MULTIPLE CLAIMS, *IVANHOE* AND SUBSTANTIVE CONSOLIDATION

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The Supreme Court's 1935 Ivanhoe *decision created the specter of undue multiplication of claims, particularly in bankruptcies that involve large business enterprises conducted through many separate legal entities.* Ivanhoe *should be overruled on its own facts, but even if it is not, its extension to other situations is indefensible. Until overruled*, Ivanhoe *is properly limited to creditors secured by nondebtor collateral, foreclosure of which does not give rise to reimbursement or subrogation claims against the bankruptcy estate. While even in that case* Ivanhoe *overcompensates the creditor, such cases are rare and do not entail large-scale multiplication of claims against bankruptcy estates. If* Ivanhoe *is so limited, co-debtor liability among insolvent estates can be dealt with through a form of marshaling described in this Article. Otherwise, the practical second-best solution to the multiple claims problem is likely to remain liberal reliance on the substantive consolidation doctrine.*

INTRODUCTION

After languishing in relative obscurity for many years, the counterintuitive holding of *Ivanhoe Building & Loan Ass'n v. Orr*,[1] is receiving greater notice in

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[1] (*Ivanhoe*), 295 U.S. 243, 244–45, 247 (1935). In *Ivanhoe*, the bankruptcy debtor, Eastern Sash & Door Company, assumed the obligation of a note and mortgage on certain land it acquired and immediately reconveyed subject to the mortgage to Yavne, who subsequently defaulted. The mortgagee, Ivanhoe, foreclosed, purchasing the property at the foreclosure sale for $100, and then presented a claim against Eastern's bankruptcy estate for $10,739.94, the amount due on the note less the $100 bid at the sale. The parties stipulated that the property acquired in foreclosure was worth $9,000. The bankruptcy court reduced Ivanhoe's claim against Eastern to the difference—$1,739.94—and the Third Circuit affirmed. Ivanhoe Building & Loan Ass'n v. Orr, 73 F.2d 609 (3d Cir. 1934) *rev'd*, 295 U.S. 243 (1935). As summarized in the text *infra* at notes 5–6, the Supreme Court reversed, holding that Ivanhoe could continue to assert its claim of $10,739.94 against Eastern without taking into account the value of the property it had already obtained from Yavne in respect of the same obligation, subject however to the limitation that in no event could

bankruptcy law circles, perhaps due to its prominent treatment in Professor Kenneth Klee's BANKRUPTCY AND THE SUPREME COURT[2] and the Fourth Circuit's reliance on its holding in the *NEGT* case.[3] *Ivanhoe*'s holding disproportionately overcompensates creditors with limited recourse against nondebtor collateral or nondebtor guarantors. Worse, extending *Ivanhoe* to apply in cases of nondebtor co-obligors and guarantors with rights of contribution, reimbursement or subrogation further depletes the bankruptcy estate by multiplying claims. Worst of all (and least well understood) is that *Ivanhoe*, if extended to debtor co-obligors, provides a powerful incentive to substantively consolidate bankruptcy estates whose separateness could and should otherwise be respected. Unnecessary resort to substantive consolidation has broad systemic implications.[4] This Article suggests that only the first of these adverse consequences (the least important) is actually mandated by *Ivanhoe*, and that by properly limiting the case the more serious harms implied by its extension can be readily avoided. There is no need to allow multiplication of claims against bankruptcy estates, or to remedy that entirely avoidable problem through substantive consolidation.

DISCUSSION

Ivanhoe is a brief unanimous opinion authored by Justice Owen Roberts for the Nine Old Men.[5] It held that notwithstanding a creditor's prior foreclosure and sale

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Ivanhoe collect more than $10,739.94 from all sources in respect of the obligation of the note and mortgage. 295 U.S. at 244–45, 247.

[2] *Ivanhoe* ranks No. 2 on Professor Klee's list of "Old Favorites." KENNETH N. KLEE, BANKRUPTCY AND THE SUPREME COURT 281, 286, 455–57 (Lexis-Nexis 2008).

[3] Nat'l Energy & Gas Transmission, Inc. v. Liberty Elec. Power, LLC (*In re* Nat'l Energy & Gas Transmission, Inc.) (*NEGT*), 492 F.3d 297, 301 (4th Cir. 2007) (applying *Ivanhoe*). *NEGT* is discussed in Martin J. Bienenstock, *Recent Developments Affecting Chapter 11 Cases*, 916 PRAC. L. INSTI. COMM. L. & PRAC. HANDBOOK SERIES 539, 561–67 (2009) (analyzing *NEGT* and its implications), and Hon. Nancy Dreher, *Fourth Circuit Rules Creditor Cannot Allocate First to Interest*, BANKR. SERV. CURRENT AWARENESS ALERT 7 (Sept. 2007) at 7, *available at* 2007 (No. 9) BSV-BCA 7 (Westlaw) (discussing *NEGT*). *See also* Reconstr. Fin. Corp. v. Denver & Rio Grande W. R.R. Co., 328 U.S. 495, 528 (1946) (invoking *Ivanhoe* to assert "[t]he rule is settled in bankruptcy proceedings that a creditor secured by the property of others need not deduct the value of that collateral or its proceeds in proving his debt."); *In re* Emergency Beacon Corp., 48 B.R. 341, 352 (S.D.N.Y. 1985) ("[I]t is settled law that a creditor, secured by property of a third party, may assert the full amount of its claim against the debtor's estate without deduction for the security."); *In re* Sacred Heart Hosp., 182 B.R. 413, 417, 418 n.3 (Bankr. E.D. Pa. 1995) (under *Ivanhoe* creditor may assert its entire claim against debtor notwithstanding existence of third party collateral or guarantees so long as creditor recovers only single satisfaction from all sources); *In re* F.W.D.C., Inc., 158 B.R. 523, 527–28 (Bankr. S.D. Fla. 1993) (treating *Ivanhoe* as controlling law).

