No. 98-130

In the Supreme Court of the United States

OCTOBER TERM, 1997

UNITED STATES OF AMERICA,
PETITIONER

v.

CONTINENTAL AIRLINES
THOMAS E. ROSS, TRUSTEE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Whether, notwithstanding 11 U.S.C. 553(a)'s provision that "this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title," the confirmation of a bankruptcy reorganization plan under 11 U.S.C. 1141 causes a creditor to lose its setoff rights against the debtor.

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The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-14a) is reported at 134 F.3d 536. The opinion of the district court (App., *infra*, 18a-30a) is reported at 218 B.R. 324. The report and recommendations of the magistrate judge (App., *infra*, 31a-51a) and the decision of the bankruptcy court are unreported (App., *infra*, 52a-56a).

JURISDICTION

The judgment of the court of appeals was entered on January 20, 1998, and was amended on March 23, 1998. A petition for rehearing was denied on March 23, 1998. On June 12, 1998, Justice Souter extended the time for filing a petition for a writ of certiorari to and including July 21, 1998. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

Sections 553 and 1141 of the Bankruptcy Code, 11 U.S.C. 553, 1141, are reproduced at App., *infra*, 65a-68a.

STATEMENT

1. In December 1990, Continental Airlines filed a petition for reorganization under Chapter 11 of the Bankruptcy Code. Several federal agencies filed claims that totaled more than $14 million.[1] The debtor challenged many of those government claims as to their amounts and validity. To date, most of those challenges have not yet been resolved.

The claims filed by the various federal agencies followed different forms. The proof of claim filed on November 27, 1991, by the Federal Aviation Admini-

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[1] The claims were filed by the Immigration and Naturalization Service ($5,859,955.06), the United States Customs Service ($5,420,830), the Federal Aviation Administration ($3,405,700), the United States Postal Service ($42,275), the Department of Agriculture ($94,266.71), the United States Air Force ($155,572.89), the Department of Labor ($42,000), the Equal Employment Opportunity Commission ($3,500), the Drug Enforcement Administration ($837.50), and the Peace Corps ($934.90). See C.A. App. 58 (Attachment (Facts) to Bankruptcy Court Order dated Sept. 30, 1993); C.A. App. 50 (Proofs of Claim Filed on Behalf of the United States).

stration (FAA) stated: "The United States reserves its right to effect any and all appropriate setoffs." C.A. App. 40 (FAA Proof of Claim, Rider A). Neither the trustee nor any other party objected to or opposed the claim filed by the FAA, or challenged the expressed reservation of the setoff rights of the United States. Other claims did not expressly preserve the government's setoff rights. See App., *infra*, 32a-35a.

On April 16, 1993, the bankruptcy court confirmed respondent's reorganization plan. Under the plan, as unsecured creditors, the federal agencies were to receive payment equivalent to approximately 4.8 percent of their allowed claims. The Plan of Reorganization further provided that the Debtor and the new entity, "New Cal," could, but were not required to, exercise their own setoff rights available under applicable law. See C.A. Supp. App. B-50 (Debtor's Second Revised Amended Joint Plan of Reorganization ¶ 14.8). The plan did not provide for or mention the setoff rights of creditors.

2. In September 1990, before it filed for bankruptcy, Continental Airlines, together with several other airlines, filed an action in the U.S. District Court for the District of Columbia seeking to force the General Services Administration (GSA) to pay for air travel. GSA had withheld funds because of perceived overcharges by the airlines on past air travel. On August 11, 1992, the district court granted summary judgment in favor of the airlines.[2] The district court ordered GSA to return "all monies held

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[2] The court held that, although GSA has the right to audit ticket payments and to withhold funds based upon past overcharges, it could not conduct audits on the premise that the government was entitled to the lowest fare available.

improperly." *Alaska Airlines, Inc.* v. *Austin*, 801 F. Supp. 760 (D.D.C. 1992), aff'd in part, rev'd in part, 8 F.3d 791 (Fed. Cir. 1993).

