).

I. The Complaint Fails on the Merits

A. Section 541(b)(7) Does Not Remove Contributions to the ESEP from the Estate

The ESEP Committee seeks a declaration that the deferred compensation the Claimants "contributed" to the ESEP prior to the commencement of the LBI SIPA proceeding is not property of LBI's estate by operation of section 541(b)(7) of the Bankruptcy Code. The Trustee responds that a careful reading of section 541(b)(7), the applicable provisions of ERISA, and relevant caselaw require the opposite conclusion. The Court agrees.

"In 1985, each of the Pension Parties entered into the Executive and Select Employees Deferred Compensation Agreements (the "ESEP Agreements") with Shearson, each in the form annexed as Exhibit 1 to the Declaration of Richard J.J. Scarola, dated December 23, 2019. See also ECF No. 14129, at ¶2."

The explicit language of the ESEP Agreements makes clear that the ESEP was a top hat plan. (*See* ESEP Agreements §9(i).). As discussed, *supra*, a top hat plan is "a plan which is unfunded and is maintained by an employer primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees." 29 U.S.C. §§ 1051(2), 1081(a)(3), 1101(a)(1). One of the benefits of an unfunded top hat plan is that, by deferring the payment of compensation, participants can also defer the payment of taxes on the deferred amounts (and on accrued interest) until retirement, when the participant is in a lower tax bracket. *See Accardi v. IT Litig. Tr.* (*In re IT Grp., Inc.*), 448 F.3d 661, 664 (3d Cir. 2006), *as amended* (July 10, 2006). The valuable benefit of deferring taxes on income can only be obtained, however, by assuming the risks associated with the plan's unfunded status.

Being exempt from the funding requirements of title I of ERISA, the assets of a top hat plan are part of "the general assets of the employer." *See Gallione v. Flaherty*, 70 F.3d 724, 725 (2d Cir. 1995). In order to achieve the purpose of tax deferral, the compensation deferred under top hat plans, as part of the employer's general assets, remains subject to the claims of the employer's general unsecured creditors in the event of the employer's insolvency. *In re IT Grp., Inc.*, 448 F.3d at 665; *see also Demery v. Extebank Deferred Comp. Plan (B)*, 216 F.3d 283, 287 (2d Cir. 2000) (a top hat plan is "unfunded" where the participants have no greater legal right to a specific set of funds than any unsecured creditor); *In re Silicon Graphics, Inc.*, 363 B.R. 690, 696-697 (Bankr. S.D.N.Y. 2007) (a top hat plan is "unfunded" where assets used to pay the deferred compensation are subject to the claims of the employer's creditors).[6]

[6] Beneficiaries of an unfunded top hat plan do not have legal rights "greater than that of an unsecured creditor to a specific set of funds from which the employer is, under the terms of the plan, obligated to pay the deferred compensation." *Demery*, 216 F.3d at 287. A top hat plan beneficiary "is not subject to tax on the compensation until he or she actually receives the deferred amount precisely because 'the employee may never receive the money if the company becomes insolvent.'" *In re IT Grp., Inc.*, 448 F.3d at 665; *see also Reliable Home Health Care, Inc. v. Union Cent. Ins. Co.*, 295 F.3d 505, 513–15 (5th Cir. 2002).

Top hat plans are subject to ERISA's administrative and enforcement provisions but are "exempted from ERISA's requirements relating to vesting, participation, fiduciary responsibilities and funding." *In re New Century Holdings, Inc.*, 387 B.R. 95, 110 (Bankr. D. Del. 2008); *Paneccasio v. Unisource Worldwide, Inc.*, 532 F.3d 101, 108 (2d Cir. 2008) (same). Stated differently, top hat plans are subject to the procedural safeguards of ERISA, but not to its substantive provisions. The reason for this departure has been explained in a Department of Labor advisory opinion as follows:

> [I]n providing relief for "top-hat" plans from the broad remedial provisions of ERISA, Congress recognized that certain individuals, by virtue of their position or compensation level, have the ability to affect or substantially influence, through negotiation or otherwise, the design and operation of their deferred compensation plan, taking into consideration any risks attendant thereto, and, therefore, would not need the substantive rights and protections of Title I.

Opinion No. 90-14 A (E.R.I.S.A.), 1990 WL 123933, at *1 (Dep't of Labor May 8, 1990).

Section 541(b)(7) of the Bankruptcy Code was enacted on April 20, 2005, as part of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), Pub. L. No. 109-8, § 323, 119 Stat. 23 (2005).[7] In support of their argument that section 541(b)(7) applies to exclude the ESEP amounts from the LBI estate, Claimants cite to the portion of section 541(b)(7) which excludes from property of the estate funds that are either (a) "withheld by an employer from the wages of employees for payment as contributions" to "an employee benefit plan that is subject to title I" of ERISA or (b) "received by an employer from employees for payment as contributions" to "an employee benefit plan that is subject to title I" of ERISA. 11 U.S.C. § 541(b)(7)(A)(i)(I), (B)(i)(I). Because, Claimants assert, the ESEP was a benefit plan subject to

[7] The Court has been provided with no legislative history or other information supporting the assertion that Congress intended section 541(b)(7) to affect top hat plans or render them inconsistent with the requirements of the Internal Revenue Code for an individual to defer income taxes.

portions of title I of ERISA, they claim that section 541(b)(7) excludes from property of LBI's estate the deferred compensation contributed to the ESEP.

Were the ESEP Committee's interpretation of section 541(b)(7) correct, it would create a conflict between the Bankruptcy Code, on the one hand, and federal tax and ERISA law, on the other hand. Stated differently, applying section 541(b)(7) to an unfunded top hat plan like the ESEP would, as the Trustee correctly points out, "nullify the ERISA and tax code provisions that make top hat plans possible." (Motion to Dismiss, p. 22.) As discussed *supra*, a central feature of a top hat plan such as the ESEP is its unfunded status, which, by being exempt from the substantive provisions of ERISA, is distinct from a "funded" plan, in which the plan's assets must be segregated from the general assets of the employer.[8] With an unfunded top hat plan, at the time of income deferral, the participant is not considered to have received any money or property; the Internal Revenue Code explicitly excludes from the definition of property for purposes of assessing taxable income "an unfunded and unsecured promise to pay money or property in the future." *See* 26 C.F.R. § 1.83-3(e); *Miller v. Heller*, 915 F. Supp. 651, 659 (S.D.N.Y. 1996). Accordingly, income deferred under an unfunded top hat plan, unlike funds paid into a plan covered by the substantive provisions of title I of ERISA, is not held in a "constructive trust" for the benefit of participants, because "there is no nexus or property identifiably belonging to the [p]lan [p]articipants on which a constructive trust can be placed. . . ." *In re Washington Mut., Inc.*, 450 B.R. 490, 504 (Bankr. D. Del. 2011).

[8] In contrast to an "unfunded" plan, a plan that is subject to both the procedural and substantive rights and protections of ERISA, is a "funded" plan, and "the plan assets must be "segregated from the general assets of the employer [such that the assets] are not available to general creditors if the employer becomes insolvent." *Northwestern Mut. Life Ins. Co. v. Resolution Tr. Corp.*, 848 F. Supp. 1515, 1517 (N.D. Ala. 1994); *see also Dependahl v. Falstaff Brewing Corp.*, 653 F.2d 1208, 1214 (8th Cir. 1981) ("Funding implies the existence of a res separate from the ordinary assets of the corporation.").

If section 541(b)(7) did in fact remove the contributions to unfunded top hat plans from the reach of creditors, it would effectively undo the tax-exempt status of such contributions, upsetting the function and tax structure of top hat plans. The purpose of unfunded top hat plans – income tax deferral – depends on the deferred compensation remaining subject to the claims of unsecured creditors. Nothing in the language of the statute or the legislative history of BAPCPA supports the conclusion that section 541(b)(7) was intended to treat top hat plans in bankruptcy in a manner inconsistent with the requirements of the Internal Revenue Code for deferred taxation, and the Court declines to do so here. As the Supreme Court has directed, "when two statutes are capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." *Morton v. Mancari*, 417 U.S. 535, 551 (1974); *see also SmithKline Beecham Consumer Healthcare, L.P. v. Watson Pharm., Inc.*, 211 F.3d 21, 27–28 (2d Cir. 2000) ("where two laws are in conflict, courts should adopt the interpretation that preserves the principal purposes of each").

Further, as explained by the Trustee in the Motion to Dismiss and in the Reply, numerous courts addressing the issue have held that section 541(b)(7) does not apply to unfunded top hat plans such as the ESEP. As one court explained:

> To exclude the assets of an unfunded plan from property of the estate and remove those assets from the reach of general unsecured creditors would therefore fly in the face of the very purpose, structure and function of a top hat plan. It would place 11 U.S.C. § 541(b)(7) at odds with ERISA and essentially nullify a top hat plan in the bankruptcy context. It would upend the policy of ERISA and the tax law that the deferred amounts in a top hat plan remain part of the general assets of the company subject to the claims of its general creditors.

In re The Colonial BancGroup, Inc., 436 B.R. 695, 712 (Bankr. M.D. Ala. 2010) ("*In re The Colonial BancGroup I*") (concluding that plan assets were not excluded from property of the estate pursuant to section 541(b)(7)). Certain of these courts have based their reasoning on the

fact that income deferred under a top hat plan is not "withheld" by an employer or "received" by an employee" within the meaning of section 541(b)(7). *See Korneff v. Downey Reg'l Med. Ctr. Hosp., Inc.* (*In re Downey Reg'l Med. Ctr. Hosp., Inc.*), 441 B.R. 120, 131 (B.A.P. 9th Cir. 2010) (affirming bankruptcy court's determination that deferred compensation in a top hat plan was not "withheld" from wages as required by section 541(b)(7) and, therefore whether the plan was "subject to" ERISA was of no import); *Synovus Tr. Co. v. Bill Heard Enter., Inc.* (*In re Bill Heard Enter., Inc.*), 419 B.R. 858, 867–68 (Bankr. N.D. Ala. 2009) (holding that a deferral is neither a withholding by an employer nor an amount received by an employer from employees, as the employee has no present entitlement to the income).