[4] *See infra* notes 29–35 and accompanying text.

[5] *See supra* note 1. The genesis of the phrase "nine old men" to describe the Supreme Court of the United States is obscure. In the 1930s, however, as the constitutionality of the New Deal's vast assertions of federal power dominated the national political and legal agenda, Drew Pearson and Robert Allen popularized the phrase in the gossipy pro-New Deal column *Washington Merry-Go-Round* they wrote for the *Washington*

of third-party collateral, that creditor is entitled to assert the full amount of its claim against the bankrupt (not merely the deficiency remaining after the application of the proceeds of the foreclosure to the debt) subject only to the limitation that the creditor not receive more than 100% of its claim from all sources (the "single satisfaction" limitation).[6] It is a troubling decision,[7] as the hypothetical cases below illustrate:

Post and subsequently in their book THE NINE OLD MEN. *See* DREW PEARSON & ROBERT S. ALLEN, THE NINE OLD MEN (Doubleday, Doran & Co. 1937); *see also* William E. Leuchtenburg, *The Origins of Franklin D. Roosevelt's "Court-Packing" Plan*, 1966 SUP. CT. REV. 347, 390 (1966) (noting A.A. Berle used phrase "nine old men" to refer to Supreme Court in his 1933 article *Law and the Social Revolution* in SURVEY GRAPHIC, a popular sociological and political research publication, but Pearson and Allen made it a "household word"). Joining Justice Roberts in *Ivanhoe* were Chief Justice Hughes and Justices Van Devanter, McReynolds, Brandeis, Sutherland, Butler, Stone and Cardozo—the Court that is forever identified as "the nine old men." Of course, far more momentous matters than *Ivanhoe* were on the Court's mind in the spring of 1935. Two weeks before the *Ivanhoe* decision was announced, the Court granted certiorari in A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935). Argument was heard in that matter on May 2-3, 1935, and on May 27, 1935 the Court subsequently declared the National Industrial Recovery Act, a centerpiece of the early New Deal, unconstitutional. *Id*. at 541–42. *Schechter* had been foreshadowed a few months before in *Panama Refining Co. v. Ryan*, 293 U.S. 388, 414–21, 433 (1935) (finding section 9(c) of the National Industrial Recovery Act unconstitutional). Also decided by the Court on February 18, 1935 were the intensely controversial *Gold Clause Cases*. Perry v. United States, 294 U.S. 330 (1935); Nortz v. United States, 294 U.S. 317 (1935); Norman v. Balt. & Ohio R.R. Co., 294 U.S. 240 (1935) (consolidated for review with United States v. Bankers Trust Co.); *see also* Kenneth W. Dam, *From the Gold Clause Cases to the Gold Commission: A Half Century of American Monetary Law*, 50 U. CHI. L. REV. 504, 514–16 (1983) (discussing *Gold Clause Cases*).

[6] *Ivanhoe*, 295 U.S. at 245–46; *see also* St. Louis Sw. Ry. Co. v. Henwood, 157 F.2d 337, 406 (8th Cir. 1946) ("[W]here a creditor of a bankrupt has recovered a portion of his debt from security not owned by bankrupt, he may prove his claim in bankruptcy for the full amount of the debt (without such deduction) but . . . he may not collect and retain dividends which would make his total payment more than the amount of his debt."); Bank Comm'rs v. Sec. Trust Co., 49 A. 113, 116 (N.H. 1901) (noting single satisfaction qualification under pre-*Ivanhoe* chancery rule).