When the district court refused to stay its order requiring GSA to pay the airlines, the United States sought a stay from the Federal Circuit. The court of appeals initially denied a stay. The United States filed a motion for partial reconsideration, pointing out that if it turned over the funds to the airlines in bankruptcy, it could lose the right to set off the funds against debts owed by the airlines to the United States. The United States asked for permission to pay the funds into the registries of the respective bankruptcy courts so that the funds could be held in escrow while the government asserted its setoff rights in bankruptcy court. In response to the United States' motion expressly seeking to preserve its setoff rights, the Federal Circuit issued an order on February 25, 1993, staying the district court's order to pay the airlines in bankruptcy. *Alaska Airlines* v. *Jones*, Nos. 93-1028, 93-1117, 93-1125 & 93-1161 (Fed. Cir. Feb. 25, 1993) (Order per Rich, J.). Then, on April 12, 1993, to afford the United States an opportunity to assert its setoff rights before turning the funds over to the airlines in bankruptcy, the Federal Circuit modified the district court's order and directed the United States to deposit the funds in the registries of the bankruptcy courts for the airlines then in bankruptcy proceedings. C.A. App. 26-27 (Federal Circuit Order dated April 12, 1993). Accordingly, on May 19, 1993, more than one month after the confirmation of the respondent's reorganization plan, the United States deposited $4,763,219.60 with the registry of the Bankruptcy Court for the District of Delaware. App., *infra*, 16a, 58a.

3. On May 28, 1993, the United States filed a motion in the bankruptcy court seeking permission, pursuant to 11 U.S.C. 553, to set off the deposited funds against Continental's prepetition debts to the United States. On September 30, 1993, the bankruptcy court denied the motion. The bankruptcy court held, *inter alia*, that the United States lost its setoff rights when the reorganization plan was confirmed. Relying upon *United States* v. *Norton*, 717 F.2d 767 (3d Cir. 1983), the bankruptcy court held that, under 11 U.S.C. 1141, upon confirmation of the plan all property of the estate vested in the newly-reorganized entity free and clear of any claims or interests. App., *infra*, 54a.

4. The government appealed the bankruptcy court's ruling to the district court. The district court referred the matter to a magistrate judge, who filed a report and recommendations agreeing with the bankruptcy court. App., *infra*, 31a-51a. On January 9, 1997, the district court issued an order affirming the decision of the bankruptcy court. App., *infra*, 18a-30a. Relying on *Norton*, *supra*, the district court held that, under 11 U.S.C. 1141, confirmation of a Chapter 11 plan extinguishes a creditor's right to setoff. App., *infra*, 29a.

5. The United States appealed to the United States Court of Appeals for the Third Circuit, and argued that the reasoning of *Norton* was inconsistent with the rationale of *Citizens Bank of Maryland* v. *Strumpf*, 516 U.S. 16 (1995). The government contended that, under *Strumpf*, funds held by a creditor that may be subject to a setoff right are not to be treated as "property of the estate." Hence, such funds do not vest free and clear in the reorganized debtor upon confirmation of a plan of reorganization.

The United States also contended that confirmation under Section 1141 cannot extinguish pre-petition setoff rights because Section 553 specifies that none of the Code provisions (except as provided therein) affect a creditor's setoff rights.

On January 20, 1998, the Third Circuit affirmed the district court's judgment. The court agreed that *Norton* "implicitly held that the funds withheld by the creditor subject to set-off were 'property of the estate,'" and that under *Strumpf*, "the relevant 'property of the estate' is instead the bankrupt debtor's claim to the funds as opposed to the possession of the physical funds themselves." App., *infra*, 7a-8a. The court distinguished *Norton* and *Strumpf* on the ground that, in both of those cases, "the creditor retained possession of the funds; here the Government deposited the $4.8 million into the registry of the court pending an appeal." App., *infra*, 8a. The court held that such funds "are comparable to the res of a trust," and that the government had no beneficial interest in the funds at that juncture. *Ibid.* The court explained that, under *Norton*, the government's setoff right was extinguished by the confirmation of the plan: "Although the actual funds themselves may not have passed as property of the estate, upon confirmation of the plan, [respondent] did acquire a claim or interest in them subject only to final resolution of the Government's appeal." *Ibid.*