The sole case cited by the ESEP Committee in support of its interpretation of section 541(b)(7) , *see* Motion for Summary Judgment, pp. 28-29 (citing *In re Twin City Hospital*, No. 10-64360, 2011 WL 2946172 (Bankr. N.D. Ohio July 21, 2011), is distinguishable from the instant case. *Twin City* addresses the application of a different subsection of section 541(b)(7), which subsection specifically removes from the estate contributions to a "deferred compensation plan under section 457 of the Internal Revenue Code of 1986." 11 U.S.C. § 541(b)(7)(A)(i)(II), (B)(i)(II). Here, the ESEP Committee's argument under section 541(b)(7) relies on subsections (A)(i)(I) and (B)(i)(I), neither of which contains any reference to top hat plans. The ESEP Committee fails to cite any additional caselaw that persuasively establishes that section 541(b)(7)(A)(i)(I) and (B)(i)(I) exclude the ESEP amounts from property of the estate.

The express contractual language governing the ESEP, which language was agreed to by the Claimants, also confirms that compensation deferred under the ESEP is part of the capital of LBI and remains subject to the claims of its creditors in the event of insolvency. As described *supra*, the ESEP Agreements expressly provide that "[t]he amounts credited to the deferred compensation account hereunder shall be dealt with in all respects as capital of [LBI] [and] shall

be subject to the risks of the business." (ESEP Agreements § 9(i).) The ESEP Agreements also provide that each of the Claimants irrevocably agrees that the deferred compensation payments "are and shall be subordinate in right of payment and subject to the prior payment or provision for payment in full of all claims of all other present and future creditors of [LBI] whose claims are not similarly subordinated." (*Id.* § 9(d).). Each Claimant agreed that any future payments made to him or her under the ESEP Agreements were "unsecured subordinated obligations of [LBI] only," and that he or she is "only a general subordinated creditor of [LBI] in that respect." (*Id*. § 5(d).)

Finally, the Court observes that, even if Claimants were to prevail on their request for a declaratory judgment that the ESEP amounts are not property of the LBI estate, this declaration alone would not provide them with an ownership right in the ESEP amounts. Where applicable, section 541(b)(7) excludes property from the estate, but it does not create ownership rights. As the Trustee correctly asserts, "[e]ven if section 541(b)(7) applies to ESEP deferred compensation – which . . . it does not – Claimants would have to establish an independent right to those amounts." (Motion to Dismiss, p. 26 (citing *In re The Colonial BancGroup I*, 436 B.R. at 712 (concluding that even if "plan assets were excluded from property of the estate, it would not give the plan participants any greater claim to the funds than they now have")).) Claimants have failed to establish that section 541(b)(7) creates a legal entitlement to the ESEP amounts (or to interest, costs, and fees), and the Court declines to accept Claimants' unsupported assertion that a declaration that section 541(b)(7) applies would create rights to the ESEP amounts independent of the ESEP Agreements. Courts considering this issue have reached the same result. *See In re Downey*, 441 B.R. at 131 (where deferred compensation plan provides that the participants have no ownership interest in the funds, "removing the plan funds from the estate would not establish ownership in the participants"); *Rosen v. Chowaiki & Co. Fine Art Ltd. (In re Chowaiki & Co.*

Fine Art), 593 B.R. 699, 718 (Bankr. S.D.N.Y. 2018) ("a declaratory ruling under § 541(d), by itself, would not impart any equitable interest in the [disputed assets] to [Claimant]") (internal citations omitted); *In re Expert S. Tulsa, LLC*, 456 B.R. 84, 88 (Bankr. D. Kan. 2011) (determining that funds held in escrow were outside the bankruptcy estate and that plaintiffs had to pursue their rights under the relevant escrow agreement to seek return of the funds), *aff'd*, 522 B.R. 634 (B.A.P. 10th Cir. 2014), *aff'd*, 619 F. App'x 779 (10th Cir. 2015). As the Court has already determined that the Complaint must be dismissed on the merits, the Court need not determine whether Claimants are correct regarding ownership. The Court observes, however, that Claimants' litigation over the past six years has left them with, at most, a contractual claim under the ESEP Agreements that is subordinate to the claims of LBI's general creditors, which differs greatly from a right to payment of the ESEP funds to which they now assert an entitlement.[9]

Under the terms of the ESEP Agreements, deferred compensation directed to the ESEP by the Claimants is part of LBI's estate and remains subject to the claims of LBI's general creditors. For all of the foregoing reasons, Section 541(b)(7) does not apply to unfunded top hat plans such as the ESEP to exclude deferred compensation contributed to the ESEP from the LBI bankruptcy estate or remove such amounts from the reach of LBI's creditors. The Court concludes that the Complaint fails to state a claim upon which relief can be granted and, accordingly, should be dismissed on the merits.

[9] The Trustee states, persuasively, that "Claimants' own actions also undercut their claim to ESEP amounts," as Claimants have not asserted that they paid taxes on any ESEP amounts that they now claim to own, which weighs against their argument that the ESEP funds are their property. (Reply, p. 16 (citing *In re Cheeks*, 467 B.R. 136, 154 (Bankr. N.D. Ill. 2012) ("Even if it could be argued that Trust funds in this case were segregated from CFMC's general assets, Plaintiff still could not establish any proprietary interest in the Trust's funds because Plaintiff did not treat the funds as his property for tax purposes.").)

II. The Complaint is Barred by the Statute of Limitations

Section 1658(a) of title 28 of the United States Code provides for a four-year statute of limitations to cases arising under federal law when no other statute of limitations applies. The statute provides that "[e]xcept as otherwise provided by law, a civil action arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues." 28 U.S.C. § 1658(a). The statute was enacted in order to create a uniform statute of limitations applicable to federal causes of action and eliminate the previous piecemeal practice of adopting a local statute of limitation where no applicable federal statute of limitations existed. *Jones v. R.R. Donnelly & Sons Co.*, 541 U.S. 369, 377–84 (2004).

Section 1658(a) was enacted on December 1, 1990, and it applies to actions arising under federal laws enacted after that date. Where a federal law was first enacted prior to December 1, 1990, but amended after that date, the four-year statute of limitations applies to cases arising under the amended portions of the statute "if the plaintiff's claim against the defendant was made possible by [the] post-1990 enactment." *Jones*, 541 U.S. at 382.

The statute of limitations applicable to declaratory judgment actions is the limitation applicable to the underlying cause of action. *See 118 E. 60th Owners, Inc. v. Bonner Props., Inc.*, 677 F.2d 200, 202 (2d Cir. 1982) ("What determines the applicable limitations period is 'the basic nature of the suit in which the issues involved would have been litigated if the Declaratory Judgment Act had not been adopted.'") (quoting *Romer v. Leary*, 425 F.2d 186 (2d Cir. 1970)). Here, the Complaint seeks declaratory relief under 28 U.S.C. § 2201 based solely on 11 U.S.C. § 541(b)(7). (*See* Complaint, ¶¶ 21-22.) As discussed *supra*, Section 541(b)(7) was enacted on April 20, 2005, as part of BAPCPA.

Because section 541(b)(7) does not contain its own statute of limitations and because it was enacted in 2005, well after 1990, the Trustee argues that section 1658(a) applies to actions arising under section 541(b)(7). As to whether the statute of limitations set forth in section 1658(a) has lapsed with respect to the Adversary Proceeding, the Trustee submits that Claimants' cause of action under section 541(b)(7) accrued on the Filing Date, when the LBI bankruptcy estate was formed and Claimants had a complete and present cause of action. As the Complaint was not filed until more than eleven years after the Filing Date, well beyond the four-year statute of limitations established by section 1658(a), the Trustee asserts that the Adversary Proceeding is time-barred and should be dismissed.

The ESEP Committee opposes the application of the statute of limitations set forth in section 1658(a) by arguing that section 1658(a) only applies to a "civil action," not to an "adversary proceeding." (Motion for Summary Judgment, pp. 46-50.) Second, the ESEP Committee argues that other parts of the Bankruptcy Code do not have time limits, and, accordingly, no statute of limitations applies to a cause of action under section 541(b)(7).

The Court finds that Claimants have failed to demonstrate that an "adversary proceeding" filed in a bankruptcy court is not a "civil action," such that section 1658(a) would be inapplicable here. First, as Claimants concede in a footnote, Federal Rule of Bankruptcy Procedure 9002(1) explicitly states that a "'civil action' means an adversary proceeding." (Motion for Summary Judgment, p. 48, n. 15.) Further, bankruptcy courts have clarified that civil actions may be labeled "adversary proceedings" by a bankruptcy court. *See, e.g.*, *In re Yelverton*, No. 09-00414, 2014 WL 7212967, at *1 (Bankr. D.D.C. Dec. 17, 2014), as amended (Dec. 19, 2014) ("The 'adversary proceeding' label the civil action carries in the bankruptcy court is of no import, as it merely distinguishes the civil action from a 'contested matter' (the other category of civil proceedings tried in the bankruptcy court . . .)"), *aff'd sub nom. United States ex rel. Yelverton v.*

Fed. Ins. Co., 831 F.3d 585 (D.C. Cir. 2016). Finally, the cases cited by the ESEP Committee in support of its argument are inapposite and do not support its argument in this regard.[10]

The ESEP Committee also has failed to persuade the Court that, simply because certain other provisions of the Bankruptcy Code do not set time limitations, no statute of limitations applies to a cause of action invoking section 541(b)(7). In support of their assertion, Claimants have not cited to any case addressing section 541(b)(7). Instead, they cite to cases addressing sections of the Bankruptcy Code enacted prior to 1990 and not subsequently amended in any relevant respect, seemingly ignoring the fact that section 1658(a) applies to actions arising under federal laws enacted after December 1, 1990. Accordingly, because section 541(b)(7) does not contain its own statute of limitations and because it was enacted in 2005, after the 1990 enactment of 28 U.S.C. § 1658(a), the Court concludes that the four-year statute of limitations contained in section 1658(a) applies to causes of action seeking relief pursuant to section 541(b)(7) of the Bankruptcy Code.