[7] *Ivanhoe* is grounded on the ancient "chancery rule," which, subject to the single satisfaction qualification, generally privileged secured creditors to assert their claims independently of their mortgage. Originally, the "chancery rule" applied even with respect to secured claims against the bankrupt itself, privileging the secured creditor to collect dividends on its full claim, and keep its security too, so long as it did not receive more than 100 cents on the dollar. Merrill v. Nat'l Bank of Jacksonville, 173 U.S. 131, 162 (1899) (noting chancery rule allows "a mortgage creditor . . . possess[ing] the contract right to assert his whole claim … without regard to his mortgage security"). The "chancery rule" was abandoned in England in the 19th century, *see* English Judicature Act of 1873 § 10; *Bank Comm'rs*, 49 A. at 117 ("[A]fter the chancery rule had been adopted … the bankruptcy rule was substituted by Acts of Parliament."); Note, *Proof of Claim in Bankruptcy by Creditor Holding Security on Property Transferred by Bankrupt to Third Party*, 45 YALE L.J. 531, 531 n.4 (1936) (noting chancery rule continued to be law of England until Judicature Act), and, at least as to claims secured by the property of bankruptcy estates, was superseded in the United States in the Bankruptcy Act of 1898 which adopted the so-called "bankruptcy rule," *see* Bankruptcy Act of 1898, ch. 541 §§ 1(23), 59(e), 30 Stat. 560 (repealed 1979); *see also* 11 U.S.C. § 506(a) (2006) (bifurcating secured claims and limiting the undersecured creditor's resulting unsecured claim to the amount of its deficiency). *Ivanhoe* constitutes a narrow judicially-imposed limitation on the scope of the "bankruptcy rule." *See Ivanhoe*, 295 U.S. at 245–46. Early American cases applying the "chancery rule" include *Merrill*, 173 U.S. at 138, 162–64, and *Chem. Nat'l Bank v. Armstrong,* 59 F. 372, 381–82 (6th Cir. 1893). *Swarts v. Fourth Nat. Bank of St. Louis*, 117 F. 1, 12 (8th Cir. 1902), is a prominent pre-*Ivanhoe* application of the "chancery

Case 1 (Unsecured claim): Assume that Creditor (C) is owed $100 and the bankruptcy estate pays dividends of forty cents on the dollar on account of unsecured claims. The estate will distribute $40 to C who is out $60.

Case 2 (Unsecured claim supported by full nondebtor guarantee): Same facts as Case 1 otherwise, but now assume C has full recourse to solvent Guarantor (G). C collects $100 from G who in turn may assert a general unsecured claim for reimbursement or subrogation against the bankruptcy estate for $100.[8] The bankruptcy estate will be out $40, G is out $60, and C will be paid in full.

Case 3 (Unsecured claim supported by partial nondebtor guarantee): Same facts as Case 2 otherwise, but now assume that C has

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rule" in the context of a non-debtor guarantor. *See also In re* N.Y. Commercial Co., 233 F. 906, 909–10 (2d Cir. 1916); Young v. Gordon (*In re* Foster Motor Car Co.), 219 F. 168, 171 (4th Cir. 1914); Mark v. Am. Brick Mfg., 84 A. 887, 888 (Del. Ch. 1912) ("The established rule in chancery . . . is that a creditor with collateral shall have the right to prove and receive payment on his full claim . . . without deducting from such claims the amount collected by him from his collateral, provided . . . that in no event shall such secured creditor receive more than his full debt."). In addition to the bankruptcy rule and the traditional chancery rule various local hybrids also co-existed. *See Merrill*, 173 U.S. at 135–37; Annotation, *Treatment of Collateral Held by Creditor of Insolvent or Bankrupt*, 94 A.L.R. 468 (1935) (setting out various alternative rules and authorities). The operative statutes today regarding the allowance and disallowance of claims, like those in force at the time of *Ivanhoe*, do not expressly address the issue of accounting for the existence of non-debtor collateral or non-debtor recourse, and, accordingly, the issue of whether the "chancery rule" or "bankruptcy rule" or some variant thereof should apply in this situation remains a matter of statutory interpretation for which the text of the Bankruptcy Code itself supplies no clear answer.

Ivanhoe has long been subject to sharp criticism as "seem[ing] to be unjust," 1 COLLIER ON BANKRUPTCY, ¶ 1.28, at 130.25 n.13 (James W. Moore et al. eds., 14th ed. 1977), having "little justification" and resulting in a "windfall to the creditor" with "deplorable" consequences for the estate. 3 COLLIER ON BANKRUPTCY, ¶ 57.07, at 164–66 (James W. Moore et al. eds., 14th ed. 1977). As the Bankruptcy Reform Act of 1978 was being considered, Professor Darrell Dunham forcefully, but futilely, urged *Ivanhoe*'s legislative overruling. Darrell Dunham, *Creditors' Claims in Bankruptcy: A Plea for Complete Adoption of the Bankruptcy Rule*, 52 AM. BANKR. L.J. 299, 319 (1978) ("[*Ivanhoe*] only preserves the theoretical rights of the assured creditor, which he never uses, . . . tramples on the indemnification rights of the surety . . . [and] has created insoluble problems where co-debtors are involved . . . [while] [a]pplication of the bankruptcy rule to the assured creditor is an effective solution to these problems while treating all creditors fairly"). *See also* Ralph E. Clark, *Proof by Secured Creditors in Insolvency and Receivership Proceedings*, 15 ILL. L. REV. 171, 176–77 (1921) (critiquing"chancery rule"); Note, *Bankruptcy—Amount for Which Creditor May Prove After Foreclosure of Mortgage on Property Not of the Bankrupt*, 35 COLUM. L. REV. 1129, 1130 (1935) (observing *Ivanhoe* will "lead to an inequitable result"); Note, Bankruptcy—*Definition of Secured Creditor*, 21 IOWA L. REV. 145, 146 (1936) (*Ivanhoe* "seriously prejudice[s] the interests of unsecured creditors"); Note, *Bankruptcy: Rights of Secured Creditors to Dividend Upon the Full Amount of Their Claims*, 19 CAL. L. REV. 638, 640 (1931) (noting bankruptcy rule "more equitable and consistent"); Note, *Proof of Claim in Bankruptcy by Creditor Holding Security on Property Transferred by Bankrupt to Third Party*, 45 YALE L.J. 531, 533 (1936) (*Ivanhoe*'s result is "unfortunate"). *But see* D. W. Markham, *Bankruptcy—Rights of Partially Secured Creditors*, 14 N.C. L. REV. 79, 80 (1936) (*Ivanhoe* "illustrates the Court's long-maintained preference . . . [that] the Court will . . . apply [the chancery] rule, even in bankruptcy cases, whenever it is not bound by strict statutory language").

