# 09-5122-bk
# 09-5142-bk

## United States Court of Appeals
## for the Second Circuit

ENRON CREDITORS RECOVERY CORP.,
*Plaintiff-Appellant,*

v.

ALFA, S.A.B. DE C.V., ING VP BALANCED PORTFOLIO, INC., ING VP BOND PORTFOLIO, INC.,
*Defendants-Appellees.*

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

**BRIEF OF AMICUS CURIAE**
**SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION**
**IN SUPPORT OF APPELLEES AND IN FAVOR OF AFFIRMANCE**


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## CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rules of Appellate Procedure 26.1 and 29(c), amicus curiae the Securities Industry and Financial Markets Association hereby certifies that it is a non-profit corporation. It has no parent corporation and no publicly-held corporation owns 10% or more of its stock.

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## STATEMENT OF INTEREST[1]

The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

SIFMA has a particular interest in the commercial paper market. Working with member firms, SIFMA has developed widely-accepted form contracts that have successfully advanced standardization in that market. *See, e.g.*, SIFMA Model Commercial Paper Dealer Agreement: 3(a)(3) Program.[2] SIFMA also was involved in the development of several of the provisions of the Bankruptcy Code that are at issue in this case. *See, e.g.*, International Swaps and Derivatives Association, Inc. & The Public Securities Association, *Financial Transactions*

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1 Pursuant to Local Rule 29.1(b), SIFMA states that no party's counsel authored this brief in whole or in part; that no party or party's counsel contributed money that was intended to fund preparing or submitting the brief; and that no person other than SIFMA, its members, and its counsel contributed money that was intended to fund preparing or submitting this brief.

2 *Available at* http://www.sifma.org/services/stdforms/pdf/guaranteed_3-a-3_cp_dealer_ agreement.pdf.

*Insolvency: Reducing Risk through Legislative Reform*, 13-14 (1996).[3] The issues at stake here bear directly on SIFMA's role in enhancing the safety and efficiency of U.S. financial markets.

SIFMA often appears as amicus curiae in cases raising issues of importance to the securities markets and the commercial banking industry (including by submitting two briefs in the Bankruptcy Court below), and courts frequently rely on its views and those of its predecessor organizations. *See, e.g.*, *Arnold Chase Family, LLC v. UBS AG*, No. 3:08cv00581, 2008 WL 3089484, at *1 (D. Conn. Aug. 4, 2008); *Bevill, Bresler & Schulman Asset Mgmt. Corp. v. Spencer Sav. & Loan Ass'n*, 878 F.2d 742, 745 (3d Cir. 1989); *RTC v. Harris Trust & Sav. Bank*, No. 90 C 7330, 1992 WL 223807, at *6 & n.13 (N.D. Ill. Sept. 2, 1992) (all citing amicus briefs). The threat that the appellant's position poses to the commercial paper market and the rehabilitation of companies in financial distress implicates SIFMA's interests here. Federal regulators recognize that the market for commercial paper is a "critical financial market" that provides "the means for banks, securities firms, and other financial institutions to adjust their cash and

[3] This white paper was prepared by PSA in conjunction with ISDA, the trade association for the swaps and derivatives industry. PSA was a predecessor to The Bond Market Association, which in turn was a predecessor to SIFMA.

securities positions and those of their customers in order to manage liquidity, market, and other risks to their organizations."[4]

If, as the Bankruptcy Court held, bankruptcy trustees may reopen long-settled buyback transactions such as those as issue in this case, that risk will diminish the opportunity of weakening companies to secure longer-term financing, removing a valuable stabilizing mechanism. It will also unduly punish investors in commercial paper, who will be unable to sell back their paper if financial intermediaries are unwilling to risk a later avoidance action—indeed, in this very case, those intermediaries incurred huge expenses litigating and then settling.

In fact, the extremely narrow interpretation of Section 546(e) advanced by Enron Creditors Recovery Corp. ("Enron") threatens not only the commercial paper market, but all markets in which debt is traded. Enron's position on appeal goes even farther than the erroneous holding of the Bankruptcy Court, by asserting that ***absolutely no*** instruments cleared by the Depository Trust Corporation ("DTC") can qualify for the safe harbor. By carving unexpected and unwritten exceptions into the statutory safe harbor for settlement payments, Enron would inject substantial uncertainty into the clearing of trades in debt securities and

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4 Federal Reserve Sys. Docket No. R-1128, Dep't of Treasury, Office of the Comptroller of the Currency Docket No. 03-05, SEC Release No. 34-47638, *April 7, 2003 Interagency Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System* ("Interagency Paper"), *available at* www.sec.gov/news/studies/34-47638.htm.

threaten the type of cascading market losses that Section 546(e) was designed to avoid.