A cause of action is deemed to accrue pursuant to section 1658(a) "when the plaintiff has a complete and present cause of action." *City of New York v FedEx Ground Package Sys., Inc.*, 351 F. Supp. 3d 456, 475 (S.D.N.Y. 2018) (citing *Wallace v. Kato*, 549 U.S. 384, 388 (2007)). Here, Claimants' cause of action accrued on September 19, 2008, the date LBI's SIPA proceeding commenced, at which time the LBI bankruptcy estate was formed and Claimants had a complete and present cause of action. Indeed, the Complaint seeks a determination that

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[10] *See, e.g.*, *Oppenheim v. Campbell*, 571 F.2d 660, 662-63 (D.C. Cir. 1978) (holding that while the federal statute of limitations under 28 U.S.C. § 2401(a) would apply to a complaint filed with a court, it did not apply to a claim filed with the Civil Service Commission, an administrative agency); *Official Employment-Related Issues Comm. Of Enron Corp. v. Arnold (In re Enron Corp.)*, 317 B.R. 701, 706 (Bankr. S.D. Tex. 2004) (concluding that 28 U.S.C. § 1391 and other nonbankruptcy venue statutes are applicable in bankruptcy cases only to the extent provided by bankruptcy venue statutes); *In re Salau*, No. CV 1:15-11080, 2016 WL 183704, at *2 (S.D.W. Va. Jan. 14, 2016) (distinguishing Federal Rule of Bankruptcy Procedure 7004, which governs service of process in actions filed in bankruptcy court, from Federal Rule of Civil Procedure 4, which governs actions filed in a district court); *In re Lindsey*, 177 B.R. 748, 749 (Bankr. N.D. Ga. 1995) (same).

accruals under the ESEP "through the time of LBI's bankruptcy filing" are not part of the LBI estate. (Complaint, ¶¶ 7, 21.). As the Complaint was not filed until more than eleven years after the Filing Date, well beyond the four-year statute of limitations established by section 1658(a), the relief sought by the Adversary Proceeding is time-barred.

Even if the Complaint was not subject to dismissal on the merits for failure to state a claim upon which relief can be granted, the Complaint is barred by the statute of limitations and must be dismissed.

III. The Complaint is Barred by Laches

Although the Complaint must be dismissed on the merits and because it is time barred, the extraordinary undisputed facts present here support dismissal of the Complaint as a matter of law based on the doctrine of laches.

The equitable doctrine of laches prohibits "unreasonable, inexcusable and prejudicial delay." *Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 491 B.R. 27, 32–35 (S.D.N.Y. 2013), *aff'd sub nom. Picard v. Fairfield Greenwich Ltd.*, 762 F.3d 199 (2d Cir. 2014). The doctrine of laches is particularly important in bankruptcy, where "the chief purpose" is to "secure a prompt and effectual administration and settlement of the estate." *Gazes v. DeArakie (In re DeArakie)*, 199 B.R. 821, 827 (Bankr. S.D.N.Y. 1996) (quoting *Crosby v. Mills*, 413 F.2d 1273, 1276 (10th Cir. 1969)); *see also In re Dini*, 566 B.R. 220 (Bankr. N.D. Ill. 2017) (holding that laches barred creditor's motion to dismiss chapter 7 bankruptcy case where creditor had inexcusably delayed for two years after learning of the basis for its motion).

There are two elements to a laches defense. "A party asserting a laches defense must show that the plaintiff has inexcusably slept on its rights so as to make a decree against the defendant unfair" and "that [defendant] has been prejudiced by the plaintiff's unreasonable delay in bringing the action." *Zuckerman v. Metro. Museum of Art*, 928 F.3d at193 (quoting *Merrill*

Lynch Inv. Managers v. Optibase, Ltd., 337 F.3d 127, 132 (2d Cir. 2003)); *see also Conopco, Inc. v. Campbell Soup Co.*, 95 F.3d 187, 192 (2d Cir. 1996) (holding that a defendant had been prejudiced when "the assertion of a claim available some time ago would be 'inequitable' in light of the delay in bringing the claim"). These two elements are integrally related and must be weighed together. "Where there is no excuse for delay . . . defendants need show little prejudice." *Stone v. Williams*, 873 F.2d 620, 625 (2d Cir. 1989), *vacated on other grounds*, 891 F.2d 401 (2d Cir. 1989). Under appropriate circumstances, laches may be decided as a matter of law and a court may dismiss a complaint at the pleading stage. *Zuckerman*, 928 F.3d at 193 (concluding that "laches may be decided as a matter of law when the [plaintiff's] lack of due diligence and prejudice to the [defendant] are apparent").

To begin, the Court takes judicial notice of Claimants' Claims and of their previous public filings during the many years of litigation which Claimants have pursued against the LBI estate with respect to such claims. *See Staehr v. Hartford Fin. Servs. Grp., Inc.*, 547 F.3d 406, 424–25 (2d Cir. 2008) (concluding that the district court did not abuse its discretion where it took judicial notice of certain assertions that had been made in other lawsuits). After reviewing the uncontroverted history of protracted litigation pursued by the Claimants in the LBI SIPA proceeding, the inexcusable delay of the Claimants in bringing this Adversary Proceeding and the prejudice to other creditors of the LBI estate are apparent here.

The Claims filed by Claimants in 2009 were premised upon Claimants' status as creditors of the estate; as discussed *supra*, the large majority of the Claims asserted that they were secured claims based upon section 541(b)(7). As a result, the Claimants and the Trustee have been litigating for six years about the priority of such Claims – whether, among other things, the Claims are (i) secured claims, (ii) unsubordinated general creditor claims, or (iii) subordinated general creditor claims – but never whether the Claims are in fact claims against property which

is not property of the LBI estate at all.[11] During the entirety of that litigation, notwithstanding their 2009 invocation of section 541(b)(7), Claimants have never argued to this Court that the ESEP amounts they were seeking are not part of the LBI estate or that Claimants are not creditors of the estate.

It is crystal clear that, since the time the Claims were filed, Claimants were aware of section 541(b)(7) of the Bankruptcy Code. As the Trustee points out, Claimants relied on section 541(b)(7) to argue that it gave them a secured claim to funds *within* the estate, a suggestion that both this Court and the District Court found meritless, and which issue the Claimants have now appealed to the Second Circuit by their appeal of this Court's November 10, 2015 Reclassification Order, as discussed *supra*. (*344 Individuals v. Giddens (In re LBI)*, Case No. 19-3245 (2d Cir.).) The issue before the District Court, and now the Second Circuit, is premised on Claimants' allegation that they have a claim to property that is included in the LBI estate. Claimants' multi-year delay in attempting to utilize section 541(b)(7) to now argue a directly contrary position – that the ESEP amounts were improperly included in the LBI estate – is inexcusable.

The Court recognizes that a litigant is permitted to plead in the alternative and to posit different theories of recovery. But that does not translate into an entitlement to engage in costly and protracted Dickensian litigation. Here, since the filing of the Claims over a decade ago, Claimants have steadfastly asserted that they are creditors of the estate and that they have a claim to approximately $270 million in estate property. Now, for the first time, and after losing in this Court, the District Court, and the Court of Appeals, Claimants seek, through the Adversary Proceeding, a declaratory judgment that the ESEP amounts – the estate property to which the

[11] Claims are only allowable if they are enforceable against "property of the debtor." See, e.g., 11 U.S.C. § 502(b)(1). Likewise, a secured claim is, by definition, "secured by a lien on property in which the estate has an interest." 11 U.S.C. § 506(a)(1).

Claims lay claim – are not property of the estate. There is no reasonable justification for their prolonged failure to make this argument since the time they filed the Claims in 2009.

In addition, as the Trustee highlights in the Motion to Dismiss, Claimants also did not raise their section 541(b)(7) argument (i) in connection with any of the allocation motions filed by LBI to allocate LBI estate assets to satisfy customer claims[12] or (ii) in response to the numerous distribution motions and orders that created claims reserves from the funds in the LBI estate and distributed funds then deemed part of the LBI estate to customers and creditors.[13] (Motion to Dismiss, p. 14.) Courts have held that the doctrine of laches bars attempts to assert ownership rights where, as here, a party has unreasonably delayed taking action to assert such rights in the face of bankruptcy court orders. *See, e.g., Barbieri v. Barbieri (In re Barbieri)*, 380 B.R. 284, 297 (Bankr. E.D.N.Y. 2007) (dismissing adversary proceedings seeking declaration that plaintiff was the true owner of certain property pursuant to laches and waiver where plaintiff had delayed taking action to assert ownership and did not raise ownership interest during asset sale proceedings). Claimants' untimely delay in asserting their argument that the ESEP amounts are not property of the estate cannot be countenanced. *See, e.g.*, *In re Huffman*, No. 06-50096, 2007 WL 4212292, at *3 (Bankr. D.S.D. Nov. 27, 2007) (stating that "[t]he time for [the claimant] to argue a portion of the [funds] was not property of the estate was much earlier in the case" and dismissing party's claim to ownership of assets held by estate).

Moreover, Claimants' inexcusable delay in asserting their section 541(b)(7) argument has significantly prejudiced the Trustee and creditors of the LBI estate. First, Claimants have been litigating against the Trustee for six years regarding the priority of the Claims, at significant

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[12] Bankr. Doc. Nos. 1866 (noting that the Trustee "expects that most of the LBI Estate will be allocated to Customer Property"), 2743, 4760, 6023.

[13] Bankr. Doc. Nos. 8885, 9273, 9246, 9520, 11147, 11358, 12478, 12579, 13642, 13683, 14162, 14210, 14568, 14595, 14596, 14605.

expense to the estate. The Trustee submits that, had Claimants raised their 541(b)(7) argument in a more timely manner during the six years of litigation regarding the ESEP amounts, "these issues could have been litigated in tandem, which would have been more efficient, and, of course, would have led to a much more timely final resolution of the issues." The Court agrees. *See Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC (In re Madoff Sec.)*, 491 B.R. at 34-35 (finding prejudice where delay in filing action caused defendants to engage in litigation for three years that might have been avoided if action had been timely-filed); *In re Dini*, 566 B.R. at 232 (finding prejudice where debtor was exposed to prolonged uncertainty about his legal rights and forced to incur significant litigation expenses which potentially could have been avoided if creditor had not delayed).