[8] 11 U.S.C. §§ 502(a), (e), 509 (2006).

> only limited recourse against G for $60 under the terms of its guaranty. Assuming *Ivanhoe* applies in this scenario notwithstanding the existence of subrogation and reimbursement rights in favor of G, the estate pays $40 to C, and C may obtain the $60 balance from G either before or after receiving its dividend from the estate. When G pays C $60, G's $60 claim for reimbursement, indemnity or subrogation against the bankruptcy estate becomes fixed. C is paid in full (even though only the insolvent bankruptcy estate, which is paying claims at a forty percent rate, not solvent G, was on the hook for the last $40), G receives $24 on account of its $60 unsecured reimbursement claim, and, somehow, the bankruptcy estate is now out $64.

Oddly, if C bargains for no recourse to G (Case 1), or full recourse to G (Case 2), only $40 is distributed from the estate, but if C has limited recourse (Case 3), claims multiply, and the estate's liability expands to $64. Meanwhile, in Case 3, C, which only held a partial guarantee, nevertheless receives full satisfaction of the $40 shortfall, a shortfall that constitutes an unsecured claim against the insolvent estate only, and not a claim against G, because of the contractual cap on G's guarantee.

Now to be fair to the Nine Old Men, *Ivanhoe* itself did not involve a nondebtor guarantor with subrogation or reimbursement rights.[9] In *Ivanhoe*, the nondebtor had acquired property from the debtor subject to a mortgage and was therefore primarily liable to mortgagee on a nonrecourse basis to the extent of its interest in the transferred property.[10] The debtor was also liable based on its prior assumption of the debt, but the nondebtor transferee had no right of reimbursement or subrogation against the debtor following the nondebtor's default on the mortgage and the subsequent foreclosure. The problem of multiplication of claims arises in Case 3 because G timely asserts an allowable claim for reimbursement or subrogation. In *Ivanhoe*, however, multiple claims were not presented to the estate and the estate's liability was limited to a pro rata distribution on account of a single unsecured claim, albeit one not reduced by the prior collection from nondebtor sources. One can certainly quarrel with the Supreme Court's disposition of *Ivanhoe*: Why should the debtor face an unsecured claim greater than the amount of the deficiency after the mortgagee has foreclosed on its collateral?[11] Nevertheless, not reducing the claim against the estate to account for collections is not the same as authorizing the

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[9] *Ivanhoe*, 295 U.S. at 244.
[10] *Id.*
[11] *See supra* note 7 (citing contemporaneous criticism of *Ivanhoe*).

multiplication of claims.[12] In Case 3, if rights of reimbursement or subrogation are non-existent, disallowed, or unasserted, the "windfall" to C, arguably, comes at the countervailing expense of G and the result, arguably, is neutral to the estate. Moreover, as between G and C, the risk of the primary obligor's insolvency is properly assigned to G—that's what it means to be a guarantor. Note that (again assuming no reimbursement or subrogation), if we reverse the order of distribution with C first collecting $40 from the estate and only thereafter collecting on the limited guarantee or pledge from G, the same result is obtained: C is made whole, G is out $60 and the estate is out $40.[13]

These distributive effects do not depend on the dividend rate, even if increases or decreases in the rate implicate the cap on G's liability or the single satisfaction rule. If the pro rata dividend is reduced to ten cents on the dollar, $10 is distributed out of the bankruptcy estate to C, G pays C $60 (its maximum liability) and C is left with a $30 loss, having mitigated what would have otherwise been a $90 loss but for the existence of the capped $60 guarantee. If the dividend rate is increased to seventy cents, the single satisfaction qualification in *Ivanhoe* comes into play and C's dividend from the estate is limited to $40, assuming C has previously collected $60 from G. There is a windfall to the estate in that circumstance (it gets away with distributing only $40 on a $100 liability even though by hypothesis it is a seventy-cent case) but that windfall arises from the failure to assert or recognize G's reimbursement claim. If contingent rights of reimbursement or subrogation do not exist (*e.g.* the *Ivanhoe* facts) or are disallowed or unasserted, *Ivanhoe* may provide a tolerable shortcut to the proper apportionment of liability between (i) a solvent nondebtor against whom there is limited recourse, and (ii) the bankruptcy estate. Given the prevailing pre-Code view that rights of reimbursement and indemnity against the debtor in bankruptcy were not allowable,[14] *Ivanhoe*, at the time

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[12] Indeed this Article argues that *Ivanhoe* (properly read) does not authorize multiplication of claims, and that, in no event more than a pro rata distribution on account of a single claim is appropriate. *See infra* notes 35–36 and accompanying text.