For those reasons, SIFMA urges this Court to affirm the decision of the District Court.

## SUMMARY OF THE ARGUMENT

This case concerns the application of Section 546(e) of the Bankruptcy Code to the early redemption of commercial paper. Section 546(e) provides in relevant part that:

> the trustee may not avoid a transfer that is a . . . settlement payment, as defined in section 101 or 741 of this title, made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency . . . .

Section 741(8) defines "settlement payment" to "mean[] a preliminary settlement payment, a partial settlement payment, an interim settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade." The question is whether Section 546(e) applies, as its plain language states, to all payments that settle securities trades, or whether it contains various exceptions, all unwritten, that carve-out, among other things, all debt securities from the safe harbor.

The commercial paper market is of critical importance to the nation's economy. The transactions at issue here settled at the DTC in the same way that over $100 billion dollars of commercial paper transactions settle each day. Congress enacted the safe harbor for the clear and explicit purpose of providing certainty and predictability in settling securities transactions such as these.

The safe harbor standard advanced by Enron, by contrast, amounts to a hodgepodge of exceptions, each of which is contrary to the statute's purpose. Whether the transferee of a security also happens to be the issuer of that security has nothing to do with the sound policies underlying the safe harbor. Nor does the identity of the clearinghouse, or the particular clearing method. The safe harbor was designed to avoid market disruption that would result if a bankruptcy court had the power, years after the event, to unwind the settlement of securities trades made through financial intermediaries. The District Court recognized that both the text of the statute and its underlying purpose squarely apply here. Aside from their substantive flaws, Enron's proposed exceptions threaten to inject uncertainty into market transactions, because they are highly technical and would be impossible for market participants to evaluate (and apply or not) in the short period that may be available in determining whether to participate in a commercial paper buyback. The broad interpretation of Section 546(e) that courts across the country—and the District Court below—have adopted far better serves the purposes of the statute and ***faithfully implements its text***.

## ARGUMENT

### I. The Commercial Paper Market Has a Special Need for Safe Harbor Protection.

#### A. Commercial paper is a critical source of funding for many companies, and stability in that market is critical.

Commercial paper has historically played an important role in the financing and growth of U.S. corporations. The commercial paper market is a "critical financial market" that provides "the means for banks, securities firms, and other financial institutions to adjust their cash and securities positions and those of their customers in order to manage liquidity, market, and other risks to their organizations."[5] Industrial issuers use commercial paper as a source of working capital, finance companies use it to fund consumer and small-business loans, and public utilities use commercial paper to purchase raw materials and fund construction. *See generally* Federal Reserve Bank of Richmond, *Instruments of the Money Market* 108–10 (reissued 1998) ("Richmond Fed Report").[6] The commercial paper market is very large, with over $1 trillion outstanding as of August 18, 2010; even that figure was down almost a third from the end of 2008.

5 Interagency Paper, *supra*; *see also* Zuckerman, *Sinking Commercial Paper Market Broadens Effect of Enron Troubles*, WALL ST. J., March 28, 2002.

6 *Available at* http://www.richmondfed.org/publications/research/-special_reports/instruments_of_the_money_market/pdf/chapter_09.pdf.

*See* Federal Reserve Release, *Commercial Paper Outstanding*.[7] It is this broad access to inexpensive financing afforded by the commercial paper market that Congress recognized (as explained below) as warranting special legislative protection from the hazards of a market participant's insolvency.

Because of its short maturity, commercial paper has a very low default rate, historically much lower than the default rate on ordinary commercial loans. *See* Richmond Fed Report, *supra*, at 119 ("Historically, the commercial paper market has been remarkably free of default."). As a result of this minimal credit risk, the interest rate on commercial paper is typically several percentage points lower than that of long-term bonds and bank loans.

But the very characteristic that makes commercial paper so useful—its safety—also makes the market fragile and highly sensitive to legal changes that introduce uncertainty. Not only does commercial paper have a short contractual maturity period, but the short period of attendant risk is confirmed by the understanding that payments on such paper are immune from a bankruptcy trustee's avoidance powers. That immunity means that the holder of commercial paper need not worry about being drawn in to a bankruptcy proceeding that begins months after the paper matures. If Enron's current position were adopted by this Court, however, that risk would reappear and would apply to an even broader

[7] *Available at* http://www.federalreserve.gov/releases/cp/outstandings.htm (last visited Aug. 19, 2010).

range of securities than that reached by the Bankruptcy Court's opinion. The consequences for the market could be grave.