In addition to prejudice resulting from the additional, significant litigation expenses which could have been avoided had the Claimants not delayed at least six years in asserting this new cause of action, the Trustee has articulated a second form of prejudice here. The Adversary Proceeding and Claimants' pending Second Circuit appeal are the only remaining open matters in the LBI SIPA proceeding. (*See, e.g.*, Bankr. Doc. No. 14905 (April 30, 2019 letter from Trustee informing the Court that, upon final resolution of the pending ESEP claims matters, the Trustee will immediately seek Court approval for a final distribution and other closing procedures).) Stated differently, Claimants' delay in raising a new argument directly contrary to their prior position as creditors of the estate impedes the ability of the Trustee to move forward with closing the LBI estate. Keeping the estate open causes the Trustee to incur substantial operational costs that are separate and apart from litigation costs. (*See id.*). Such costs are detrimental to other creditors of the estate, as they reduce the total funds available for distribution and the amounts that creditors will ultimately receive. The delay in closing the LBI

estate also prejudices these creditors, as it forces them to wait additional time for final distributions in an otherwise fully-administered case that was commenced over eleven years ago.

For all of these reasons, the Court finds that Claimants' inexcusable delay has caused significant prejudice to the LBI estate, its creditors, and the Trustee, and holds that the doctrine of laches, as a matter of law, mandates dismissal of the Adversary Proceeding.

CONCLUSION

For all of the reasons stated herein, the Trustee's Motion to Dismiss is granted. The ESEP Committee's Motion for Summary Judgment is denied as moot. Any other arguments made by the ESEP Committee and not specifically addressed in this Memorandum Opinion and Order are hereby overruled.

IT IS SO ORDERED.

Dated: New York, New York
June 15, 2020

/s/ Shelley C. Chapman
SHELLEY C. CHAPMAN
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: LEHMAN BROTHERS INC.	Case No. 08-01420 (SCC) SIPA
THE LEHMAN BROTHERS INC. DEFERRED COMPENSATION DEFENSE STEERING COMMITTEE as Attorney in Fact for those Specified, Plaintiffs, - against - JAMES W. GIDDENS, as Trustee for the SIPA Liquidation of Lehman Brothers Inc., Defendant.	Adv. No. 19-01368 (SCC)

ORDER DENYING MOTION FOR RECUSAL

Upon the motion of Plaintiff The Lehman Brothers Inc. Deferred Compensation Defense Steering Committee as Attorney-in-Fact for Recusal in accordance with Federal Rule of Bankruptcy Procedure 5004(a) and 28 U.S.C. § 455(a) & (b)(1), dated January 14, 2020 (ECF No. 16) (the "Motion") and all filings related thereto (ECF Nos. 15 & 19); the memorandum of law of James W. Giddens, as trustee for the liquidation of the business of Lehman Brothers Inc., in opposition to the Motion, dated January 24, 2020 (ECF No. 22); and the parties' oral argument at the January 28, 2020 hearing before the Court (the "Hearing"); and after due deliberation, it is hereby

ORDERED that, upon the record and for the reasons set forth by the Court during the Hearing and in the decision of the Court read into the record at the Hearing, which are

incorporated herein by reference, and a transcript of which is annexed hereto as Exhibit 1, the Motion is DENIED in all respects.

Dated: New York, New York
February 7, 2020

/S/ Shelley C. Chapman
HONORABLE SHELLEY C. CHAPMAN
UNITED STATES BANKRUPTCY JUDGE

EXHIBIT 1

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

- x
In the Matter of:
LEHMAN BROTHERS INC., Case No. 08-01420-scc SIPA
Debtor.
- x
THE LEHMAN BROTHERS INC.
DEFERRED COMPENSATION DEFENSE
STEERING COMMITTEE As Attorney
In Fact for those Specified,

Plaintiffs,

VS. Adv. No. 19-01368-scc
JAMES W. GIDDENS, as Trustee
For the SIPA Liquidation of
Lehman Brothers Inc.
Defendant.
- x

United States Bankruptcy Court
One Bowling Green
New York, New York 10004-1408

January 28, 2020
10:06 AM

B E F O R E:

HON. SHELLEY C. CHAPMAN

U.S. BANKRUPTCY JUDGE

IN RE: Adversary proceeding: 19-01368-scc The Lehman Brothers Inc. Deferred Compensation Def v Giddens, Doc#16 Motion for Recusal filed by Scarola Zubatov Schaffzin PLLC on behalf of The Lehman Brothers Inc. Deferred Compensation Defense Steering Committee.

Transcribed by: Pamela A. Skaw

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BY: HEMANT SHARMA

P R O C E E D I N G S

THE COURT: Please have a seat.

Okay. Good morning. May I have appearances, please?

MR. SCAROLA: Your Honor, Richard Scarola with my colleague, Alex Zubatov, Scarola Zubatov Schaffzin for the Plaintiffs in the adversary case.

THE COURT: Okay. Good morning.

MR. SWERDLOFF: Good morning, Your Honor.

Nick Swerdloff from Hughes Hubbard & Reed. And with me is Greg Farrell, also from Hughes Hubbard & Reed. I'm counsel for the Trustee.

Also at the table is Hemant Sharma from SIPC.

THE COURT: Okay. All right.

Mr. Scarola, it's your motion.

MR. SCAROLA: Thank you, Your Honor. To the podium.

THE COURT: I have read the papers. I'm happy to give you time to say what you'd like but please don't repeat what's in the papers.

MR. SCAROLA: I don't intend to. It's a difficult kind of motion for an attorney to argue and I'm sorry to be here in some senses.

But briefly the statute under which we are moving has two parts. Section 455(b)(1), of course, is a bias,

predetermination, prejudice standard and our brief makes the case as to why we believe that applies.

I think from there --

THE COURT: Mr. Scarola, we might take a moment to look at the specific statements that you make regarding what occurred because I'd like to bring to your attention what I would suggest to you are mischaracterizations or perhaps misunderstandings of things that were said in the transcript because a number of the points that you made are categorically at odds with what occurred and are incorrect.

And it might be useful to you for me to point those out to you. Would you like me to do that?

MR. SCAROLA: Yes, Your Honor.

THE COURT: Okay. So, first of all, you point out at page four of your memorandum that there was a fully formed and firm determination and intention to rule against the pension parties. And there was no such thing.

Indeed, the statement that you cite to you neglect to include the fact that the statement that I made said, "subject to" hearing something from someone else, which is my way of expressing that -- an acknowledgement that there is always two sides to every story and that even when I might come out on the bench and have wholly prepared, I still come out with an open mind and, indeed, during many, many arguments over the past ten years, I've come out

inclined to rule one way and, then, I end up in another place.

So I express that by saying, "subject to" hearing something from someone else.

So I did not express a fully formed and firm determination to rule one way or another.

So, that's point number one.

Secondly, what you characterized as the Court's ex parte strategizing with counsel for the Trustee as to the steps to follow when the pension parties would ultimately lose this case and in connection with appeal rights -- how an appeal might -- might -- the pension parties might take -- might be directed to a district judge most amenable to the result the Court would like to see; that's a sheer fabrication.

The discussion that you allude to was simply a discussion of the timing of an appeal; whether that would be taken by your clients, yourself, or the Trustee, in the event that a ruling went the other way, and was a recitation or was an exploration of the amount of time that that would take against the backdrop of the need to close these cases and there was a statement that said, well, you may get another district judge.

That word "get" was not "obtain". That word "get" was you might be assigned to another district judge. That's

what you might "get"- as a result of the assignment process at the district court.

This Court has nothing whatsoever to do with appeals once they are taken from rulings. That goes off up the street and I have nothing to do with it. Indeed, on any given day, I can't even tell you who is presiding over the appeals that I have.

It is true when parties come in for status I ask the status, the timing and the like. But the suggestion that I said that I would steer an appeal to a district court judge inclined against you is an absolute falsity and it's very important for me that you understand that no such thing occurred. That is a very, very serious and incorrect allegation.

Finally, you state that I expressly and clearly stated a goal that the funds in this case would not go to the pension parties but, instead, to others deemed by this Court to have legitimate entitlements.

Again, I will say that that's either a misunderstanding or a mischaracterization.

The shared goal to which you allude was the Trustee's goal and this Court's goal of closing these cases which have been pending for almost 12 years. That's all.

And you also neglect to acknowledge the history that this Court has on these cases. I've spent weeks. I've

spent countless hours adjudicating the rights of individual claimants. Individuals who were indisputably and undoubtedly harmed by the Lehman bankruptcy.

Indeed, I have thank you letters from creditors who I've had to rule against because of application of the law, applicable law. But I've had thank you letters from creditors saying, thank you, that was the first time that anybody listened to me.

I conducted trials on restricted stock units; days and days of testimony, one after another, of employees who unfortunately had equity-like securities in the -- that were given to them as deferred compensation and I was unable to grant them allowed claims.

Now another judge might have just summarily dismissed those claims. I thought it was very important to hear from them and I've said out loud that it's never a good day when an individual claimant gets their claim expunged.

And I've also said on numerous occasions, in both the LBI case and the LBHI cases, that there is no such thing as Lehman. There seems to be this notion that the Court "sides" with Lehman but there is no Lehman.

All that there is are folks who have fiduciary duties to marshal the remaining assets and distribute them to creditors with allowed claims. That's all. And that's my job to call those balls and strikes.

So I thought it was important before you proceeded for me to correct those misunderstandings so that we put that to one side.

MR. SCAROLA: I understand that. I was about to say actually that with regard to the actual bias component, the 451 -- the 455(b)(1) component, there's nothing further I believe that I could say because essentially that inquiry is the Court's own inquiry into its own mind and I understand your expression --

THE COURT: But I'd like you to acknowledge what I just said to you.

And I just said some very significant things to you to clarify your understanding of what occurred.

MR. SCAROLA: I hear it. I understand it. And I appreciate it and I'm very glad to hear it.

There remains part of the motion because I assume that is implicitly the answer your Court's --

THE COURT: No. I'm not asking you any question. I'm asking you to acknowledge that you had a misunderstanding; that the statements that you made were not accurate representations of what occurred.

MR. SCAROLA: Your Honor, I understand --

THE COURT: Are you still maintaining that I said out loud that I would direct an appeal to a district court judge who was inclined against you? Is that your position,

sir?

MR. SCAROLA: I don't think we used those words. I think --

THE COURT: Yes, it is -- they are your words.

MR. SCAROLA: It -- well, I think what was said was that it was something discussed. It certainly isn't something that could be done and it certainly, in our view, reflects on the mindset which appears on a cold transcript which is what we are bringing to the Court, both under --

THE COURT: I just want to be perfectly clear.

MR. SCAROLA: -- 455(b)(1) and 455(a).

