IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
BRUNSWICK DIVISION

IN RE:	:	
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DURANGO-GEORGIA PAPER CO.;	:	Case No. 02-21669-JSD
DURANGO-GEORGIA CONVERTING CORPORATION; and	:	Chapter 11
DURANGO-GEORGIA CONVERTING, LLC,	:	Jointly Administered
	:	
Debtors.	:	
	:	
Durango-Georgia Paper Company, Durango-Georgia Converting Corporation, and Durango-Georgia Converting, LLC,	:	
	:	Adversary No. 15-02009
Plaintiffs,	:	
	:	
v.	:	
	:	
Pension Benefit Guaranty Corporation,	:	
	:	
Defendant.	:	
	:	

MOTION TO DISMISS

PBGC hereby moves to dismiss the Debtor's Complaint (the "Complaint") for equitable subordination of PBGC's claims. The Complaint fails to state a claim upon which relief can be granted under Bankruptcy Rule 7012(b) and Rule 12(b)(6) of the Federal Rules of Civil Procedure because the conduct complained of — PBGC's exercising its admitted discretion to decline to bring an enforcement action — is not

inequitable. In addition, it is clear that PBGC's enforcement decisions are not reviewable in the courts. Accordingly, the Complaint should be dismissed.

A. Standard of review

A complaint should be dismissed for failure to state a claim under Rule 12(b)(6) where it appears that the facts alleged fail to state a plausible claim for relief.[1] The court must accept as true all facts alleged in the complaint and construe all reasonable inferences in the light most favorable to the plaintiff.[2] The court, however, need not accept the complaint's legal conclusions as true, only its well-pled facts.[3] A complaint is plausible "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged."[4] Plausibility requires something more than "a sheer possibility that a defendant has acted unlawfully."[5] "Factual allegations must be enough to raise a right to relief above the speculative level."[6]

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[1] *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009).

[2] *See Hoffman–Pugh v. Ramsey*, 312 F.3d 1222, 1225 (11th Cir.2002).

[3] *Iqbal*, 556 U.S. at 678.

[4] *Id.* (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 554, 556 (2007)).

[5] *Id.*

[6] *Twombly*, 550 U.S. at 555.

Under the foregoing standards, the allegations of the Complaint are plainly insufficient to state a claim for equitable subordination. The conduct alleged in the Complaint is not inequitable at all, but is simply PBGC's lawful exercise of its enforcement discretion under Title IV of ERISA,[7] a point that the Complaint concedes.[8] As PBGC explains below, this exercise of enforcement discretion does not constitute inequitable conduct for purposes of section 510(c) of the Bankruptcy Code. In addition, PBGC's discretionary decisions about whether to bring an action to enforce the provisions of Title IV of ERISA are not reviewable in the courts.

B. Inequitable Conduct

The remedy of equitable subordination is set forth in section 510 of the Bankruptcy Code, which states that "the court may[,] under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim . . . ."[9] Courts have held that "principles of equitable subordination" in the foregoing provision refers to "relevant case law."[10] The purpose of

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[7] ERISA is the Employee Retirement Income Security Act of 1974, Title IV of which is codified as amended at 29 U.S.C. §§ 1301-1461. PBGC's authority to bring civil actions under ERISA is set forth at 29 U.S.C. § 1303(e)(1).

[8] *See* Complaint ¶ 72.

[9] 11 U.S.C. § 510(c).

[10] *In re Structurlite Plastics*, 193 B.R. 451, 463 (Bankr. S.D. Ohio 1995).

equitable subordination is to adjust the rights of creditors, relative to one another, when one of them has engaged in inequitable conduct and, as a consequence, should not share in the estate ratably with creditors who were harmed by the inequitable conduct.[11]

The legal standard for establishing equitable subordination — often called the *Mobile Steel* test — requires that the following three circumstances be shown:

1. The claimant must have engaged in some type of inequitable conduct;

2. The misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant; and

3. Equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy [Code].[12]

The first of these criteria is crucial; "[w]ithout a showing of inequitable conduct, the remaining two prongs of the test are not applicable and the Court cannot subordinate the claim."[13]

Further, the application of this standard depends on whether the creditor is an insider or a non-insider. As the Eleventh Circuit explained,

> [w]here the claimant is an insider or a fiduciary, the trustee bears the burden of presenting material evidence of unfair conduct . . . . If the

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[11] *See In re Enron Corp.*, 333 B.R. 205, 218 (Bankr. S.D.N.Y. 2005) ("The purpose of section 510(c) of the Bankruptcy Code is to correct inequitable conduct and ensure no creditor gain an unfair advantage in the distribution of the estate.").

[12] *In re Mobile Steel Co.*, 563 F.2d 692, 699-700 (5th Cir. 1977).