### B. Issuers in financial distress often avoid insolvency by replacing commercial paper with longer-term debt.

Enron argues that the payments at issue here were "aberrant and extraordinary," not of a type "commonly used in the securities trade." Br. 57.[8] Nothing could be farther from the truth. Most relevantly, the ***payments*** that settled these transactions were the same type of ***payments*** that are always used to settle trades of commercial paper. It is undisputed that the transactions here were settled either by "delivery-versus-payment" (by which the securities and purchase price are exchanged simultaneously) or "free delivery" (which allows the two to be separated) and that those methods are common—they are the very methods used to settle well over $100 billion of commercial paper every day at DTC. *See* DTC & The Bond Market Association, *Issues and Recommendations Regarding Commercial Paper Settlement Practices* (March 2003), at 4 ("Issues & Recommendations").[9] Even if the section did impose some commonness

[8] SIFMA agrees with the District Court's conclusion that the "commonly used" clause should not be applied to narrow the meaning of each type of settlement payment: if a transfer is a "settlement payment," it satisfies the definition, regardless of whether it is also common. Nonetheless, even if the District Court's parsing of the definition were incorrect, the payments here satisfy any test of commonness.

[9] *Available at* http://www.dtcc.com/downloads/leadership/whitepapers/-cppaper.pdf.

requirement, it imposes it on the "settlement ***payment***," and there is no question that the payments here met that standard.

Enron glosses over the mode of payment and instead focuses on the fact that the transactions were in connection with Enron's negotiated "pre-payment" of its commercial debt, shortly before maturity. Br. 57. It then asserts that such buyback transactions are not common. But that, too, is incorrect. Firms facing financial challenges often wish to replace their short-term debt with longer-term sources of financing, such as may be available under an existing line of credit. As the record below demonstrates, in just the last decade, hundreds of commercial-paper issuers have repurchased their paper prior to maturity. *See* Bankr. Court Docket #1753 at 58–59 (summarizing sealed expert reports). When these buy-backs of outstanding paper help a company to restore the confidence of credit markets and avoid bankruptcy, the safe harbor, of course, is not implicated. But pre-payments would be effectively impossible if holders of the paper knew that they could later be avoided.

## II. Section 546(e) protects against systemic risk, not threats to particular clearinghouses.

Enron criticizes the District Court for taking an "expansive view of the safe harbor" and an "expansive view of the legislative purpose." Br. 35. Enron posits that "the primary concern of Congress was to protect clearing systems," not "to protect[] the stability of the securities market from the systemic risk of insolvencies spreading from collapsed securities institutions to other firms." *Id.* In fact, however, courts uniformly interpret the safe harbors—including Section 546(e)—broadly. Moreover, both courts and Congress have described the legislative purpose in precisely the terms that Enron disputes, explaining that the statute is intended to prevent "the insolvency of one commodity or security firm from spreading to other firms" and "threaten[ing] the collapse of the affected industry." H.R. REP. 97–420, at 2 (1982) (quoted in *In re Enron Creditors Recovery Corp.*, 422 B.R. 423, 429 (S.D.N.Y. 2009)). Enron offers no persuasive reason for this Court to declare a new, narrow reading of these provisions.

### A. The Safe Harbors Should Be, and Are, Interpreted Broadly.

Reflecting Congress's concern with protecting financial markets and with removing uncertainty over the application of statutory safe harbors to particular payments, courts consistently have noted that Section 546(e) and its relevant definitions are read broadly, and not in the cramped fashion advanced by Enron. The Third Circuit has held repeatedly that the definition of "settlement payment" is "extremely broad." *Lowenschuss v. Resorts Int'l*, 181 F.3d 505, 515 (3d Cir. 1989); *Bevill, Bresler & Schulman*, 878 F.2d at 751 ("Section 741(8) of the 1982 amendments gives an extremely broad definition of 'settlement payment'"). So have the Tenth and the Ninth Circuits. *See In re Kaiser Steel Corp.*, 952 F.2d 1230, 1237 (10th Cir. 1991) ("As a natural reading suggests, and as we and others have noted, this definition is "extremely broad."); *In re Comark*, 971 F.2d 322, 325 (9th Cir. 1992) ("Fortunately, the courts that have addressed the meaning of the term 'settlement payment' in the Bankruptcy Code provisions at issue adopt a uniform approach. We follow our sister circuits in adopting a broad definition of settlement payment"); *see also In re Blanton (Blanton v. Prudential-Bache Securities, Inc.),* 105 B.R. 321, 347 (Bankr. E.D. Va.1989) (definition is "very broad").