THE COURT: Is it your position that I discussed with counsel, these are your words, "how any appeal the pension parties might take might be directed to a district judge most amenable to the result the Court would like to see"? Is that -- is it your position that I said that?

MR. SCAROLA: It is our position that that's a reasonable reading of a reasonable objective person of the cold transcript. It is not at all to say Your Honor is being untruthful in your explanation of Your Honor's meaning and intent.

At the same time, I don't believe we've mischaracterized what we read on a cold transcript and I think it's our obligation to do as best we can as advocates to see what's on what page and describe it as best we

interpret it and that's what we did, which is not to say that's what is in the Court's mind, as I was saying.

It's not our -- it's not possible on a motion like this for me to go beyond saying this is how we see the cold record and it is for the Court to determine what is in the Court's mind, at least in the first instance, in terms of analysis under 455(b)(1).

And I do not think we erred in making the descriptions we made based on what's in the record. I couldn't say that that's the case.

I understand Your Honor's view of what was said on the record and, consistent with that view, our view is incorrect.

But, as an advocate, we're obligated to see what we see and describe it as it appears to us and I can tell you that I spent considerable time with a number of people considering whether the remarks on the record, on December 17th, were as we described them in terms of what we said and in terms of the overall presentation of what, to us, to our clients, appears to be a predetermination.

THE COURT: Just to be clear, it's your position that in the December 17th hearing, I strategized with the Trustee's counsel on how to steer an appeal to a district court judge who would rule against you; is that your position?

MR. SCAROLA: No. I think that would be too strong. I think there was --

THE COURT: But that's what you say in your papers.

So I'm just trying to understand --

MR. SCAROLA: As a paraphrase, Your Honor, I think that would be too strong.

What we see in that paragraph, and I don't at all want --

THE COURT: No. I'm asking you whether, in light of what we've just discussed, it is your position that I strategized with counsel such that in connection with the pension parties' prospective appeal rights, "how any appeal the pension parties might take might be directed to a district judge most amenable to the result the Court would like to see"?

I'm asking you, based on the reading of the record, where the only sentence that has anything to do with this, is the sentence says; "oh, you might get another district judge"; and the Trustee responded: "yes, that's possible and that would make four", which was a statement that clarifies that what was happening was there was simply making observations about the fact that, yes, it might get assigned as a related case, and that would depend on who checks what box, I suppose, or some other process at the

district court, which I have nothing to do with, or it might go to a judge who has never been -- heard an appeal before, and that was the fourth one.

So, in light of the entirety of that record, I'm asking you if you stand by your characterization, in your papers, that that's what occurred.

MR. SCAROLA: Your Honor, recognizing that the prior appeal took four years for a decision from the district court, Judge Gardephe, and, in that context, my reading and our reading and I think the reading of many, of that discussion was that it was an off the cuff, thinking out loud, discussion of in what manner can the inevitable appeal once a ruling in this adversary case would issue against plaintiffs, how that could be -- how that could find its way to a more expeditious track than that four-year track, the appeal before Judge Gardephe found.

That's not to say that it was -- nor do we say that it was --

THE COURT: That's a very, very, very, frankly, stunning and chilling view to take not only about the Court but also about the SIPA Trustee. That's a truly, truly serious allegation that, in essence, someone would attempt to fix the Court's --

MR. SCAROLA: But that's not the allegation nor is there --

THE COURT: But --

MR. SCAROLA: -- any allegation, Your Honor.

THE COURT: You --

MR. SCAROLA: There is no allegation. There is a description of what we see on a cold record --

THE COURT: And you've been now -- you've now been told -- it's now been pointed out to you what the overall context was and the one word from which you derived this entire constellation of assumptions, it's been explained to you why that was incorrect.

Context is everything, Mr. Scarola. You've been provided the context and, yet, you seem to still be suggesting that somehow this Court, together with the Trustee, would intervene or attempt to influence the course of an appeal. It's a very serious allegation and I could not be stronger in my -- frankly, in my desire to have you come to a different understanding because it's completely unfounded.

Why don't you move on to --

MR. SCAROLA: I do --

THE COURT: Why don't you move on to your argument?

MR. SCAROLA: But may I address that? I mean, I do understand the Court's explication of those remarks. As I said, I appreciate them. I'm glad to hear them.

I don't have any reason to dispute them. I thought the question you were posing was whether the characterization, in our brief, was in some sense inappropriate or unfair based upon the record presented and I respectfully have to say I do not believe, based on the record as handed to us --

THE COURT: Why don't you continue, Mr. Scarola?

MR. SCAROLA: I will.

Your Honor referred to context a moment ago and I'll turn to Section 455(a).

The standard there is different. It's the objective standard. Quoting it, it's that impartiality might reasonably be questioned and that standard is through the eyes of what's -- you've discussed it, I think -- the cases are on page 12 of our brief.

THE COURT: I've read your briefs.

MR. SCAROLA: The reasonable person, not a judicial officer, someone generally apprised of the situation.

In there, the analysis is generally done in terms of briefing together with the (b)(1) analysis but it's a very different analysis.

It is about appearances and, to some extent, it's about common sense. And I've heard everything Your Honor

said about your view of the remarks made in context. They are still the remarks that I have to deal with as counsel in representing clients.

It's not evidence but I spoke to many people, because I didn't bring this motion lightly, about what they thought was being said on the record --

THE COURT: I'm not -- it's not evidence and I'm not interested in who you spoke to.

MR. SCAROLA: But I say it for the sake of urging Your Honor to consider impartiality in context and in terms of appearance, or, the words are, would "reasonably be questioned".

THE COURT: I understand. I understand. I understand what the law is and this is not the first time that someone has made a motion asking me to recuse from a case.

MR. SCAROLA: If I may, I'll take a step out of this and -- to amplify my view of context and appearance.

I've read Your Honor's article about an appearance your own family member made in a different court.

And one of things Your Honor --

THE COURT: I don't quite know what to say about this, Mr. Scarola. I don't know what to say about this. You're making a record about an article that I published regarding my experience in the Bronx Criminal Court.

MR. SCAROLA: I'm not making a record, Your Honor. I'm talking about the --

THE COURT: What --

MR. SCAROLA: -- issue. The issue is appearance. In that instance, Your Honor recognized something, maybe truthfully and I don't think you could know or would say that you know, but as to appearance.

And the point that I'm making here is that while, again, I can't say what is in your mind, or was in your mind, or what you believe or would believe you believe, I can say that the amalgam of the remarks on the record, taken as a whole of the overall array of the comments made --

THE COURT: Let's talk about the overall array of the comments made.

The overall array of the comments made were in a regularly scheduled omnibus hearing as I have conducted in these cases for the past six years. Consistent with my obligations to oversee this liquidation, I asked Trustee's counsel for the status of pending matters.

For the first time in quite a long time, other than the administrative aspects of wrapping up the estate, there was news to report which was that there had been two decisions in the two prior actions that you have brought on behalf of 344 individuals making claims against the SIPA estate.

In that context, I was told what decisions had been rendered, both of those were affirming orders of this Court or orders of the district court and, indeed, one of them was rendered by Judge Gardephe after however many years it was, four plus years.

You, of course, understand that this Court has had no contact, connection, communication whatsoever with Judge Gardephe. That -- and when an appeal --

MR. SCAROLA: Of course. And I --

THE COURT: -- goes up to the district court, it goes to the district court. I have certainly nothing to say about that. Nothing --

MR. SCAROLA: Your Honor, I don't believe we've ever suggested anything otherwise and I --

THE COURT: I understand. So in the context of my -- every single time I have an omnibus hearing wanting to know when I can close the case, it was pointed out to me, as has been the case for quite some time, that the only contested matter, the only open matters before me -- at one point, there was nothing, because everything was up on appeal.

So there was nothing. And then you filed your adversary complaint and you're talking about an objective observer. Well, an objective observer who saw that there was another action that was filed, an objective observer

would understand that this Court had already issued two decisions dealing with the underlying predicate facts of your claims.

I understand you're making a different claim in the new adversary but the underlying predicate facts; so an objective observer would take that into account.

And then, and context is everything, and then I expressed my confusion as to trying to remind myself of what it is that was still left to do since I had already decided that the -- and have been affirmed by the Second Circuit, that the claims were subordinated and I had already decided that the claims did not enjoy secured status.

And, mind you, when you claim that a claim is -- when you make the allegation that a claim is secured, by definition you're taking the position that what secures it is property of the estate.

So, admittedly, I was confused and I said that subject to hearing something from someone else, which was an allusion to plaintiffs, I think this is frivolous. It's there. It's in the transcript. I said it.

The only other comment had to do with my continuing desire, which I will restate, that I'd like to see these cases closed.

Now if I were to rule in your favor, I would hazard a guess that the Trustee would appeal. If I rule in

the Trustee's favor, I would hazard a guess that you will appeal.

So I'm simply confronted with the circumstance that we now have another appeal that's going to have to be resolved. I have no influence over the timing. I did not offer a suggestion; did not offer a suggestion even, that it be designated as a related case.

I offered no suggestion. I merely made an observation that it will go up on appeal and you might "get" another judge, meaning you might be assigned a judge who has not yet had anything to do with this.

And remember you also sought to withdraw the reference to pursue arbitration. You also sought to compel the arbitration clause and you also sought to withdraw the reference.

MR. SCAROLA: Yes, we did.

THE COURT: So I frankly don't have a good grip on how many district court judges have already touched this but there have been a number.

In any event, those are the facts. That's what they are.

What that has to do with my personal experience going to criminal court and writing an article about it is a little unclear to me.

MR. SCAROLA: If I may explain that and then I

think I'll close because I understand much of what Your Honor has said.

It is an objective standard and I'll submit to you that someone reading the transcript and the array of comments that include this is frivolous litigation, it's costing the estate a lot of money, it's costing --

THE COURT: You're leaving out the part, the "subject to" part, Mr. Scarola.

MR. SCAROLA: And I'm getting to that, Your Honor.

THE COURT: You're leaving --

MR. SCAROLA: And if I --

THE COURT: You're leaving it out.

MR. SCAROLA: And if I could get the sentence out, I would get to that.

The "subject to" language, you've explained your view of it. I'll submit to you that the objective reader's view of that in the context of the flow and array of those comments is not that it's an invitation to argument. It's not that it's an indication of an open mind.

It's of -- the array of those comments is an indication that, this case, this adversary case lacks merit, shouldn't be there and should be dispensed with as expeditiously as possible against our clients.