[13] *In re Graycarr, Inc.*, 330 B.R. 741, 749 (Bankr. W.D. Ark. 2005) (citing *In re Lifschultz Fast Freight*, 132 F.3d 339, 344 (7th Cir. 1997)).

> claimant is not an insider or fiduciary, however, the trustee must prove more egregious conduct such as fraud, spoliation or overreaching, and prove it with particularity.[14]

In this case, there is no allegation in the Complaint that PBGC is an insider, nor could there be. The Complaint correctly identifies PBGC as a United States government corporation.[15] PBGC had no control over the Debtors' business. PBGC did not sit on the Debtors' Creditors Committee and did not otherwise have a corporate relationship to any of the Debtors that would make it an "insider" for purposes of equitable subordination.[16] Accordingly, to satisfy the first prong of the *Mobile Steel* test, the Plaintiffs here must allege and prove that PBGC committed gross misconduct tantamount to "fraud, overreaching or spoliation."[17]

The Complaint completely fails on this point; it does not allege the sort of egregious misconduct that would support a prayer for equitable subordination of PBGC's

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[14] *Estes v. N&D Properties, Inc.* (*In re N&D Properties, Inc.*), 799 F.2d 726, 731 (11th Cir. 1986); *see also First Nat'l Bank of Barnesville v. Rafoth* (*In re Baker & Getty Fin. Servs. Inc.*), 974 F.2d 712, 718 (6th Cir. 1992) (quoting In re Teltronics Serv., Inc., 29 B.R. 139, 169 (Bankr. E.D.N.Y. 1983)).

[15] Complaint ¶ 7. *See* 5 U.S.C. § 103.

[16] Neither does the relative size of PBGC's claims cause it to be an insider, absent some indication that PBGC used this factor to control the Debtors. "[T]o find control, the court must find an opportunity by the defendant to self-deal or exert more control than is available to other unsecured creditors. Mere financial power does not amount to control over the debtor, as this is simply an incident of the debtor-creditor relationship." *In re Sullivan has Coyle, Inc.*, 208 B.R. 239, 243 (Bankr. N.D. Ga. 1997) (citing *In re UVAS Farming Corp.*, 89 B.R. 889, 892 (Bankr. D.N.M. 1988)).

[17] *N&D Properties*, 799 F.2d at 731.

claims. It does not, in fact, allege any misconduct at all. The Complaint admits that PBGC has discretion whether to bring actions under 29 U.S.C. § 1369(a).[18] Discretion is defined as "the freedom or authority to make decisions and choices."[19] The Complaint therefore admits that PBGC had the freedom to bring, or not bring, an action under 29 U.S.C. § 1369(a). This conclusion is confirmed by the permissive language of the provision that empowers PBGC to bring civil actions, which states that "[c]ivil actions *may* be brought by [PBGC] for appropriate relief, legal or equitable or both, to enforce . . . the provisions of this title . . . ."[20]

Notwithstanding its admission that PBGC had discretion whether to bring suit, the Complaint alleges that PBGC's misconduct was its "failure to exercise [its] discretion" in a particular way. This allegation is absurd. As noted above, to have discretion is to have the freedom to choose. Nothing in ERISA or the Bankruptcy Code requires that PBGC exercise its discretion in a particular way. PBGC submits that, as a matter of law, PBGC's exercise of its admitted discretion to bring, or not bring, an action under Title IV of ERISA cannot be deemed "inequitable conduct."

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[18] Complaint ¶ 72.

[19] *Webster's New World Dictionary* 392 (3d College ed. 1988). *See also Black's Law Dictionary*: 466 (6th ed. 1990) ("When applied to public functionaries, discretion means a power or right conferred upon them by law of acting officially in certain circumstances, according to the dictates of their own judgment and conscience, uncontrolled by the judgment or conscience of others").

[20] 29 U.S.C. § 1303(e)(1).

An examination of equitable subordination cases in the Eleventh Circuit involving non-insiders readily confirms that the conduct alleged here — PBGC's discretionary act of declining to bring an action under Title IV of ERISA — has nothing in common with the sort of egregious or fraudulent conduct that is required to support a claim for equitable subordination. For example, in *In re Sayman's,*[21] one of the debtor's utility providers disconnected the debtor's telephone service in violation of the automatic stay under 11 U.S.C. § 362 and in apparent disregard of a deposit that had been provided toward post-petition telephone service. The utility disconnection caused direct harm to the operations of the Debtor. On these facts, the Court concluded that the telephone company's claims should not share in the distribution "on a parity with other unsecured creditors of th[e] estate."[22]

In another case in the Northern District of Georgia, a non-insider claimant falsely alleged that he was the sole owner of certain proprietary technology that was actually owned by the debtor, and actively communicated this information to third parties. Because of these misrepresentations, a potential purchaser withdrew its letter of intent to purchase the technology from the debtor, causing harm to the estate and its creditors.[23]

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[21] *See In re Sayman's, Inc.*, 15 B.R. 229, 230 (Bankr. N.D. Ga. 1981).