The court reasoned that allowing the government to attempt to exercise its setoff right post-confirmation could disadvantage the other unsecured creditors, disrupt the plan of reorganization, and protract the bankruptcy proceedings. App., *infra*, 9a-10a. Thus, the court concluded, "we reaffirm the ruling in *Norton* and hold that the right of a creditor to set-off

in a bankruptcy reorganization proceeding must be duly exercised in the bankruptcy court before the plan of reorganization is confirmed; the failure to do so extinguishes the claim." *Id.* at 13a.

6. On March 5, 1998, the United States filed a timely petition for rehearing and suggestion for rehearing *en banc*. In the petition, the government argued that the court's ruling was legally erroneous, inconsistent with this Court's *Strumpf* decision, in conflict with decisions of the Ninth and Tenth Circuits, contrary to the prevailing view of the lower courts, and based upon several critical erroneous factual assumptions. One of the factual errors identified in the rehearing petition was that the court of appeals appeared to base its legal conclusion on the incorrect assumption that the $4.8 million was in the estate's possession prior to confirmation of the plan of reorganization. On March 23, 1998, the court of appeals amended its decision to reflect that those funds were in fact held by the government until after the confirmation of the plan. Compare App., *infra*, 16a with App., *infra*, 8a. On that same date, the court denied the petition and the suggestion for rehearing *en banc*. *Id.* at 61a-62a.

REASONS FOR GRANTING THE PETITION

The court of appeals held that a creditor's setoff rights must be asserted in the bankruptcy proceedings and that setoff rights not asserted or provided for in the reorganization plan are extinguished by a Section 1141 confirmation order. That decision is inconsistent with the plain language of Section 553, this Court's decision in *Citizens Bank of Maryland* v. *Strumpf*, 516 U.S. 16 (1995), and the majority of court decisions, including decisions of the Ninth and Tenth

Circuits. Because the issue is fundamental to the sound administration of the Nation's bankruptcy laws—for governmental and private creditors alike—the Court should grant review.

1. a. The right of setoff permits a creditor to deduct a debt it owes to a debtor from a claim the creditor has against the debtor arising out of a separate transaction. See 5 *Collier on Bankruptcy* ¶ 553.01 (15th rev. ed. 1998). It "allows parties that owe mutual debts to state the accounts between them, subtract one from the other and pay only the balance." *In re Bevill, Bresler & Schulman Asset Management Corp.*, 896 F.2d 54, 57 (3d Cir. 1990). Setoffs have been an established part of the law dating back to the Roman Empire and have been incorporated into American bankruptcy law consistently since 1800. See *In re Davis*, 889 F.2d 658, 661 n.5 (5th Cir. 1989), cert. denied, 495 U.S. 933 (1990); 5 *Collier on Bankruptcy*, *supra*, ¶ 553.LH. The rule is based upon the "common sense notion that 'a man should not be compelled to pay one moment what he will be entitled to recover back the next.'" *In re Davis*, 889 F.2d at 661 n.5 (quoting Lloyd, *The Development of Setoff*, 64 U. Pa. L. Rev. 541, 541 (1916)). See also *In re Patterson*, 967 F.2d 505, 508 (11th Cir. 1992). This Court recently explained:

> The right of setoff (also called "offset") allows entities that owe each other money to apply their mutual debts against each other, thereby avoiding "the absurdity of making A pay B when B owes A."

Citizens Bank of Maryland v. *Strumpf*, 516 U.S. at 18 (quoting *Studley* v. *Boylston Nat'l Bank*, 229 U.S. 523, 528 (1913)).