I submit that is the objective, reasonable person, non-judicial officer's reading of what's in this transcript.

That's what we rest on.

THE COURT: Okay.

MR. SCAROLA: That's the 451(a).

THE COURT: Thank you.

MR. SCAROLA: And I appreciate your time. Thank you very much.

(Pause)

MR. SWERDLOFF: Good morning, Your Honor.

THE COURT: Hi.

MR. SWERDLOFF: I know you read the papers.

THE COURT: I did.

MR. SWERDLOFF: Our position is set forth in there. So, I'll be very brief and just say two things.

One, I read the transcript. I read it with the perspective of someone who has never been involved in this Lehman matter at all and I came away with the distinct view that there's nothing wrong in there; particularly on under the very high reasonable person standard.

Number two, we are totally confident that Your Honor, as you have in the past, will act impartially, fairly on the underlying case with regard to all parties, claimants included.

That's all I have unless you have questions for me.

THE COURT: Okay. Thank you.

MR. SWERDLOFF: Thank you.

THE COURT: Mr. Scarola, did you want to say anything more?

MR. SCAROLA: No, Your Honor. Thank you.

THE COURT: All right. Just to be clear, I mean, nobody seems to be disagreeing with me that whatever happens in the underlying adversary proceeding, the motion to dismiss or the -- whatever subsequent proceedings, that there may well be an appeal, right?

Nobody disagrees with that? Nobody's willing to stake out that position? Mr. Scarola?

MR. SCAROLA: I'm sorry. I'm not -- I was trying to make a note. Is the question --

THE COURT: I just -- there seems to be a general consensus that whatever happens, whichever side ultimately prevails, that there's likely to be an appeal, right?

MR. SCAROLA: I obviously can't speak for the Trustee --

THE COURT: Well, they've indicated with great certainty that if you -- if I were to rule in your favor on the underlying adversary proceeding that they would appeal.

And I'm simply asking you, based on what you've said, is that it's likely that you would appeal if there were an adverse determination.

MR. SCAROLA: I guess my --

THE COURT: Well, you'll have the option of appealing, right?

MR. SCAROLA: We have the option of appealing, Your Honor. We think the arguments are strong. We haven't seen a decision against us. So it would be strange for me to say, just as I said to the Trustee's counsel --

THE COURT: Sure. But --

MR. SCAROLA: -- some months ago, if you have a silver bullet of some sort --

THE COURT: Well, I don't want to -- I don't --

MR. SCAROLA: -- we don't want to go down this path. And I will concede I've read their opposition papers by now and -- as they came in, I think, a week ago today.

THE COURT: Uh-huh.

MR. SCAROLA: A week ago today. I don't believe they have that silver bullet in terms of an argument that the --

THE COURT: I'm asking for a very limited purpose, I'm sorry, and that's because, just making the observation that ultimately, one way or the other, and that it's true, whether I recuse or whether this would go to another judge, there's going to be an Article III set of eyes doing a de novo review of the law.

MR. SCAROLA: There may be, Your Honor, but I will point out if the drift of that is that it matters less what

Your Honor says, --

THE COURT: Well, I --

MR. SCAROLA: But I need to point this out, because it is very important to the issue that I think I'm hearing, which is that, on some of the issues Your Honor will be confronted with on their motion to dismiss, our cross motion for summary judgment, there is a deference standard, not a de novo review standard. So to the extent what Your Honor was saying is that, whether the first decision is yours or some other member of the Bankruptcy Court of the Southern District, it makes no difference. Well, it always makes a difference.

In any event, --

THE COURT: Your point --

MR. SCAROLA: -- but it makes especially a strong difference in that regard.

THE COURT: Mr. Scarola, you're putting words in my mouth.

MR. SCAROLA: I didn't mean to. I'm simply trying to be clear, in terms of what question I'm answering and what the possibilities would be.

THE COURT: Okay.

All right. Anyone else?

Okay, well, as I indicated before I went on the bench, I have spent a lot of time thinking about this, soul

searching, reading cases, reading the law, reviewing prior situations in which motions have been made for my recusal, and I'm prepared to read the decision, so that this case can move forward. So if you would indulge me, this will probably take about 20 minutes or a half an hour. It will comprise the ruling of the Court. I will then ask for an order to be submitted, which will incorporate the decision that I've read on the record into that order.

Before the Court is the motion of Lehman Brothers Inc. Deferred Compensation Defense Steering Committee, as Attorney in Fact for those Specified, the "ESEP Committee", for the recusal of this Court from presiding over any further proceedings involving their rights, including Adversary Proceeding 19-1368. The trustee for the SIPA liquidation of Lehman Brothers Inc., James W. Giddens, the "trustee", opposes the motion. See trustee's memorandum of law in opposition to plaintiffs' motions to recuse dated January 24th, 2020 at Docket No. 22. For the reasons that follow, this Court declines to recuse, and the motion is denied.

Background -- the December 17th hearing. On December 17th, at approximately 10:00 a.m., this Court held a regularly scheduled hearing in the Lehman Brothers Inc. SIPA liquidation proceedings. At that duly noticed omnibus hearing, several uncontested matters were before the Court.

Five months had passed since the last omnibus hearing in the SIPA proceeding, and the Court, in keeping with past practices, asked trustee's counsel for an update on the status of the case, which has now been pending for over 12 years. See transcript of December 17th hearing, at page 5, lines 2 to 10.

Counsel for the trustee updated the Court on the two rulings on appeal by the District Court and the Second Circuit Court of Appeals, respectively, that had been handed down since the last hearing had occurred before the Court in July. Both of such decisions addressed disputes that arose in the SIPA proceeding between, on the one hand, the trustee, and on the other hand, a group of claimants represented by the firm Scarola, Zubatov, Schaffin, PLLC, now acting as counsel to the ESEP Committee. These claimants are former Lehman executives, who had agreed to defer significant portions of their compensation for retirement benefits, under the Executive and Select Employees Plan (the "ESEP claimants"). Mr. Richard Scarola and his firm first appeared on behalf of certain ESEP claimants in the SIPA proceeding, on February 13th, 2014, quote, "For the limited purpose of opposing the efforts of the trustee to subordinate their claims, certain claims, to the claims of general unsecured creditors." See Docket No. 8234.

The ESEP claimants have filed proofs of claim in the SIPA proceeding, asserting secured claims against the debtor. The trustee had objected to these claims, on the basis that they were subject to subordination to general unsecured claims, pursuant to the subordination provision in the relevant agreements. While that litigation was proceeding, the trustee filed the second action, seeking to declare the claims unsecured. The trustee was required to reserve 100 cents on the dollar for any disputed secured claim, but could reserve less for a disputed unsecured claim. This Court granted the trustee's objection to the secured status of the ESEP claimants' claims, reclassifying them as unsecured by order dated November 10th, 2015. See Docket No. 13053.

This Court granted the trustee's objection seeking to subordinate the claims of the ESEP claimants to the claims of general unsecured creditors on July 13th, 2017. See Docket No. 14338. Both orders were appealed.

Turning to the most recent rulings on appeal, first, the District Court entered a decision on September 29th, 2019, affirming this Court's decision reclassifying the claims of the ESEP claimants from secured to unsecured. See Case No. 08-1420, Docket No. 15008.

Second, the Second Circuit Court of Appeals entered a summary order on November 1st, 2019, affirming the

judgment of the District Court, which had affirmed this Court's decision that the claims of the ESEP claimants were subordinated to the claims of general unsecured creditors, pursuant to enforceable subordination provisions in their agreements with the debtor. See summary order dated November 1st, 2019, Case No. -- Second Circuit Case No. 18-3188.

At the December 17th omnibus hearing, trustee's counsel informed the Court that the District Court decision on the reclassification had been further appealed to the Second Circuit, with the opening brief due January 8th, and that the trustee was trying to, quote, "advance the briefing as quickly as we can in the first half of 2020." The Court followed up by asking, quote, "Okay, so explain to me again, because it's been so many years, why the Second Circuit's ruling on subordination is not dispositive of the subsequent issue" on secured status? Transcript at page 6, lines 6 to 8.

Trustee's counsel reminded the Court of the complicated background of the case and explained that it is the trustee's position that the Second Circuit's decision on November 1st resolves the issue in the other appeal, and effectively moots the arguments on reclassification. Page 7 of the transcript, lines 18 to 24. He stated, quote, "How can claimants be reclassified from secured to unsecured when

three courts have already said they're subordinate" to unsecured?

The Court responded, quote, "But then that's at odds with the latest lawsuit. So you can't be Schrodinger's cat, right? You can't be secured, which, by definition, requires that your claim is secured by property of the estate -- you can't say that as point one and then, as point two, say that this stuff is not property of the estate." Transcript page 8, lines 11 to 22.

This Court was aware that, on October 7th, 2019, shortly after the District Court decision and shortly before the Second Circuit's ruling, the ESEP Committee, through Mr. Scarola's firm, had filed a complaint against the trustee, seeking a declaratory judgment that the deferred compensation withheld by the debtor from the ESEP claimants' wages was not, in fact, property of the estate. See Complaint, Adversary No. 19-1368, at Docket No. 1.

Trustee's counsel informed the Court that this was a basis for their motion to dismiss the complaint, which was scheduled for a hearing on January 28th, 2019, along with the cross motion for summary judgment by the ESEP Committee. The Court then noted, in order to, quote, "mark this out on the calendar," end quote, that, if there were an appeal from this Court's decision in that adversary, quote, "I don't know whether any appeal, at this point, from this Court,

would necessarily go to the same judge. You could actually get another judge in the District Court to look at this, right?" Transcript page 9, lines 16 to 21.

Trustee's counsel confirmed that, indeed, they could, quote, unquote, "get another district court judge, who would be "the fourth district court judge" in the case. Transcript page 9, page (sic) 22 to 23.

Court then offered the following comment, quote, "I mean, if this were any other situation -- and I'm not sure why it doesn't pertain in this situation, but I defer to you -- this would be a situation where it might be appropriate to talk about sanctions. This has now become, in my view -- subject to someone telling me something else -- this is frivolous litigation. And it's costing the estate a lot of money. And it's costing the legitimate creditors money." Transcript page 9, lines 25 to page 10, line 8.

