

Piccadilly Predicament Concerning Pre-Confirmation Transfers

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In its recent decision in *Florida Dept. of Revenue v. Piccadilly Cafeterias, Inc.*, the U.S. Supreme Court addressed the issue of whether the stamp tax exemption under 11 U.S.C. § 1146(a) applies to asset transfers made *before*, as opposed to *after*, a plan of reorganization is confirmed under 11 U.S.C. § 1129.² The Court held that the stamp tax exemption applies only to transfers made after a Chapter 11 plan has been confirmed.³ The Court justified this reading based on the “natural” reading of the statute, the provision’s placement in the Bankruptcy Code, and applicable canons of statutory construction support this conclusion.⁴ This holding resolves a 2-2 split that existed among the circuit courts that had considered this issue.⁵

In *Piccadilly*, Piccadilly Cafeterias, Inc. (“Piccadilly”) filed for Chapter 11 bankruptcy and requested the Bankruptcy Court to conduct an auction of substantially all of Piccadilly’s assets. At the auction, Piccadilly Investments, LLC, made the highest bid of \$80 million. The Bankruptcy Court later approved the sale of Piccadilly’s assets to Piccadilly Investments, and held that the sale was exempt from stamp taxes under § 1146(a). The Bankruptcy Court denied a motion by the Florida Dept. of Revenue

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² Fla. Dep’t of Revenue v. Piccadilly Cafeterias, Inc., 2008 WL 2404077 (U.S. June 16, 2008).

³ *Id.* at *13.

⁴ *Id.*

⁵ Compare *In re Jacoby-Bender, Inc.*, 758 F.2d 840 (2d Cir. 1985) and *Piccadilly*, 484 F.3d 1299 (11th Cir. 2007) (holding that the stamp tax exemption under § 1146(a) applies to both pre- and post-confirmation transfers) with *In re Hechinger Inv. Co. of Del.*, 335 F.3d 243 (3d Cir. 2003) and *In re NVR, LP*, 189 F.3d 442 (4th Cir. 1999) (holding that the stamp tax exemption under § 1146(a) applies only to post-confirmation transfers).

(“Florida”) to reconsider, or amend the sale order. Piccadilly subsequently filed a Plan of Liquidation. Florida objected to the plan and commenced an adversary action by filing a complaint against Piccadilly, seeking a declaration that the stamp taxes were not exempt under § 1146(a). The Bankruptcy Court overruled the objection and confirmed the plan. Florida then filed an amended complaint in the adversary proceeding, and both Piccadilly and Florida filed motions for summary judgment. After a hearing, the bankruptcy court granted summary judgment in favor of Piccadilly, holding that the asset sale was exempt from stamp taxes under § 1146(a). The bankruptcy court reasoned that the sale of substantially all of Piccadilly’s assets was a transfer “under” its confirmed plan of reorganization because the sale was necessary to consummate the plan. On appeal, the district court affirmed the bankruptcy court’s order granting summary judgment to Piccadilly.

Florida appealed the district court’s order to the Eleventh Circuit, arguing that the district court erred in holding that the § 1146 stamp tax exemption may apply to pre-confirmation asset sales. In a per curiam decision, the Eleventh Circuit upheld the decision and rejected Florida’s argument, holding that the stamp tax *does* apply to pre-confirmation transfers. The appellate court first considered holdings in the Third and Fourth Circuit that the § 1146(a) exemption does not apply to such transfers.⁶ Both of these courts held that the plain language of the statutory phrase “under a plan confirmed” means “authorized by,” and therefore a transfer could not be authorized by such a plan without a confirmed plan already in existence.⁷ The Eleventh Circuit also considered a decision out of the Second Circuit, which held that the phrase “under a plan” refers to a

⁶ In *Re Piccadilly*, 484 F.3d 1299; *see also* *Hechinger*, 335 F.3d 243 *and* *NVR*, 189 F.3d 442.

⁷ *See* *Hechinger* 335 F.3d at 252-54; *NVR*, 189 F.3d at 456-58.