[22] *Id.*

[23] *In re Apyron Techs., Inc.*, No. ADV 04-6443, 2005 WL 6485938, at *4 (Bankr. N.D. Ga. Sept. 13, 2005). The Court also awarded the Debtor the costs of litigating the adversary proceeding. *Id.* Such an award in PBGC's favor would be appropriate in this case.

The Court found this conduct sufficiently injurious to the debtor to warrant equitable subordination.[24]

In contrast, when the non-insider creditor in question has *not* engaged in "egregious conduct such as fraud, spoliation, or overreaching,"[25] courts reject pleas for equitable subordination of the creditor's claim. In one case, the Resolution Trust Corporation ("RTC") was a successor in interest to a creditor who had agreed not to enforce a certain lien beyond $150,000.[26] The RTC enforced the lien without the restriction that its predecessor agreed to, because federal law rendered the restriction unenforceable.[27] Another creditor complained that RTC's claim should be equitably subordinated because it was inequitable for the RTC not to abide by the lien restriction. But the Court rejected the plea for equitable subordination. "The fact that the terms of the [lien restriction] are unenforceable by operation of law against Great Southern's successor in interest, RTC, pursuant to 12 U.S.C. § 1823(c), does not support equitable subordination of RTC's claim under 11 U.S.C. § 510(c)."[28] Here, too, the supposedly

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[24] *Id.*

[25] *N&D Properties*, 799 F.2d at 731.

[26] *In re Van Puffelen*, No. 90-41092, 1992 WL 12004359 (Bankr. S.D. Ga. Mar. 31, 1992), *aff'd sub nom. Muller v. RTC*, 148 B.R. 650 (S.D. Ga. 1992), *aff'd*, 7 F.3d 241 (11th Cir. 1993).

[27] *See* 12 U.S.C. § 1823(e).

[28] *Van Puffelen*, 1992 WL 12004359, at *7

inequitable conduct of PBGC, like that of RTC, is actually a lawful exercise of the agency's authority and discretion — in this case, the authority and discretion to bring suit under 29 U.S.C. § 1303. Nothing in ERISA or the Bankruptcy Code compels PBGC to take particular action, and its decision not to act cannot be deemed inequitable for purposes of 11 U.S.C. § 510(c).

C. Unreviewability

It is also clear that a federal agency's enforcement decisions are presumptively unreviewable. The Supreme Court explained this principle in *Heckler v. Chaney*[29] and the Ninth Circuit recently affirmed it with respect to PBGC's investigative and enforcement decisions in *Paulsen v. CNF Inc.*[30]

In *Chaney*, the respondents, who were convicted of capital offenses and sentenced to death, challenged the use of certain drugs for lethal injections on the ground that such use had not been approved by the federal Food and Drug Administration ("FDA"). They claimed that under the Food, Drug, and Cosmetic Act,[31] the FDA was required to approve the drugs as "safe and effective" for human execution before the drugs could be used in

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[29] 470 U.S. 821 (1985).

[30] 559 F.3d 1061 (9th Cir. 2009).

[31] 21 U.S.C. §§ 301 *et seq.*

interstate commerce. Accordingly, they requested that the FDA "fulfill its statutory function" by taking various investigative and enforcement actions.[32]

The Supreme Court began by examining the provisions of the Administrative Procedure Act ("APA") relating to review of agency action.[33] It observed that "before any review at all may be had, a party must first clear the hurdle of [5 U.S.C.] § 701(a)," which states that judicial review of agency action is available "except to the extent that — (1) statutes preclude judicial review; or (2) agency action is committed to agency discretion by law."[34] It concluded that an agency's decision not to prosecute or enforce, whether through civil or criminal process, is a decision generally committed to an agency's discretion.[35] That conclusion is attributable to the general unsuitability for judicial review of agency decisions not to pursue enforcement.

> The reasons for this general unsuitability are many. First, an agency decision not to enforce often involves a complicated balancing of a number of factors which are peculiarly within its expertise. Thus the agency must not only assess whether a violation has occurred, but whether agency resources are best spent on this violation or another, whether the agency is likely to succeed if it acts, whether the particular enforcement action requested best fits the agency's overall policies, and, indeed, whether the agency has enough resources to undertake the action at all. An agency generally cannot act against each technical violation with the statute it is charged with enforcing.

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[32] 470 U.S. at 823-24.

[33] *See* 5 U.S.C. §§ 701-706.

[34] 470 U.S. at 828.

[35] *Id.* at 831.