In the bankruptcy context, without the right of setoff a creditor would have the "worst of both worlds." *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d 1269, 1277 (9th Cir.), cert. denied, 506 U.S. 918 (1992). Absent the setoff right, the creditor would have to pay the debtor in full, but would recover only a small portion of the fund it is owed. *Ibid.* To avoid that fundamental unfairness, Congress enacted Section 553 of the Bankruptcy Code. That provision specifically recognizes and preserves a creditor's setoff rights by stating that a creditor's setoff right for pre-petition mutual debts is *not* subject to the other Code provisions, except Sections 362 and 363 of the Code:

> Except as otherwise provided in this section and in sections 362 and 363 of this title, *this title does not affect any right* of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor that arose before the commencement of the case * * *.

11 U.S.C. 553(a) (emphasis added).

Section 553's instruction that "this title does not affect any right" of setoff on its face means that the other provisions of Title 11 (not mentioned in Section 553) simply do not affect a creditor's right to setoff. See *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d at 1276-1277. The court of appeals here held that the confirmation of a bankruptcy plan causes a creditor's claim to be discharged (except insofar as payment is provided for in the plan), and that the creditor's pre-petition setoff rights not provided for in the plan are extinguished upon confirmation. The

Code's provisions regarding discharge of debts and confirmation of reorganization plans, 11 U.S.C. 524, 1141, 1327, however, are *not* among the provisions listed in Section 553. See App., *infra*, 65a-66a. Because Section 1141 is omitted from the expressly specified provisions that create exceptions, the court of appeals' ruling conflicts with Section 553's general rule that a creditor's rights are not affected by the Bankruptcy Code.

b. Indeed, this Court has recognized that "Section 553(a) * * * sets forth a general rule, with certain exceptions, that any right of setoff that a creditor possessed prior to the debtor's filing for bankruptcy is not affected by the Bankruptcy Code." *Strumpf*, 516 U.S. at 20. Those "certain exceptions," the Court made clear, are those explicitly stated in the text of Section 553 "and in sections 362 and 363." *Ibid.* (quoting 11 U.S.C. 553(a)). The court below instead based its holding on Section 1141 of the Bankruptcy Code, which concerns the "property of the estate." See 11 U.S.C. 1141(b) ("Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor."). The court of appeals reasoned that, because confirmation vested a property right in the debtor's estate, the creditor's setoff rights were thereby extinguished because the debtor had a claim to that property. App., *infra*, 7a-8a; 16a-17a.

The court of appeals' holding and rationale cannot be squared with *Strumpf*, *supra*. In *Strumpf*, a bank held funds subject to a setoff right. The estate argued that the bank's retention of the funds violated the Bankruptcy Code's automatic stay, which prohibits a creditor from exercising "dominion over property that belong[s] to the [estate]." 516 U.S. at 21. This

Court unanimously rejected that argument, holding that refusal to pay a debt subject to a right of setoff is not an exercise of control over property of the estate. The Court explained that the refusal to pay "was neither a taking of possession of [the debtor's] property nor an exercising of control over it, but merely a refusal to perform [the creditor's] promise." *Ibid.*[3] Hence, under *Strumpf*, funds held by a creditor subject to a setoff claim are not "property of the estate." Those funds, therefore, are not properly subject to a Section 1141 confirmation order that would take precedence over a Section 553 right of setoff.

The decision below relied on circuit precedent that pre-dated *Strumpf*. See App., *infra*, 7a-9a, 16a-17a (discussing *United States* v. *Norton*, 717 F.2d 767 (3d Cir. 1983)). *Norton* treated funds held by the creditor subject to a possible setoff right as "property of the estate." Accordingly, *Norton* concluded that such funds vested free and clear in the reorganized entity emerging from bankruptcy. After *Strumpf*, however, it is now clear that *Norton*'s fundamental premise was incorrect. Funds being held by the creditor at the time of confirmation are not "property of the estate." See 516 U.S. at 21. Thus, such funds do not vest free and clear in the reorganized debtor upon confirmation of the plan.

The court of appeals here conceded that *Norton*'s reasoning is incorrect in one respect in light of this Court's subsequent decision in *Strumpf*. App., *infra*,

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[3] The Court declined to address the issue raised in this petition, whether "confirmation of [the debtor's] Chapter 13 plan under 11 U.S.C. § 1327 precluded petitioner's exercise of its setoff right," because the respondent had not raised that contention in the courts below. See 516 U.S. at 21 n.*.