Trustee's counsel replied that, quote, "In the first instance, that we would respectfully request, at the January 28th hearing, a ruling on the motion to dismiss." The Court pressed trustee's counsel. Quote, "Well, you know, as we're about to turn the page into 2020, it's no secret, I would like you to be able to close the case in 2020. There is no impediment to that, as far as I can tell," end quote. Transcript at page 10, lines 19 to 22.

Trustee's counsel explained that, subject to a final determination on the issues involving the ESEP claimants' claims, they were moving the case to a conclusion, with approximately six to nine months required at the end to distribute to creditors and close the case. Transcript page 10, lines 23 to page 11, line 14.

The Court stated, quote, "All right. Well, we share the same goal then. Okay, we can turn to today's agenda." At the conclusion of the hearing, the Court reiterated, quote, "I wish you happy holidays and a happy new year and a new decade. And hopefully, the year that Case No. 08-1420 will be closed."

The day after the hearing, December 17th hearing, trustee's counsel sent an email attaching the hearing transcript to Mr. Scarola. Trustee's Counsel noted that, quote, "The Court asked some questions about the status of the ESEP litigation." On January 14th, 2020, the ESEP Committee moved this court to recuse itself from presiding over any further proceedings with respect to ESEP claimants' rights, including in particular, this adversary proceeding. Motion at pages 1 to 2.

The motion to recuse. The ESEP Committee argues that certain of the Court's comments at the December 17th hearing require a recusal, as, in their view, it shows the

Court's impartiality as to the issues in this adversary case is reasonably in question and reflect, quote, "an actual bias and prejudice against" the ESEP creditors. I've already gone through, in detail, the statements that were made at page 4 of the committee's memorandum and clarified the ways in which this Court views that they inaccurately describe or mischaracterize or miscomprehend the meaning of certain words that were spoken during the December 17th hearing, and I'm not going to, here, repeat that prior discussion.

In short, the ESEP Committee argues that, because this Court has, their words, "predetermined the outcome of the adversary proceeding," recusal is required. Although the comments in question remain in the courtroom and thus, are not extrajudicial, the ESEP Committee argues that the comments were not made in Adversary Proceeding No. 19-1368 and were ex parte as to counsel to the ESEP Committee, who was not present. The ESEP Committee contends that the comments made, quote, "reveal such a high degree of favoritism or antagonism as to make fair judgment impossible." Memorandum of Law, at page 11.

The ESEP Committee suggests that the Court consider the, quote, "chilling effect" of the Court's comments on this point, and "the ways in which they would impair the function of the justice system in the face of"

their characterization, "an announced predetermination against" the ESEP Committee.

The Trustee's Objection. The Trustee disagrees with the ESEP Committee on both the law and the facts. The trustee asserts that the Court did not demonstrate bias by observing that the allegations in the complaint may be at odds with prior litigation positions, but rather, quote, "raised an obvious question based on the status of the litigation." See trustee's objection at page 2 and page 11.

The trustee denies that the Court announced how it would rule on the trustee's motion to dismiss. The Court merely raised questions about the arguments being asserted, given the lengthy litigation history between the parties. See objection, at pages 10 to 11.

The trustee urges that the Court did not, quote, unquote, "strategize," again, the committee's words, with the trustee's counsel about how to direct any appeal to a District Court judge, quote, "most amenable to the result the Court would like to see," but, rather, simply "discussed the amount of time any such appeal might take," -- see objection at pages 2 to 3 -- and merely noted that any appeal could go to a new judge. Objection, at page 12.

The trustee asserts that, in raising the question of whether adversary proceeding might be considered frivolous or whether it might be appropriate to talk about

sanctions, the Court specifically prefaced its comments, noting that this "view [was] subject to someone," i.e., the ESEP Committee, "telling [it] something else." Objection at page 3 and page 13, quoting the transcript.

Trustee urges that the Court was simply making clear that, while I had noted an issue, based on the litigation history, "it had not prejudged this case." Objection, at page 13.

The trustee further declares that the Court did not state its goal to ensure that the funds did not go to the ESEP claimants, but rather, that the Court stated its goal was, quote, "the closure of the case, as efficiently and promptly as practicable." Objection, at page 3.

The shared goal counsel to the trustee and the Court discussed at the hearing was to move the case to its closure. Objection, at page 14. The trustee also disagrees with the ESEP Committee's characterization of this as some nefarious ex parte discussion, noting that the Court's comments were made on the record in a public hearing in the ESEP proceeding, which was on notice to all interested parties, including the ESEP claimants. The trustee further notes that omnibus hearings have generally taken place on a quarterly basis, as the estate heads towards closure, and that such hearings, quote, "frequently commence with a status report from the trustee's counsel to the Court as to

the progress of outstanding matters in liquidation and related proceedings and appeals since the last hearing and outstanding measures needed to conclude the liquidation." Objection, at page 7. The trustee observes that these status reports, quote, "regularly include matters not directly related to the hearing agenda matters, but are in furtherance of advancing the liquidation and overall efficient case management."

At the December 17th omnibus hearing, the trustee's counsel naturally updated the Court on the status of the appeals involving the ESEP creditors and the status of this adversary proceeding, which are, indeed, the last remaining contested matters in this case. The trustee argues on the law that the ESEP Committee bears a substantial burden to show that the Court is not impartial, which they have failed to meet." Objection, at page 10, citing Flores vs. United States Department of Justice, 391 F. Supp. 3d 353, 365-66, Southern District of New York 2019.

The trustee asserts that no "reasonable person, knowing all the relevant facts and circumstances, would conclude that the Court should be recused." Objection, at page 15.

Finally, the trustee argues that the subjective test cited by the ESEP Committee is inconsistent with the law in the Second Circuit, which requires that courts apply

an objective test to determine whether recusal is required. Objection, at page 15, citing In re Drexel Burnham Lambert, 861 F.2d 1307 at 1312, Second Circuit, 1988.

Discussion -- Section 455 of Title 28 of the United States Code governs the disqualification of federal judges. The ESEP Committee has invoked the following provisions: (A) "Any justice, judge, or magistrate judge in the United States shall disqualify herself in any proceeding in which her impartiality might reasonably be questioned." (B) She shall also disqualify herself in the following circumstances: (1) where she has a personal bias or prejudice concerning a party. 28 U.S.C. Section 455(a) and (b)(1).

Unlike Section 455(b), which addresses the problem of actual bias by mandating recusal on certain specific circumstances where partiality is presumed, recusal under Section 455(a) is, quote, "not limited to cases of actual bias, but rather, the statute requires that a judge recuse herself whenever an objective, informed observer could reasonably question the judge's impartiality, regardless of whether she is actually partial or biased." United States vs. Bayless, 201 F.3d 116 at 126 Second Circuit, 2000, citing Liljeberg vs. Health Services Acquisition Corp., 485 U.S. 847 and 816, 1988.

The standard for recusal under 455(a) is objective reasonableness -- "whether an objective, disinterested

observer, fully informed of the underlying facts, would entertain significant doubt that justice would be done absent recusal." United States vs. Carlton, 534 F.3d 97 at 100, Second Circuit, 2008. See also United States vs. Bayless, 201 F.3d at 126; Diamondstone vs. Macaluso, 148 F.3d 113, 120 to 121, Second Circuit, 1998; United States vs. Lovaglia, 954 F.2d 811 at 815, Second Circuit, 1992.

Recusal under Section 455, quote, "is commonly limited to those circumstances in which the alleged partiality stems from an extrajudicial source." United States vs. Carlton, 534 F.3d 97 at 100, Second Circuit, 2008, quoting Liteky vs. United States, 510 U.S. 540 at 544, 1994. As such, quote, "Opinions held by judges as a result of what they learned in earlier proceedings in a particular case are not ordinarily a basis for recusal." Id., quoting Liteky, 520 U.S. at 551. Quote, "The same rationale applies to proceedings in a different case involving the same parties and the same set of facts." Id. The Supreme Court notes that, quote, "It has long been regarded as normal and proper for a judge to sit in the same case upon its remand, and to sit in successive trials involving the same defendant." Liteky, 510 U.S. at 552.

The Second Circuit has confirmed multiple times that a judge's knowledge and opinions, based on facts presented in related civil cases did not compel her recusal,

United States vs. Stitsky, 536 Federal Appendix 98 at 110, Second Circuit, 2013, citing United States vs. Carlton, 534 F.3d at 100. The standard is clear. When a judge's comments or opinions at issue are based on, quote, "facts introduced or events occurring in the course of the current proceedings, or of prior proceedings," they will only constitute a basis for a motion to recuse where they show, quote, 'a deep-seated favoritism or antagonism that would make fair judgment impossible." Liteky vs. United States, 510 U.S. at 555.

The Supreme Court has elaborated on the standard as follows: "Thus, judicial remarks during the course of a trial that are critical or disapproving of, or even hostile to, counsel, the parties, or their cases, ordinarily do not support a bias or partiality challenge. They may do so if they reveal an opinion that derives from an extrajudicial source; and they will do so if they were beyond such a high degree of favoritism or antagonism as to make fair judgment impossible." Id.

"An example of the latter (and perhaps of the former as well) is the statement that was alleged to have been made by the District Judge in Berger vs. United States, 255 U.S. 22, 41 Supreme Court 230, 1921, a World War I espionage case against German-American defendants," quote, "'One must have a very judicial mind, indeed, not [to be]

prejudiced against the German Americans' because their 'hearts are reeking with disloyalty.' Id., at 28 (internal quotation marks omitted). Not establishing bias or partiality, however, are expressions of impatience, dissatisfaction, annoyance, and even anger, that are within the bounds of what imperfect men and women, even after having been confirmed as federal judges, sometimes display. A judge's ordinary efforts at courtroom administration -- even a stern and short-tempered judge's ordinary efforts at courtroom administration -- remain immune." Liteky vs. United States, 510 U.S. at 555 to 56.

One Second Circuit decision deserves particular notice. In LoCascio vs. United States, 473 F.3d 493, Second Circuit, 2007, the Court of Appeals concluded that a district court judge's comment during a scheduling hearing that he may institute disbarment proceedings against counsel, when "read in context, cannot reasonably be construed as exhibiting personal animosity toward counsel or his client, neither of who was present, or displaying hostility toward the appellant's claim." As here, that comment came up in the context of a scheduling discussion. Id. at 497, Note 3.