Narrow, technical readings are undesirable in this context, because the uncertainty that they engender would threaten the confidence of market participants, who often need to make trading decisions without the time for extensive legal analysis. *See Matter of Munford, Inc.*, 98 F.3d 604, 610 n.4 (11th Cir. 1996) ("even granting trustees avoidance powers under limited circumstances in the LBO context has the potential to lessen confidence in the commodity market as a whole"). That point has been made persuasively in the context of Section 547(c)(2) (the "ordinary course" exception):

> To the extent that the preference laws enter into the trade creditor's calculation of whether to do business with the debtor or not, they provide a disincentive to deal, because they increase the risk of eventual non-payment. However, to the extent trade creditors are aware of preference exceptions, and are able to use them creatively to prevent the subsequent avoidance of preferential transfers, this disincentive is reduced. Section 547(a)(2) can only reduce the disincentive to deal if it is read in such a way as to address the preference problem created by debtor/trade creditor workout.

Michael J. Herbert, *The Trustee Versus the Trade Creditor II: The 1984 Amendment to Section 547(c)(2) of the Bankruptcy Code*, 2 EMORY BANKR. DEVELOPMENTS J. 201, 205 (1985).

Similarly, a restrictive reading that creates uncertainty over whether any particular payment in exchange for commercial paper will satisfy a byzantine multi-step test to qualify for Section 546(e) would undermine the purpose of the statute and damage the commercial paper market. *See In re Adler, Coleman Clearing Corp.*, 263 B.R. 406, 477 (S.D.N.Y. 2001) ("These interests demand ***stability and certainty*** in settled transactions, and ***legal definitions adaptable to the usage, understanding and realities of the market***. To promote these aims, Congress adopted § 546(e) . . . . The statute recognizes that if the pre-bankruptcy transactions of a securities broker-debtor could be readily reversed, confidence in the chain of guarantees upon which the functioning of the system depends would be undermined and the entire market could be threatened by serial bankruptcies.") (emphasis added). As noted above, it is in part because commercial paper buyers do not have to worry about bankruptcy complications that the market can provide companies with financing on such advantageous terms. Hence, the Court should give effect to the comprehensive and practical scope that Congress intended and signified in the statutory language rather than imposing the kind of artificial limitations that Enron urges.

**B. Enron's distinction between debt repurchases and other securities trades is irrelevant in light of congressional intent.**

1. Sections 546(e) and 741(8) do not carve-out issuer repurchases from the safe harbor.

Enron argues that the applicability of Section 546(e) depends upon the relationship of the debtor-purchaser to the security; it suggests that Section 546(e) applies only to securities issued by third parties and not to those issued by the debtor. Br. 45–51. Rather than rely on the plain text of the Code, however, Enron builds a mountain of sequential definitions: a "settlement payment" under Section 741(8) requires a "securities transaction" as defined in the Securities Exchange Act (not the Bankruptcy Code); that in turn requires a "purchase," which itself depends on a "transfer of ownership." *Id.* at 22, 28, 30–31. This last point depends on an arcane analysis that apparently is to be governed by the U.C.C., but which Enron delegates to expert witnesses rather than legal authorities. *Id.* at 27. This precarious edifice is arbitrary and has no support in the text of Section 546 or its purpose.

Section 546 references only one definition, that of "settlement payment" in Section 741(8). It does not mention the Exchange Act or any definition of "securities transaction," or purport to require a purchase or a technical transfer of ownership. Rather, the focus of the safe harbor is on the payment side of the transaction ("settlement payment," "margin payment"), not on what happens to the securities afterward. That focus is natural, because it is the belated recovery of payments from a chain of market intermediaries that threatens instability—the claw-back of a payment would be no less harmful because the payment "extinguished" a debt rather than changed its "ownership."

Indeed, other safe harbors cover payments under repurchase agreements (subsection (f))—which do not go through clearinghouses—and swap agreements (subsection (g))—which are not cleared and also involve no transfer of ownership. The broad scope of Section 546 is no accident. It reflects a broad legislative intent. *See In re Kaiser Steel Corp.*, 952 F.2d at 1239 ("As the appellees and the SEC have urged, there is no reason to narrow the plain concept of 'settlement' to a single type of securities transaction. The Code has been expanded to explicitly cover five different types of financial transactions, all of which, with the exception of swap agreements, involve 'settlement payments' of one form or another. In fact, the definition of 'settlement payment' found in § 741(8) also applies to payments made in connection with a repurchase agreement, which is not a 'trade' entered into on an exchange, and which involves a completely different settlement process.") (footnote omitted); *In re Comark*, 971 F.2d at 326 (applying Section 546(e) to the "settlement" of a withdrawal from a broken repo transaction).