[13] Disregarding reimbursement or subrogation rights, the transfer subject-to a mortgage, the naked pledge of third-party collateral to support an obligation of the debtor, and a nonrecourse secured guarantee all generally fit within this analysis, although at least as a formal matter, the transferor rather than the transferee in a subject-to transaction is the primary obligor and not a guarantor. *See* D. Benjamin Beard, *The Restatement of Suretyship: Suretyship on the Fringe—Suretyship by Operation of Law and by Analogy*, 34 WM. & MARY L. REV. 1157, 1173–77 (1993). Note that some courts permit separate classification of unsecured claims in chapter 11 plans based on the claimant's recourse against nondebtor collateral. *See, e.g.*, Steelcase Inc. v. Johnston (*In re* Johnston), 21 F.3d 323, 328 (9th Cir. 1994) (approving separate classification).

[14] Bankruptcy Act of 1898, ch. 541 § 57i, 30 Stat. 560 (repealed 1978) and Bankruptcy Rule 304 (repealed 1979) (restating General Order 21(40) (vacated 1973)) were construed to preclude sureties from asserting claims against the bankruptcy estate by way of reimbursement and indemnity, and, moreover, limited the rights of sureties to dividends under the law of subrogation until payment in full of the assured creditor to avoid multiplication of claims. The operation of these pre-Code rules is discussed at length in 3 COLLIER ON BANKRUPTCY, ¶ 57.21[1], at 365–72 (James William Moore et al. eds., 14th ed. 1977) (concluding "section 57i and Rule 304 should be understood to constitute nothing but a technical procedural

it was decided, did not unduly threaten to multiply claims against the bankruptcy estate.

But that is not the world we live in today. The Bankruptcy Code only disallows *contingent* rights of reimbursement, and plainly authorizes a limited recourse guarantor to fix its liability through payment and in turn assert rights of reimbursement and subrogation.[15] *NEGT* illustrates the point:

> **Case 4** *(NEGT)***:** GTN was a solvent subsidiary of NEGT that had guaranteed up to $140 million of principal and interest of NEGT's liability[16] under NEGT's tolling agreement with Liberty. Liberty was owed $140 million in principal and subsequently accrued $17 million in post-bankruptcy interest on that claim under the terms of the tolling agreement. The interest portion was not allowable against NEGT under bankruptcy law,[17] but did constitute a valid claim against GTN. So Liberty claimed (i) $157 million in principal and interest; (ii) the right to collect $140 million in principal

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device to secure a single charge against the estate on what is for all practical intents and purposes a single debt . . . perhaps [resulting in] the legal paradox of a provable debt that may not be proved in its own right"). *See* Phoenix Indem. Co. v. Earle, 218 F.2d 645, 650 (9th Cir. 1955) (asserting that section 57i "which permits a surety to be subrogated to the rights of creditors to the extent that he pays the creditors" did not support appellant's argument that tax liens take priority over other creditors); United States v. Burke (*In re* Miller), 105 F.2d 926, 929 (2d Cir. 1939) (stating section 57i gives protection to surety who must prove creditor's claim, not his own, by allowing subrogation); *see also* Max Nathan, Jr. & F.A. Little, *The Surety of a Bankrupt: His Status in the Bankruptcy Proceedings*, 38 TUL. L. REV. 649, 650–52 (1964) (discussing section 57i's relation with section 63(a)(8) and procedural protections provided for surety under section 57i).

[15] *See* 11 U.S.C. § 502(e) (2006) ("[T]he court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that—(B) such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution; . . . A claim for reimbursement or contribution of such an entity that becomes fixed after the commencement of the case shall be determined, and shall be allowed under subsection (a), (b), or (c) of this section, or disallowed under subsection (d) of this section, the same as if such claim had become fixed before the date of the filing of the petition."); 11 U.S.C. § 509(a) (2006) ("[A]n entity that is liable with the debtor on, or that has secured, a claim of a creditor against the debtor, and that pays such claim, is subrogated to the rights of such creditor to the extent of such payment."); 11 U.S.C. § 509(c) (subordinating subrogation and reimbursement claims to claims of primary obligee until primary obligation satisfied in full).

[16] *NEGT*, 492 F.3d 297, 297 (4th Cir. 2007). Actually, the primary obligor on the Liberty Tolling Agreement in *NEGT* was PG&E Energy Trading Holdings Corp. (ET) an insolvent affiliate of NEGT whose own chapter 11 case was consolidated with that of NEGT. NEGT was secondarily liable on its own guarantee of the ET-Liberty Tolling Agreement. For the sake of clarity in exposition, the discussion in the text follows the Fourth Circuit in eliding any distinction between ET and NEGT. *See id.* at 299 & n.1 (describing consolidation of cases). For the same reason, the stylized hypothetical facts stated in Case 4, also otherwise differ somewhat from those of *NEGT* itself.