> The agency is far better equipped than the courts to deal with the many variables involved in the proper ordering of its priorities. Similar concerns animate the principles of administrative law that courts generally will defer to an agency's construction of the statute it is charged with implementing, and to the procedures it adopts of implementing that statute.[36]

Chaney controls the reviewability of PBGC's conduct in this case. As noted above, the language of ERISA that governs PBGC's institution of civil actions to enforce the liability provisions of the statute broadly states that "civil actions *may* be brought" by PBGC,[37] and does not otherwise limit PBGC's discretion or require PBGC to act. Even the scope of PBGC's investigations under ERISA is stated in the broadest possible terms: PBGC "may make such investigations as it deems necessary to enforce any provision" of Title IV of ERISA.[38] Thus, the statute is "drawn so that a court would have no meaningful standard against which to judge the agency's exercise of discretion. In such a case, the statute ('law') can be taken to have 'committed' the decisionmaking to the agency's judgment absolutely."[39]

A recent case in the Ninth Circuit specifically applied the principles of *Chaney* to the PBGC's investigative and enforcement decisions. In *Paulsen v. CNF Inc.*,[40] the

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[36] *Id.* at 831-32.

[37] 29 U.S.C. § 1303(e)(1).

[38] 29 U.S.C. § 1303(a).

[39] *Chaney*, 470 U.S. at 830 (quoting 5 U.S.C. § 701(a)(2)).

[40] 559 F.3d 1061 (9th Cir. 2009)

plaintiffs challenged PBGC's discretionary decision not to pursue claims against the former fiduciaries and actuary of a terminated pension plan.[41] The court reviewed *Chaney* and its progeny, noting that the presumption of unreviewability obtains where "statutes are drawn in such broad terms that in a given case there is no law to apply."[42] "The concern is that courts should not intrude upon an agency's prerogative to pick and choose its priorities, and allocate its resources accordingly, by demanding that an agency prosecute or enforce."[43]

The *Paulsen* court allowed that the presumption of unreviewability could be rebutted when the statute has provided guidelines for the agency to follow in exercising its enforcement powers. However, upon examining the relevant provisions of ERISA, the Court found a "lack of standards by which a court may review PBGC's decision not to sue," and concluded that Title IV of ERISA did not provide any such guidelines. "Nothing in ERISA expressly compels PBGC to pursue claims on the terminated plan's behalf."[44] As in *Chaney*, the Court was mindful of the litany of considerations that

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[41] Because the plaintiffs in *Paulsen* urged PBGC to bring suit on behalf of the terminated plan against its former fiduciaries, the relevant provision of ERISA was 29 U.S.C. § 1342(d)(1)(B), which states that the trustee of a terminated plan "has the power . . . to commence, prosecute, or defend on behalf of the plan any suit or proceeding involving the plan."

[42] *Id.* at 1085 (quoting *Chaney*, 470 U.S. at 830).

[43] *Id.* (quoting *Port of Seattle, Wash. v. FERC*, 499 F.3d 1016, 1027 (9th Cir. 2007)).

[44] *Id.* at 1086.

inform PBGC's decision whether to file lawsuits, including its assessment of the alleged violations of ERISA, its perceived likelihood of success, and its allocation of agency resources.[45] The Court also noted that PBGC has a broad set of agency purposes, "not all of which conclusively favor suing each time it has an arguable claim."[46] "Taken together, PBGC must balance its statutory duties to all stakeholders, including premium payers, participants and beneficiaries in ongoing plans, and those in all of its terminated plans."[47] With those considerations in mind, the *Paulsen* court held that PBGC's decision not to bring claims against the pension plan's former fiduciaries "is immune from judicial review" and accordingly upheld the district court's dismissal of the claim based on PBGC's declining to prosecute.[48]

The Court in this case should adhere to the principles that were set forth in *Chaney* and applied to the PBGC in *Paulsen*. The relevant provision of ERISA in this case, 29 U.S.C. § 1303(e)(1), is broad and permissive, and does not compel the PBGC to file suit in the situation described in the Complaint. Indeed, the Complaint concedes that PBGC has discretion not to do so. Further, no other provision of ERISA provides guidelines for PBGC to follow in determining whether to bring an action. Accordingly, this Court

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[45] *Id.* at 1086.

[46] *Id.* See 29 U.S.C. § 1302(a)(1)-(3), which sets forth PBGC's statutory purposes.

[47] *Id.* at 1086-87.

[48] *Id.* at 1087.

should hold that PBGC's decision not to pursue the dubious "evade or avoid" action that is the subject of the Complaint is not subject to judicial review.

Conclusion

For the foregoing reasons, the Court should grant PBGC's motion and dismiss Plaintiffs' Complaint with prejudice.

Date: July 24, 2015

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