6a. On the government's petition for rehearing, the court further conceded that the basic factual predicate for its initial decision—that the funds had been transferred from the government to the court registry (and thereby, in the court's view, were part of the debtor's estate) prior to confirmation of the plan—was also incorrect. See App., *infra*, 16a. The court nonetheless adhered to the result in *Norton* that a creditor loses its setoff right upon confirmation. The court provided no cogent explanation for that conclusion, or how it can be reconciled with the language of Section 553 and this Court's decision in *Strumpf*. App., *infra*, 16a-17a.

2. The court of appeals' decision conflicts with those of the majority of other courts, which have held that neither confirmation of a reorganization plan nor discharge of a claim affects a creditor's setoff rights for mutual pre-petition debts. See *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d at 1276-1277; *In re Davidovich*, 901 F.2d 1533, 1539 (10th Cir. 1990); *In re South Park Care Assocs.*, 203 B.R. 445, 447-448 (Bankr. W.D. Mo. 1996); *In re Wiegand*, 199 B.R. 639, 641-642 (W.D. Mich. 1996); *In re Pettibone Corp.*, 161 B.R. 960 (N.D. Ill. 1993), aff'd in part, and remanded in part on other grounds, 34 F.3d 536 (7th Cir. 1994); *In re Buckner*, 218 B.R. 137, 144 (B.A.P. 10th Cir. 1998); *id.* at 149 (Matheson, Bankruptcy Judge, concurring); *In re Buckenmaier*, 127 B.R. 233, 236-237 (9th Cir. B.A.P. 1991); *In re Sedlock*, 219 B.R. 207, 209-210 (Bankr. N.D. Ohio 1998); *In re Holder*, 182 B.R. 770, 775 (Bankr. M.D. Tenn. 1995); *In re Womack*, 188 B.R. 259, 261-262 (Bankr. E.D. Ark. 1995). That conflict has been noted by the leading commentary on bankruptcy law, which has endorsed the majority position as the "better view" that confirmation and discharge

by a reorganization plan do not extinguish a creditor's setoff rights. 5 *Collier on Bankruptcy*, *supra*, ¶ 553.08[1]-[2].[4]

The court of appeals attempted to distinguish *In re De Laurentiis Entertainment Group* on the ground that the Ninth Circuit "predicated its decision upon the particular facts * * *, including the creditor's diligent pursuit of its set-off claim before the bankruptcy court." App., *infra*, 10a. The Ninth Circuit mentioned those facts, however, only *after* it had already ruled, as a matter of law and of statutory construction, that confirmation of a bankruptcy reorganization plan does not compromise a creditor's setoff rights. *In re De Laurentiis Entertainment Group*, 963 F.2d at 1276-1277. The Ninth Circuit explained that Section 553(a)'s "language not only establishes a right to setoffs in bankruptcy, subject to enumerated exceptions, but seems intended to control notwithstanding any other provision of the Bankruptcy Code." *Ibid.* "To give section 1141 precedence would be to ignore this language." *Id.* at 1277. Thus, the court held:

> We conclude that section 553 must take precedence over section 1141. In reaching this conclusion, we rely not only on the foregoing persuasive authority, but also on the language and structure of section 553 and the policies which underlie it.

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[4] For the "minority" view cases, see, *e.g.*, *United States* v. *Norton*, 717 F.2d 767, 774 (3d Cir. 1983); *In re Dezarn*, 96 B.R. 93, 94-95 (Bankr. E.D. Ky. 1988); *In re Hackney*, 20 B.R. 158, 159 (Bankr. D. Idaho 1982); *In re Holcomb*, 18 B.R. 839, 841 (Bankr. S.D. Ohio 1982); *In re Johnson*, 13 B.R. 185, 188-189 (Bankr. M.D. Tenn. 1981).

Id. at 1276. That holding is directly contrary to the court of appeals' decision in this case.