Moreover, even some of Enron's cited authorities describe the mechanics of securities transactions in terms that apply to this case and make clear that transfer of ownership is not the sine qua non of settlement. For example, the court in *Hill v. Spencer Savings & Loan* said that settlement means the "[c]onclusion of a securities transaction when a customer pays a broker/dealer for securities purchased or ***delivers*** securities sold and receives from the broker the proceeds of the sale." 94 B.R. 817, 829 (D.N.J. 1989) (emphasis added) (cited in Enron Br. 30). *See also* Jeff Stehm, *Clearance and Settlement Systems for Securities: Critical Design Choices in Emerging Market Economies*, World Bank Discussion Paper 321, at 9 (1996) ("Settlement involves the discharge of settlement obligations through the final transfer of securities from the seller to the buyer, and the final transfer of funds from the buyer to the seller.").[10] Likewise, the dictionary

[10] Some of the deposition testimony also illustrates the point that market participants do not understand "settlement" with reference to the U.C.C. For example, a Goldman Sachs commercial paper trader testified that the transactions here resulted in "normal commercial paper settlement transaction[s]," because "The issuer got paper back. The investor got their money." Joint Appendix at 2228. Whether the issuer obtained legal ownership of that paper apparently was irrelevant to his understanding.

That testimony is consistent with other sources. *See Bevill, Bresler*, 878 F.2d at 752 ("a 'settlement payment' may be the deposit of cash by the purchaser or ***the deposit or transfer*** of the securities by the dealer") (emphasis added); Group of Thirty, *Clearance and Settlement Systems in the World's Securities Markets* 86 (1989) (defining "settlement" as "[t]he completion of a transaction, wherein securities and corresponding funds are ***delivered and credited*** to the appropriate accounts") (emphasis added) (quoted in *Kaiser Steel*, 913 F.2d at 949); *Nat. Secs. Clearing Corp.*, Order Granting Registration, 42 FED. REG. 14 (Jan. 21, 1977) at 3920 n. 56 ("Obligations generated by the accounting function are satisfied through the settlement process by the ***delivery and receipt*** of funds and securities.") (emphasis added).

definitions cited on pages 28 and 29 of Enron's brief all describe the exchange of cash for the "transfer[ of] securities or financial instruments." None of these definitions suggests that, if the buyer of the security also happens to be the issuer and does not obtain ownership in some formalistic sense, then the transfer would no longer be a "settlement."

Thus, other courts have applied the safe harbor to the repurchase of securities by the debtor-issuer, without regard to whether the debtor obtained ownership or merely extinguished the obligation. In a highly instructive opinion, the Tenth Circuit held that Section 546(e) applies to transfers of stock in leveraged buyouts. *In re Kaiser Steel*, 913 F.2d at 849–50. The court considered, and rejected, the debtor's argument that the "the LBO was not a securities transaction" because the shares ceased to exist in their prior form. *Id.* at 850 n.8. The court reasoned that "[a] technical change in how Kaiser regarded the[ shares] after the merger should not obscure the more sensible interpretation of the transaction: that the owners of Kaiser Steel sold their common stock for cash and preferred stock." *Id.* The court concluded that

> What occurred in this case was "the delivery and receipt of funds and securities." The LBO was a securities transaction. The transfer of money and preferred stock was the settlement of that transaction. Therefore, the transfers to Schwab were exempt from avoidance under section 546(e) as "settlement payment[s] . . . to a . . . stockbroker."

*Id.* at 850 (citation and footnote omitted and alteration and ellipses in original).

The Third Circuit reached the same conclusion in *Lowenschuss,* where it dismissed the argument that the safe harbor did not apply because "the system of intermediaries and guarantees" was not implicated in an LBO, the same argument that Enron makes here (Br. 36–38). 181 F.3d 505, 515 (3d Cir. 1999). *See also In re The IT Group*, 359 B.R. 97 (Bankr. D. Del. 2006) (applying safe harbor to acquisition by debtor of the stock of its own subsidiary, which was privately traded and did not clear through a clearinghouse).