transfer that is necessary to the consummation of a confirmed Chapter 11 plan.⁸ The court found that this was the better reasoned approach, since it looks not to the timing of the transfer, but to the necessity of the transfer to the consummation of a confirmed plan of reorganization.⁹ The court provided four reasons for its holding. First, the court found that the plain language of the statute is ambiguous, supporting two different readings—one supporting tax exemption, and the other rejecting such exemptions.¹⁰ Second, the court noted that Congress could have placed a temporal restriction in the statute had it wanted to, but it did not.¹¹ Third, the court held that the Bankruptcy Code should be liberally construed, and although grants of tax exemptions should be narrowly construed, they should not be abrogated through too narrow an application.¹² Lastly, the court held that temporal restrictions on the statute ignore the practical realities of Chapter 11 cases, which may necessitate a pre-confirmation sale as a condition precedent to the parties' willingness to proceed with confirmation of a plan.¹³ Based on these reasons, the court concluded that the tax exemption under § 1146(a) applies to all pre-confirmation transfers that are necessary to the consummation of a confirmed plan of reorganization, but the Court noted that there must be some nexus between the pre-confirmation sale and the confirmed plan.¹⁴

Despite district and appellate court decisions accepting Piccadilly's interpretation of the Code, the Supreme Court reversed the Eleventh Circuit's decision and remanded

⁸ See *Jacoby-Bender*, 758 F.2d at 841.

⁹ *In re Piccadilly*, 484 F.3d at 1303-04.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ *In re Piccadilly*, 484 F.3d at 1303-1304.

the case for further proceedings.¹⁵ Writing for the Court, Justice Thomas explained that the decision was appropriate based on the “most natural reading of §1146(a)’s text, the provision’s placement within the Code, and applicable substantive canons.”¹⁶ The Court’s ruling renders stamp-tax exemptions applicable only when the transfers are made pursuant to a confirmed Chapter 11 plan.

The Supreme Court rejected Piccadilly’s interpretation that 1146(a) simply required the transfer to be “in accordance with” a plan confirmed under 1129 and that no temporal requirements were imposed. The Court held that such an interpretation “places greater strain on the statutory text than the simpler construction advanced by Florida and adopted by the Third and Fourth Circuits.”¹⁷ Florida’s proffered interpretation is that the exemption applies only to transfers made after the plan is confirmed because “confirmed” is a past participle that indicates “past or completed action.”¹⁸

Justice Thomas acknowledged that both Piccadilly and Florida offered credible interpretations of 1146(a); however, the Court determined that Florida’s interpretation was “the better one.”¹⁹ The Court went on to state that even if it were to accept Piccadilly’s arguments, such arguments would only establish that the language was ambiguous at most.²⁰ And, the Court found no grounds for resolving any ambiguity in Piccadilly’s favor. Instead, the Court found Florida’s arguments regarding the statute’s placement in the Code and other substantive canons to indicate that such ambiguity should be resolved in Florida’s favor. For example, the Court gave credence to Florida’s

¹⁵ Piccadilly, 2008 WL 2404077, at *13.

¹⁶ *Id.*

¹⁷ *Id.* at *5.

¹⁸ *Id.* at *4.

¹⁹ *Id.* at *5.

²⁰ Piccadilly, 2008 WL 2404077. at *9.

argument that the tax exemption’s placement in the “POSTCONFIRMATION MATTERS” section of the bankruptcy code indicated that the exemption should be interpreted as applying only to post-confirmation transfers.²¹ In addition, the Court held as decisive the canon of statutory construction that courts should not recognize an exemption from state taxation that Congress has not clearly expressed.²² So, even assuming the phrase “under a plan confirmed” is ambiguous as *Piccadilly* asserts, the ambiguity must be construed against interfering with a state’s authority to tax.²³

The Court also noted the additional benefit provided by the clear rule proposed by Florida. The Eleventh Circuit’s reading requires that there be “some nexus between the pre-confirmation transfer and the confirmed plan.”²⁴ However, no such requirement is imposed under Florida’s construction, which provides a “simple, bright-line rule instead of the complex, after-the-fact inquiry *Piccadilly* envisions.”²⁵ Based on the natural reading of the text of 1146(a), its placement within the Bankruptcy Code, the substantive canons proposed by Florida, and the applicational advantages of a bright-line rule, the Court held that the stamp tax exemption under § 1146(a) cannot be read to extend to pre-confirmation transfers.

Future Impact

The *Piccadilly* decision has obvious immediate impact on pending liquidating Chapter 11 cases. As a result of the Supreme Court’s ruling, now the debtor will be unable to obtain a stamp tax waiver in the context of a § 363 sale.

²¹ *Id.* at *8.

²² *Id.* at *11.

²³ *Id.*

²⁴ *Id.* at 5.

²⁵ *Piccadilly*, 2008 WL 2404077. at *12.

The case may have other implications, too. The Court certainly acknowledged, as did the district, that cases providing for the sale of substantially all amounts of the estate are common and, incidentally, allowed.

More important for future cases may be the “natural” method of Code interpretation. This approach may affect the future of the provisions of BAPCPA, which are, in places, less than clear.