The Third Circuit's decision is also at odds with the Tenth Circuit's decision in *In re Davidovich*, 901 F.2d at 1538-1539. In *Davidovich*, the creditor asserting the setoff right did not file a proof of claim or assert its setoff right in the bankruptcy proceeding prior to the court's discharge order. Although *Davidovich* involved a Chapter 7 bankruptcy, the court's analysis is not limited to that context.[5] Whether the discharge order is under Section 524 (as in *Davidovich*) or under Section 1141 (as is the case here and in *De Laurentiis*), the relevant legal question is whether, notwithstanding the discharge of the debtor's personal obligations, the plain language of Section 553(a) controls and the creditor's setoff rights as to mutual pre-petition claims remain intact. On that question the Tenth Circuit held that, under Section 553(a), the Bankruptcy Code "does not affect" a creditor's setoff rights. *In re Davidovich*, 901 F.2d at 1539. The court concluded that a creditor need not file a claim to preserve a setoff right, and that "the right to assert a setoff against a mutual prepetition debt * * * survives even the Bankruptcy Court's discharge of the bankrupt's debts." *Ibid.*

3. By ignoring the clear language of Section 553(a) and adopting the minority view of the extinguishment of creditor's rights after confirmation of the debtor's plan, the court of appeals has significantly impaired creditors' rights in bankruptcy in several important respects.

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[5] Similarly, the court below concluded that Third Circuit precedent in *Norton* was not limited to the Chapter 13 context. See 717 F.2d at 774.

a. Under the Code, a creditor owing funds to the debtor is expressly permitted to retain the funds that are possibly subject to a setoff right. See 11 U.S.C. 542(b). The creditor may hold the funds without violating the automatic bankruptcy stay and wait for the debtor or estate to sue it to recover the funds. See *Strumpf*, 516 U.S. at 20-21. When the debtor or estate sues the creditor, the creditor may then raise the setoff as a defense. See *Newbery Corp.* v. *Fireman's Fund Ins. Co.*, 95 F.3d 1392, 1398 (9th Cir. 1996); *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d at 1277; *In re Davidovich*, 901 F.2d at 1539; 5 *Collier on Bankruptcy*, *supra*, ¶ 553.07[1]-[2].

By contrast, the court of appeals here held that the setoff right abates unless it is adjudicated before confirmation or preserved explicitly in the confirmed plan of reorganization. That ruling has the effect of preventing a creditor from retaining funds subject to a setoff claim and raising the setoff right as a defense when sued by the debtor, as the creditor is otherwise permitted to do under the Code. The holding below instead requires a creditor affirmatively to assert its setoff right in the bankruptcy proceeding, and mandates that the setoff defense will be lost if not provided for in the reorganization plan. App., *infra*, 13a. The Ninth Circuit specifically rejected that view, under which "setoffs would be allowed under Chapter 11 only where they were written into a plan of reorganization." *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d at 1277. By giving no effect to Section 553 unless a creditor affirmatively seeks to have its setoff rights expressly protected in the plan, the Third Circuit's rule would leave a creditor's setoff rights subject to the will of the other creditors

(who, like the debtor, would ordinarily have no incentive to grant the setoff rights).

As the Ninth Circuit has held, that result is tantamount to reading Section 553 out of the Bankruptcy Code. *In re De Laurentiis Entertainment Group, Inc.*, 963 F.2d at 1277 ("Section 553 would then be largely superfluous, since a setoff could be written into the plan even without section 553."). See also *In re Pettibone Corp.*, 161 B.R. at 964. No Code provision, however, requires the assertion of the setoff in a proof of claim or any other type of assertion of a setoff right in the bankruptcy court prior to confirmation.