2. Congress's failure to mention retirement of debt is a reason to include such transactions, not to exclude them.

Particularly worrisome is Enron's assertion that, because the definition of "settlement payment" in Section 741(8) "does not address the retirement-of-debt-issue," the definition may implicitly carve out such payments. Br. 24. To the contrary, it is because the statutory definition does ***not*** include any of the exceptions that Enron advocates here that those exceptions should not be read in. *See NLRB v. Bildisco*, 465 U.S. 513, 522–23 (1983) ("Obviously, Congress knew how to draft an exclusion for collective-bargaining agreements when it wanted to; its failure to do so in this instance indicates that Congress intended that § 365(a) apply to all collective-bargaining agreements covered by the NLRA."). Reluctance to do so is especially appropriate in light of the statute's function: A harbor filled with hidden mines is not a safe one. If investors had to hire lawyers and expert witnesses first to opine on, and then, inevitably, to litigate over whether the payments they received in exchange for securities qualify for protection under Section 546(e), or whether the transaction might be characterized as not "common" in some respect, the purpose of the safe harbor—certainty—would be destroyed. Thus, in *Kaiser Steel*, though the Tenth Circuit agreed that "[n]either LBOs nor other exceptional transactions were even mentioned in the legislative history," it concluded that "because of the variety and scope of different securities transactions, and the ***absence*** of any restrictions in sections 546(e) and 741(8), it would be an act of judicial legislation to establish such a limitation." *In re Kaiser Steel*, 913 F.2d at 850 (emphasis added).

3. The District Court's decision draws the line in the right place.

While Enron argues that the decision below renders the safe harbor overbroad, it admits that that decision excludes from the safe harbor (1) all payments on "debts that are not evidenced by a note and [2] payments that are not made to or from a financial institution, stockbroker, clearinghouse, etc." Br. 34. That is exactly the result that Congress intended. All other payments—on debt that goes through financial intermediaries—***do*** implicate systemic risk and so are subject to Section 546(e). As explained in the House Report on the 2006 amendments to Section 546(e) (discussed further below),

> [t]he common thread of these transactions [covered by the safe harbors] is that they involve financial intermediaries—stockbrokers, financial institutions, financial participants or securities clearing agencies—that often hedge their risk on these transactions through other market

> transactions, repledge securities collateral received under these transactions, or both. As such these transactions implicate the systemic risk concerns that are addressed by the safe harbors.

H.R. REP. 109–648, at *4 (2006).

Enron cites a series of cases (Br. 32–33) in which courts have allowed debtors to avoid prepayments of debt. By contrast with the transactions here, however, all of those cases involved non-tradable bank loans, the repayments of which were never "settled" in any sense of the word. *See Union Bank v. Wolas*, 502 U.S. 151 (1991); *Ray v. City Bank & Trust Co.*, 899 F.2d 1490, 1493 (6th Cir. 1990); *Breeden v. L.I. Bridge Fund, LLC*, 220 B.R. 739, 741–42 (B.A.P. 2d Cir. 1998); *CEPA Consulting, Ltd. v. N.Y. Nat. Bank*, 187 B.R. 105, 107–09 (S.D.N.Y. 1995). Accordingly, they did not implicate the concerns over systemic risk that motivated the settlement-payment safe harbor.

### C. Enron's attempt to exclude all DTC-cleared trades would gravely undermine the safe harbor.

Having first engrafted onto Section 546(e) a "transfer of ownership" requirement, Enron next draws the remarkable—and dangerous—conclusion that the section does not even protect ***all clearinghouses***. Rather, Enron argues, Section 546(e) was designed to protect only certain clearinghouses, like the National Securities Clearing Corporation, and that securities exchanged through DTC are not eligible for the safe harbor. Br. 36–37. Enron even goes so far as to imply that DTC is not a clearinghouse at all. It asserts that

> [u]nlike DTC's bookkeeping process for handling commercial paper, clearance involves novation and transfer of ownership of the security, first to the NSCC, then to the counterparty. In this novation process, the clearing agency acts as a central counterparty, acquiring temporary ownership of the security before selling it to another party.

Br. 36.

In fact, however, the SEC recognizes DTC as a "registered clearing agency" under Section 17A of the Securities Exchange Act of 1934 (15 U.S.C. § 78q-1). *See Dexter v. Depository Trust & Clearing Corp.*, 406 F. Supp. 2d 260, 264 (S.D.N.Y. 2005), *aff'd*, 219 Fed. App'x 91 (2d Cir. 2007); *Capece v. The Depository Trust & Clearing Corp.*, No. 05-80498 CIV RYSKAMP, 2005 WL 4050118, at *1 (S.D. Fla. Oct. 11, 2005) ("Defendants are the nation's principal institutions for the clearing and settlement of securities transactions and for the provision of securities depository services. DTC and NSCC, both New York corporations, are wholly owned subsidiaries of DTCC, a New York holding company, and are SEC-registered clearing agencies."). And for purposes of the Bankruptcy Code, "securities clearing agency" is defined to mean any "person that is registered as a clearing agency under section 17A of the Securities Exchange Act of 1934." 11 U.S.C. § 101(48).[11]

[11] Ironically, Enron relies on Section 17A in its attempt to characterize the "national clearance and settlement system" as excluding any clearinghouse that uses a book-entry system. Br. 30.