[17] 11 U.S.C. § 502(b)(2) disallows Liberty's claim for unmatured interest. The only exceptions to the general no-post-bankruptcy-interest rule are that a secured creditor may accrue post-petition interest to the extent of the value of the collateral securing its claim, 11 U.S.C. § 506(b), and the unusual case of a solvent bankruptcy estate. 11 U.S.C. §§ 726(a)(5), 1129(a)(7) (2006).

> and interest and from nonbankrupt GTN; and (iii) the right to collect $140 million (in principal only) from bankrupt NEGT. Liberty collected $140 million from GTN (GTN's maximum liability under its guarantee) and applied the collections to interest first which, in Liberty's view, left $17 million in principal unpaid. Liberty then sought to collect this last $17 million from NEGT arguing that under *Ivanhoe* it was entitled to a full satisfaction of the principal and could assert the entire $140 million principal amount of its claim against NEGT under the tolling agreement until it received dividends satisfying in full the remaining $17 million in unpaid principal. The Fourth Circuit majority purported to follow *Ivanhoe,* but nevertheless disallowed Liberty's claim against NEGT on the basis that Liberty was effectively seeking to collect disallowed post-petition interest from NEGT however artfully it attempted to disguise the fact.

As the *NEGT* dissent points out, the Fourth Circuit majority gave no plausible legal authority for disregarding (as between GTN and Liberty) an application of proceeds principle that appears to be consistent with those nondebtor parties' agreement and otherwise applicable nonbankruptcy law.[18] Even if post-bankruptcy interest is disallowed against a bankrupt primary obligor, a guarantor is liable to the assured party for such interest in accordance with the terms of its guarantee. Accordingly, I suggest that *NEGT* inappropriately let nonbankrupt GTN off the hook for post-bankruptcy interest even though it was a solvent nonbankrupt guarantor.

The benefit to GTN becomes apparent when one considers what would have happened had NEGT first discharged its liability as primary obligor to Liberty before GTN honored its guarantee. Assume NEGT pays a dividend of sixty cents on the dollar to general unsecured creditors and that NEGT therefore distributes $84 million to Liberty on account of its $140 million unsecured claim. This leaves Liberty with a remaining claim of $56 million in principal and $17 million in interest against GTN. The $73 million in principal and interest owing is within the $140 million cap on the GTN guarantee, and GTN would have had to pay it. But if GTN reverses the order of collection, and liquidates its claim for reimbursement or subrogation against NEGT by promptly paying out $140 million to Liberty, somehow, magically, GTN limits its net liability to $56 million ($140 million paid out less $84 million received as a dividend on its reimbursement claim from NEGT) and Liberty, somehow, magically, loses its right to collect $17 million in interest guaranteed by GTN.

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[18] *NEGT*, 492 F.3d at 304–05 (Duncan, J., dissenting); *see also* Bienenstock, *supra* note 3, at 561–67 (critiquing *NEGT* majority opinion).

The theoretically sound answer to the *NEGT* problem is to treat the reimbursement claim and the primary obligation as one (they are obviously of a piece since the whole point of the guarantee cum reimbursement right is to properly allocate the liability for the primary obligation between primary obligor and guarantor) and have NEGT discharge its liability for both by distributing a final bankruptcy dividend of $84 million while leaving GTN responsible for the rest of the liability in accordance with nonbankruptcy law. If GTN has already paid out $140 million, then $67 million of that $84 million should go to GTN as reimbursement and the rest to Liberty. If GTN hasn't yet made good on its guarantee then all $84 million should go to Liberty and Liberty should be free to collect from GTN the $73 million balance due (an amount within the $140 million cap) in accordance with the terms of its guarantee. NEGT's bankruptcy should limit NEGT's liability on account of this GTN-guaranteed tolling agreement to one pro rata payment on the allowable amount of $140 million, and should leave GTN where it stands under nonbankruptcy law vis-à-vis Liberty.[19] The analysis is the same whether the bankruptcy dividend is sixty cents on the dollar or some other number, though of course on a net basis GTN can never be liable for more than $140 million under the terms of its guarantee, and the claim against NEGT cannot exceed $140 million so long as it is insolvent under the no-post-bankruptcy-interest rule. Thus, if unsecured claims against NEGT were paid at the rate of ten cents on the dollar, the pro rata distribution of $14 million from NEGT should go to Liberty, Liberty should collect $140 million from GTN and Liberty's remaining interest claim of $3 million would be uncollectible.