b. The court of appeals' decision also rests upon a fundamental misunderstanding of the effect of a discharge under established principles of bankruptcy law. A discharge does *not* eliminate or extinguish a debt. It prohibits the creditor from enforcing it as a "personal liability" against the reorganized entity emerging from bankruptcy after discharge. See *Hall* v. *National Gypsum Co.*, 105 F.3d 225, 229 (5th Cir. 1997). Discharge of a debt does not prevent a creditor from enforcing the debt in other ways, such as against a co-signor, guarantor, or surety. See *In re Walker*, 927 F.2d 1138 (10th Cir. 1991). See also *Johnson* v. *Home State Bank*, 501 U.S. 78, 84 (1991) ("a bankruptcy discharge extinguishes only one mode of enforcing a claim—namely, an action against the debtor *in personam*"). As to enforcement of a debt post-discharge, the "crucial inquiry" is whether the creditor is seeking to collect property of the estate that vested free and clear in the new entity. If so, the discharge order bars the collection. See *Hall*, 105 F.3d at 229. If not, the collection effort is entirely proper under the Code.

The assertion of a pre-petition setoff right against a pre-petition claim is not an attempt to collect affirmatively from the new entity. See *In re DeLaurentiis*, 963 F.2d at 1278; *In re Wiegand*, 199 B.R. at 641-642. Nor (as the court of appeals here conceded) is it an attempt to collect property that was in the estate at the time of the discharge order. Thus, as the Tenth Circuit has held, "the right to assert a setoff against a mutual, prepetition debt owed the bankrupt estate survives even the Bankruptcy Court's discharge of the bankrupt's debts." *In re Davidovich*, 901 F.2d at 1539; see also 5 *Collier on Bankruptcy*, *supra*, ¶ 553.08[1]-[2]. The decision below is directly to the contrary.

c. The court further erred in assuming that the assertion of a setoff right post-confirmation would disadvantage the other creditors and could disrupt the reorganization plan. See App., *infra*, 12a. Not only are those policy considerations insufficient to overcome the plain language of Section 553, they are incorrect in their own right. The reorganization plan approved in this case did not mention the *Alaska Airline* litigation or include proceeds from it as an asset. The plan did not distribute the *Alaska Airline* funds to the creditors or rely on the funds to support the reorganized debtor. C.A. Supp. App. B135-B138. Indeed, respondent apparently plans to keep those disputed funds for itself. Thus, permitting the government to assert a setoff right would not disadvantage any other creditor.

Nor was the court of appeals persuasive in suggesting that post-confirmation setoffs would protract bankruptcy proceedings. Chapter 11 bankruptcy proceedings do not end upon confirmation of the reorganization plan. The federal agencies have not yet

been paid anything on the bulk of their claims (which were duly filed in a timely fashion in the bankruptcy proceeding) almost *five years after confirmation* of respondent's plan, because the trustee's objections to the claims have not yet been adjudicated. Plainly, the bankruptcy proceedings here have not ended with the confirmation of the plan; allowing the United States to retain its setoff rights would not unduly delay the administration of the reorganization plan. Nor is this case factually unique in that respect. In any event, a creditor's post-confirmation assertion of setoff rights generally should not unduly delay the bankruptcy proceedings. A debtor can always force the creditor's hand by suing the creditor for the funds and thereby require the creditor to assert the setoff defensively before the funds are turned over.

Indeed, not only was the court incorrect in assuming that other creditors and the bankruptcy process itself would suffer, its decision places an unjustified and disproportionate burden on creditors that have setoff rights—whether they are private or public entities. Debtors will have every incentive to omit any reference to setoff rights in the plan and to do nothing about setoff until the plan is confirmed. Other creditors will not know of the funds the debtor plans to obtain after confirmation, and the plan will not provide for their distribution to creditors. Only the reorganized debtor stands to benefit from the extinguishment of a creditor's setoff rights. The decision below would allow debtors to obtain assets to which they had no right at the time of the bankruptcy filing and would ensure that those assets will not be distributed pursuant to the plan. As a result, creditors would have to monitor all plans of reorganization and object to every plan that does not contain an

express preservation of their setoff rights. Such a requirement would needlessly protract bankruptcy proceedings and require the expenditure of scarce resources. This Court should not countenance such an unwarranted departure from the express statutory scheme Congress has provided.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted.

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