Acceptance of Enron's position would have wide-ranging consequences. As the Federal Reserve has explained, the Depository Trust & Clearing Corporation (the parent of DTC) is "a national clearinghouse for the settlement of securities trades and a custodian for securities. ***DTCC performs these functions for almost all activity in the domestic CP [commercial paper] market.***" Federal Reserve Board, *Federal Reserve Release: About Commercial Paper* (emphasis added).[12] Thus, while Enron purports to target only repurchases by issuers of commercial paper, it divines a legislative intent that would exclude virtually ***all*** transactions in commercial paper from the safe harbor.[13]

The text of the statute does not justify such a disruptive result. Nothing in the definition of "settlement payment" purports to be limited to particular clearinghouses or clearing systems.[14] As importantly, concerns over finality and

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[12] *Available at* www.federalreserve.gov/Releases/cp/about.htm. *See also* Issues & Recommendations at 9 ("Through its subsidiaries, DTCC provides clearance, settlement and information services for virtually all equity, corporate debt, municipal debt, government securities, mortgage-backed securities, and emerging market sovereign debt trades in the U.S., totaling more than $1.7 trillion daily.").

[13] It is unclear what Enron means by its assertion that "[t]he District Court's statement that the commercial paper redemptions 'were consummated using the standard clearing mechanism for transactions in commercial paper' is erroneous." Br. 37. As noted in the text, almost all commercial paper is traded through DTC.

[14] Enron's reference to dividends, interest, maturity payments, service fees, and other non-settlement payments that are "processed through DTC" (Br. 38) is a red herring. SIFMA does not contend that mere "utilization of DTC" makes anything a settlement payment. Rather, SIFMA's position is that a payment made in

systemic risk are implicated with the same force by the unwinding of commercial paper transactions settled through DTC as they would be if the subject of the transaction were a share of stock cleared through NSCC. Enron's assertion that DTC's clearing method avoids risk to itself and its member banks (Br. 36–37 (citing redacted testimony)) is simply wrong. As DTC and the Bond Market Association observed in a joint white paper, even the procedure for "reclamation" of erroneous completed orders for commercial paper, on either the same or the next business day, risks "impair[ing] the finality of settlement and prolong[ing] the period during which delivering participants and the depository are at risk." Issues & Recommendations, *supra*, at 17.

More generally, the Southern District of New York explained in *In re Adler, Coleman Clearing Corp.* that

> In § 546(e), Congress recognized that the ***unwinding of settled securities transactions*** could create an environment hostile to capital formation, engendering diminished investor confidence, as well as increased costs and volatility of transactions in capital markets. To that end, strong policy reasons favor a statutory reading of settlement payments that protects participants in the securities markets and promotes ***finality of securities transactions***, as a counterbalance to safeguarding the interests of creditors.

263 B.R. at 479 (emphasis added). It is hard to understand how the finality interest identified in *Adler, Coleman* could hinge on whether the security was transferred to

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connection with the tender of a security is a settlement payment, regardless of what clearinghouse or clearing system is used, if any.

its issuer, rather than to a third party; on whether the transferee obtained ownership of the security; or on how the transfer occurred. And it does not: the harmful, market-chilling "ripple effect" arises from the loss ***by the non-debtor recipient*** of a settlement payment that is later clawed back, after that same party has given up its securities.

Other courts have agreed that the method of clearing is irrelevant to the definition of "settlement payment." In *In re Olympic Natural Gas Co.*, the Fifth Circuit addressed a bankruptcy trustee's argument that "off-exchange sales transactions between private parties should not be exempt from avoidance [under Section 546(e)], as they are not conducted on an exchange, and do not impact the financial derivatives market." 294 F.3d 737, 742 n.5 (5th Cir. 2002). Noting the same legislative history discussed in this brief, the court rejected that position, concluding that "it seems clear that Congress meant to exclude from the stay and avoidance provisions both on-market, and the corresponding off-market, transactions." *Id.* The court also "reject[ed] the Trustee's argument that in order to be exempt from avoidance, a 'settlement payment' must be made on a financial derivative contract, and be cleared or settled through a centralized system." *Id.* at 742.