More problematic than the Fourth Circuit's creative extension of the no-post-bankruptcy-interest rule in *NEGT* is that but for that creativity, following *Ivanhoe*, and applying the reimbursement claim allowance rule of section 502(e), GTN would receive $84 million on account of its $140 million reimbursement claim, and Liberty would be entitled to obtain payment in full from NEGT on a $17 million deficiency claim for a grand total of $101 million on account of a $140 million unsecured claim in a sixty cent case. That cannot be right. Facing this prospect under its understanding of the *Ivanhoe* rule, the Fourth Circuit chose to deny Liberty its right to collect interest from GTN, allowing GTN to apparently evade its

[19] 11 U.S.C. § 524(e) (2006) ("[D]ischarge of a debt of debtor does not affect liability of any other entity on, or property of any other entity for, such debt."); *see, e.g.*, Highland Capital Mgmt. v. Chesapeake Energy Corp. (*In re* Seven Seas Petroleum, Inc.), 522 F.3d 575, 590 (5th Cir. 2008) (holding bankruptcy does not alter liability of third party for damages caused to estate and unsecured creditors.); *cf.* Airadigm Commc'ns, Inc. v. FCC (*In re* Airadigm Commc'ns, Inc.), 519 F.3d 640, 656 (7th Cir. 2008) (explaining under section 524 "a creditor can still seek to collect a debt from a co-debtor who did not participate in the reorganization—even if that debt was discharged as to the debtor in the plan").

contractual liability for such interest, but thereby preventing the parties from mulcting the *NEGT* estate for an additional $17 million.[20]

NEGT, like *Ivanhoe*, is an oddity. It would be nice to get the right result in these cases, but the failure to do so does not threaten the system as a whole. Multiplication of liability on account of the existence of partial recourse from solvent nondebtor parties is a relatively minor issue. Indeed, in the absence of an allowable nondebtor reimbursement or subrogation claim, multiplication of liability would not occur, as it did not occur in *Ivanhoe* itself. Moreover, the Bankruptcy Code viewed as a whole appears to both contemplate and mitigate the problem by disallowing claims for reimbursement, contribution and subrogation unless timely fixed.[21]

But *Ivanhoe* does have implications that are more broadly troubling. While *Ivanhoe* does not directly involve the assertion of multiple claims, its logic can be extended first to the limited recourse guarantor hypothetical in which multiplication does occur, and then further extended to other forms of co-liability and finally to co-liability among related insolvent debtors. It is this last extension that creates large-scale problems.[22] Allowing the assertion of multiple claims against related insolvent estates implies collection of double or triple (or more, depending on the number of co-liable entities) dividends from related insolvent estates. *Ivanhoe*, read (unreasonably) at its broadest, authorizes assertion of unsecured claims against the debtor not reduced by the collection of proceeds from any non-debtor sources, even related insolvent estates. Large firms typically conduct their affairs through multiple subsidiaries and affiliates each of whom may be co-liable on at least some of each others' debts. Under this reading of *Ivanhoe*, the effect of that co-liability is that the same $100 claim can be asserted against and receive pro rata dividends from multiple entities. Under common law joint and several liability principles each co-obligor's liability is independent of each other's until the judgment is satisfied in full and the claimant may proceed in any order it chooses.[23]

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[20] *NEGT*, 492 F.3d at 303 ("[T]he purpose of § 502(b)(2) is best served by barring Liberty's collection of an additional $17 million from the estate.").

[21] *See* 11 U.S.C. § 502(e)(1)(B) (stating courts must disallow contingent reimbursement or contribution claims); 11 U.S.C. § 509 (2006) (limiting or subordinating subrogation claims in certain circumstances); c*f. supra* note 14 (discussing pre-Code law).

[22] Problems arising from application of the chancery rule to insolvent co-debtors have been discussed by commentators for over a century. *See* Dunham, *supra* note 7, at 310 ("[E]state may shoulder an unfair burden of the creditor's debt depending on which estate first paid a dividend."); *see also* James Barr Ames, *Proof in Bankruptcy on Joint Obligations*, 5 HARV. L. REV. 406, 406 (1892).

[23] Over the last twenty years or so, traditional joint and several liability rules have been limited in many jurisdictions. *See* RESTATEMENT (THIRD) OF TORTS: APPORTIONMENT OF LIABILITY § 17 (2000) ("If the independent tortious conduct of two or more persons is a legal cause of an indivisible injury, the law of the applicable jurisdiction determines whether those persons are jointly and severally liable, severally liable, or liable under some hybrid of joint and several and several liability."); Daniel J. Bussel, *Liability for Concurrent Breach of Contract*, 73 WASH. U. L.Q. 97, 110 (1995) (noting that under traditional joint and several

> **Case 5:** Assume MegaCorp Holding, Inc. (Holding), and its wholly owned subsidiaries MegaCorp Operating, Inc. (Operating) and MegaCorp Distributing, Inc. (Distributing), file administratively (but not substantively) consolidated chapter 11 cases. Assume further that trade creditor (or tort creditor or taxing authority) C holds a $100 claim that all three entities are co-liable on. If unsecured claims in the three MegaCorp cases receive 50, 40 and 30 cents on the dollar respectively, it is clear (under the expansive reading of *Ivanhoe* allowing C to assert its full claim against all three entities without crediting collections) that C will be entitled to receive $100 in the aggregate. But it is entirely unclear how much C will receive from each estate. If Holding pays out $50 first and Operating $40 second, then Distributing will only be liable for $10. If the payments are in reverse order, however, Distributing must pay $30, Operating $40 and Holding only $30. The permutations are countless if one takes into account various sequences of partial payments based on interim distributions.