The Second Circuit concluded that, "Since the comment revealed neither an opinion that derives from an extrajudicial source nor such a high degree of favoritism or

antagonism as to make fair judgment impossible, it did not warrant recusal." Id. at 497. No such high degree of favoritism or antagonism occurred here, and at a duly noticed omnibus hearing in the SIPA proceeding, which has been pending in this court since 2008 and before this presiding judge for the past 6 years, the trustee's counsel updated this Court on the status of the only remaining open matters that must be resolved before this proceeding can be concluded.

These matters involve the ESEP claimants and the various proceedings involving their alleged claims that have occupied this Court, various judges in the district court, and the court of appeals at various points over the past six years. This Court cannot forget and indeed, is not required to forget, what it knows. The Court knows of the long and complicated history of litigation involving the trustee and the ESEP claimants that appears to address the same or similar facts and circumstances as those alleged in the pending adversary proceeding.

This Court is charged with overseeing the administration of all cases on its docket. It is not secret that the Court wishes to see this case come to a conclusion, but, of course, not at the expense of the due process and substantive rights to which every litigant is entitled. The comments the Court made on December 17th do indeed reflect

this Court's knowledge of a history of this case and the lengthy previous litigation involving the ESEP claimants but do not reflect any deep-seated favoritism or antagonism that would require recusal.

Based on all the facts and circumstances of the case and for the reasons discussed above and during the course of the hearing, this Court concludes that nothing occurred in the December 17th omnibus hearing that demonstrates, again, "a deep-seated favoritism or antagonism that would make fair judgment impossible." Liteky vs. United States, 510 U.S. at 555. Accordingly, the Court will not recuse itself for matters involving the ESEP claimants' rights in this adversary proceeding. The motion is denied.

I would ask that, as I said at the top, that you prepare an order.

Please circulate it, Mr. Scarola. Who will take the pen preparing the order?

MR. SWERDLOFF: We will, Your Honor.

THE COURT: Trustee's counsel?

MR. SWERDLOFF: Yes.

THE COURT: Will you please circulate it to Mr. Scarola and then send it to chambers in the usual way?

MR. SWERDLOFF: Yes, Your Honor.

THE COURT: And we will enter it on the docket.

All right?

So shall we talk about scheduling a hearing on the motion to dismiss and the cross motion? Is the briefing on that fully submitted?

MR. FITZPATRICK: It is, Your Honor.

THE COURT: Mr. Scarola, is your briefing fully submitted?

MR. SCAROLA: Yes.

THE COURT: Okay. What dates would you like to come in? Well, I presume a fact not in evidence. Would you still like to have hearing on the motion, or would you like me to rule on the papers?

MR. FITZPATRICK: We would like a hearing, unless Your Honor wouldn't find it --

THE COURT: I'm just -- I'm asking for your preference.

MR. FITZPATRICK: Yes, we would request a hearing, yes.

THE COURT: Okay. We can have a hearing.

MR. FITZPATRICK: Okay.

THE COURT: And when would you like to come in?

MR. FITZPATRICK: Do you have any preference?

MR. SCAROLA: No.

THE COURT: Mr. Scarola?

MR. SCAROLA: I'm at your convenience.

THE COURT: Well, let's try to pick it today,

because we're all here.

MR. SCAROLA: Yes, yes.

THE COURT: And I have trials coming up and lots of other things. So --

MR. FITZPATRICK: Is Monday, the 3rd, a possibility, Your Honor?

THE COURT: It is for me.

Mr. Scarola?

MR. SCAROLA: Is it possible to do it the following week?

THE COURT: I will be out of the country the following week, and then that gets us into Presidents' week, which folks tend to have plans during Presidents' week.

So, Mr. Scarola, is there no -- the 3rd or the 4th and 5th doesn't work for you?

MR. SCAROLA: I have a substantial filing due on the 7th, and I'm concerned about that.

THE COURT: Okay.

MR. SCAROLA: As for Presidents' week. Does that work for you.

THE COURT: Well, Presidents' week folks have plans. If you'd like to come in then, I will be here, but folks have plans. It's also --

MR. FITZPATRICK: It's fine, Your Honor.

THE COURT: Okay. Which day on Presidents' week?

MR. FITZPATRICK: I guess I'd prefer as soon as possible. Is the 18th acceptable?

THE COURT: Well, let me just check.

MR. SCAROLA: Yes.

(Pause)

MR. FITZPATRICK: I've just got another hearing that I'm not sure is going to go on the 19th. Hoping it doesn't, but --

THE COURT: Okay. Could we do 11 o'clock on the 19th? Wednesday, the 19th?

MR. SCAROLA: Sure, yes.

MR. FITZPATRICK: Your Honor, I have another hearing that I think is going to be canceled. So can I just say yes, but it's not guaranteed to be canceled yet.

THE COURT: Yeah, I'd like to have certainty.

(Pause)

THE COURT: Yeah, how about 2 o'clock on the 19th?

MR. FITZPATRICK: On the 19th? Yes.

THE COURT: Is that better?

MR. FITZPATRICK: Yes, Your Honor, yes.

THE COURT: On the 19th.

Mr. Scarola, can you do 2 o'clock on the 19th?

MR. SCAROLA: Yes.

THE COURT: Okay, so 2 o'clock on the 19th for hearings on the cross motions.

Okay, thank you very much.

MR. FITZPATRICK: Thank you, Your Honor.

THE COURT: Have a good day.

MR. SCAROLA: Thank you, Your Honor.

(Whereupon, these proceedings were concluded at 11:04 AM)

I N D E X

R U L I N G

* * * * *

C E R T I F I C A T I O N

We, Pamela A. Skaw and Nicole Yawn, certify that the foregoing transcript is a true and accurate record of the proceedings.

_____

Pamela A. Skaw

_____

Nicole Yawn

Date: January 29, 2020

Veritext Legal Solutions
330 Old Country Road
Suite 300
Mineola, NY 11501

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UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

- x

In the Matter of:

LEHMAN BROTHERS INC., Case No. 08-01420-scc SIPA

Debtor.

- x

THE LEHMAN BROTHERS INC.
DEFERRED COMPENSATION DEFENSE
STEERING COMMITTEE as Attorney
in Fact for Those Specified,

Plaintiffs,

VS. Adv. No. 19-01368-scc

JAMES W. GIDDENS, as Trustee
For the SIPA Liquidation of
Lehman Brothers Inc.

Defendant.

- x

United States Bankruptcy Court

One Bowling Green

New York, NY 10004

11 U.S.C. § 541:

(a) The commencement of a case under section 301 , 302 , or 303 of this title 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.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is--

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b) , 363(n) , 543 , 550 , 553 , or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date--

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include--

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 et seq. ; 42 U.S.C. 2751 et seq.), or any accreditation status or State licensure of the debtor as an educational institution;

(4) any interest of the debtor in liquid or gaseous hydrocarbons to the extent that--

(A)(i) the debtor has transferred or has agreed to transfer such interest pursuant to a farmout agreement or any written agreement directly related to a farmout agreement; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 544(a)(3) of this title; or

(B)(i) the debtor has transferred such interest pursuant to a written conveyance of a production payment to an entity that does not participate in the operation of the property from which such production payment is transferred; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 542 of this title;

(5) funds placed in an education individual retirement account (as defined in section 530(b)(1) of the Internal Revenue Code of 1986) not later than 365 days before the date of the filing of the petition in a case under this title, but--

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds--

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(e) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $6,425;

(6) funds used to purchase a tuition credit or certificate or contributed to an account in accordance with section 529(b)(1)(A) of the Internal Revenue Code of 1986 under a qualified State tuition program (as defined in section 529(b)(1) of such Code) not later than 365 days before the date of the filing of the petition in a case under this title, but--

(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were paid or contributed;

(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(6) of such Code with respect to such beneficiary, as adjusted beginning on the date of the filing of the petition in a case under this title by the annual increase or decrease (rounded to the nearest tenth of 1 percent) in the education expenditure category of the Consumer Price Index prepared by the Department of Labor; and

(C) in the case of funds paid or contributed to such program having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $6,425;

(7) any amount--

(A) withheld by an employer from the wages of employees for payment as contributions--

(i) to--

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;

except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2) ; or

(ii) to a health insurance plan regulated by State law whether or not subject to such title; or

(B) received by an employer from employees for payment as contributions--

(i) to--

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986;

except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2) ; or

(ii) to a health insurance plan regulated by State law whether or not subject to such title;

(8) subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property (other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where--

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b);

(9) any interest in cash or cash equivalents that constitute proceeds of a sale by the debtor of a money order that is made--

(A) on or after the date that is 14 days prior to the date on which the petition is filed; and

(B) under an agreement with a money order issuer that prohibits the commingling of such proceeds with property of the debtor (notwithstanding that, contrary to the agreement, the proceeds may have been commingled with property of the debtor),

unless the money order issuer had not taken action, prior to the filing of the petition, to require compliance with the prohibition; or

(10) funds placed in an account of a qualified ABLE program (as defined in section 529A(b) of the Internal Revenue Code of 1986) not later than 365 days before the date of the filing of the petition in a case under this title, but--

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds--

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(h) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $6,225.

Paragraph (4) shall not be construed to exclude from the estate any consideration the debtor retains, receives, or is entitled to receive for transferring an interest in liquid or gaseous hydrocarbons pursuant to a farmout agreement.

(c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law--

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) 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 this title.

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise

the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

(e) In determining whether any of the relationships specified in paragraph (5)(A) or (6)(A) of subsection (b) exists, a legally adopted child of an individual (and a child who is a member of an individual's household, if placed with such individual by an authorized placement agency for legal adoption by such individual), or a foster child of an individual (if such child has as the child's principal place of abode the home of the debtor and is a member of the debtor's household) shall be treated as a child of such individual by blood.

(f) Notwithstanding any other provision of this title, property that is held by a debtor that is a corporation described in section 501(c)(3) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code may be transferred to an entity that is not such a corporation, but only under the same conditions as would apply if the debtor had not filed a case under this title.

28 U.S.C. § 1658:

(a) Except as otherwise provided by law, a civil action arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues.

(b) Notwithstanding subsection (a), a private right of action that involves a claim of fraud, deceit, manipulation, or contrivance in contravention of a regulatory requirement concerning the securities laws, as defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)), may be brought not later than the earlier of--

(1) 2 years after the discovery of the facts constituting the violation; or

(2) 5 years after such violation.