Similarly, in *Lowenschuss*, the Third Circuit held that "[a]lthough no clearing agency was involved in this transfer, two financial institutions—Merrill Lynch and

Chase—were. Under a literal reading of section 546, therefore, this was a settlement payment 'made by . . . a financial institution.'" 181 F.3d at 515. The court also noted that some of the trades at issue in *Kaiser Steel* involved payments outside the formal clearing system. *Id.* at 516. And the Sixth and Eighth Circuits have held that the safe harbor extends to uncleared privately-held securities. *See In re QSI Holdings, Inc.*, 571 F.3d 545, 550 (6th Cir. 2009) ("The value of the privately held securities at issue is substantial and there is no reason to think that unwinding that settlement would have any less of an impact on financial markets than publicly traded securities."), *cert. denied*, 130 S. Ct. 1131 (2010); *Contemporary Indus. Corp. v. Frost*, 564 F.3d 981, 987–88 (8th Cir. 2009) (same); *see also In re Plassein Int'l Corp.*, 388 B.R. 46, 49 (D. Del. 2006) ("the Court finds nothing in the *Resorts* case or any other Third Circuit case law supporting the Trustee's contention that the term should be limited to publicly traded securities"), *aff'd*, 590 F.3d 252 (3d Cir. 2009), *cert. denied sub nom. Brandt v. B.A. Capital Co.*, 130 S. Ct. 2389 (2010). Given the importance of certainty and clarity in this area of the law, we submit that this Court should be especially careful before creating a conflict with its sister circuits on this issue.

## III. The 2006 amendments confirm Congress's intent to include repayments of commercial paper in the safe harbor.

The 2006 amendments to Section 546(e) provide further confirmation that Congress did not intend safe harbor protection to hinge on the clearing method or on whether a transfer of ownership occurs under the U.C.C. In 2006, Congress expanded Section 546(e) to cover not only margin payments and settlement payments but also any payment:

> that is a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in section 761(4), or forward contract

PUB. L. 109-390, § 5(b)(1)(B). Had the prior language had the constricted meaning that Enron advocates, this amendment would have been a radical change. The new catch-all goes beyond any specific class of payment to include all payments that implicate systemic concerns: a payment qualifies as long as it is made to any financial intermediary and is "in connection with a securities contract," regardless of whether it satisfies some abstruse definition of "securities transaction" or relates to a transaction that is cleared through any clearinghouse.

In fact, however, the legislative history confirms that the 2006 amendments were only "technical changes" that were designed to "update the language to reflect current market and regulatory practices" and to "clarify[] the treatment of certain financial products," not to expand substantive reach of the safe harbor. H.R. REP. 109-648, at 1. The House Report also points out that the amendment merely "conforms the language of Sections 546(e) and (f)" to the treatment already accorded swap agreements under Section 546(g). *Id.* at 8. Because swaps, as noted above, are not cleared through a central clearinghouse, Congress's desire to make the settlement-payment safe harbor work in the same manner as the equivalent section governing swap payments indicates that both sections have a broader reach than the one that Enron urges. The Supreme Court has explained that "[w]hen several acts of Congress are passed, touching the same subject matter, subsequent legislation may be considered to assist in the interpretation of prior language on the same subject." *Tiger v. W. Inv. Co.*, 221 U.S. 286, 309 (1911); *Red Lion Broad. Co. v. FCC*, 395 U.S. 367, 380-81 (1969) ("Subsequent legislation declaring the intent of a prior statute is entitled to great weight in statutory construction."). The amendments here confirm the intended broad reach of Section 546(e).

In summary, Enron has overextended its arguments through the course of this litigation until they fall on their own weight. Enron would strip the entire debt securities markets and all DTC-cleared trades of safe harbor protection. As these are unacceptable results, so too was the decision of the Bankruptcy Court, which was properly reversed below.

## **CONCLUSION**

For all of the foregoing reasons, this Court should affirm the decision of the District Court.

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## CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Federal Rule of Appellate Procedure 32(a)(7)(B) because: this brief contains 6,352 words, excluding the parts of the brief exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Federal Rule of Appellate Procedure 32(a)(5) and the type style requirements of Federal Rule of Appellate Procedure 32(a)(6) because this brief has been prepared in a proportionally-spaced typeface using Microsoft Word 2007 in 14-point Times New Roman.

## CERTIFICATE OF SERVICE

I, Christopher J. Houpt, a member of the Bar of this Court, hereby certify that on Friday, August 20, 2010, I caused to be served upon each counsel of record via first-class mail and email to:

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