Co-liability of multiple related insolvent entities is a commonplace. What ought to happen in Case 5? A variant of equitable marshaling is appropriate.

Marshaling is an equitable doctrine that constrains an oversecured senior creditor with multiple pools of collateral from exercising its rights to the prejudice of junior lienors.[24] Classically, marshaling applies to creditors of a common debtor with conflicting rights in collateral.[25] Marshaling intervenes in specified circums-

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liability injured plaintiff can recover full damages from each defendant, but plaintiff can receive only one satisfaction of judgment based on account of collections from all defendants); *cf.* Ames, *supra* note 22, at 408 (arguing chancery rule properly maintains common law rights of creditor vis-à-vis joint obligors).

[24] *See, e.g.*, Meyer v. United States, 375 U.S. 233, 246 n.6 (1963) ("The equitable doctrine of marshaling rests upon the principle that a creditor having two funds to satisfy his debt may not, by his application of them to his demand, defeat another creditor, who may resort to only one of the funds." (quoting Sowell v. Fed. Reserve Bank of Dallas, 268 U.S. 449, 456–57 (1925))); *see also* Sav. Bank v. Creswell, 100 U.S. 630, 641 (1879) (marshaling requires one creditor to exhaust fund to which another creditor does not have access, if first creditor has access to two funds, whereas second creditor only holds subsidiary lien on one fund). *But see* Merrill v. Nat'l Bank of Jacksonville, 173 U.S. 131, 138 (1898) ("It is true that, in equity, a creditor having a lien upon two funds may be required to exhaust one of them in aid of creditors who can only resort to the other; but this will not be done when it trenches on the rights or operates to the prejudice of the party entitled to the double fund."). *Merrill* further emphasized that "it is well established that in marshaling assets, as respects creditors, no part of his security can be taken from a secured creditor until he is completely satisfied." *Merrill*, 173 U.S. at 138 (citing 2 WHITE & T. LEAD. CAS. EQ. (4th Am. ed.) pt. 1, pp. 258, 322).

[25] *See, e.g.*, *Creswell*, 100 U.S. at 641 (noting marshaling doctrine applies to creditors with access to same fund from debtor, one of whom has subsidiary lien and other of whom also has access to other funds); *see also In re* Hale, 141 B.R. 225, 226 (Bankr. N.D. Fla. 1992) (applying marshaling doctrine when two or more creditors have access to funds owned by common debtor, and one creditor is senior lienor while other

tances to prevent one of those creditors from exercising its rights in a sequence or manner that unduly prejudices the other creditor. In the bankruptcy context, marshaling principles do not generally constrain a secured creditor from proceeding against collateral in any order it chooses, but do require that it credit collections against the secured obligation.[26]

I suggest that in dealing with affiliated entities in a common enterprise a similar principle ought to constrain a creditor holding the advantage of having numerous related insolvent entities co-liable on a single obligation. Case 5 fits this description. Effectively, each bankruptcy estate represents a separate fund against which the single obligation may be asserted. C should have the flexibility to proceed in any order against its multiple obligors, but not concurrently, and not without crediting collections from any obligor against the remaining liability. C may first assert its claim against the most solvent of the three entities, Holding, and thereby obtain 50 cents on the dollar. In the interest of efficiency, and by analogy to section 502(e), that perhaps is all C should be entitled to unless and until it receives a timely and final distribution from Holding that fixes a deficiency of $50 that C may in turn timely assert against Operating, the next most solvent entity.[27]

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creditor is junior lienor); *In re* Murdock, 134 B.R. 417, 423 (Bankr. D. Mont. 1991) (recognizing conflicting interests between creditors, and ordering senior lienor to satisfy its secured lien first from asset other than fund to which junior lienor was entitled).

[26] Owens-Corning Fiberglas Corp. v. Ctr. Wholesale, Inc. (*In re* Center Wholesale, Inc.) (*Center Wholesale II*), 788 F.2d 541, 544 (9th Cir. 1986) (holding reverse marshaling of assets in favor of bankruptcy trustee could not be used to require senior secured creditor to satisfy its claim out of junior secured party's collateral); Owens-Corning Fiberglas Corp. v. Center Wholesale, Inc. (*In re* Center Wholesale, Inc.) (*Center Wholesale I*), 759 F.2d 1440, 1446–47 (9th Cir. 1985) (denying junior secured creditor's request for marshaling assets because it would lessen amount available for unsecured creditors); *see also In re* Azabu Bldgs. Co., 383 B.R. 738, 748 (Bankr. D. Haw. 2008) (when marshaling claims are made by multiple secured creditors, after senior lien was satisfied, surplus would be allocated to junior secured creditors); *In re* Teresi, 134 B.R. 392, 394–96, 399 (Bankr. E.D. Cal. 1991) (granting relief to secured creditor over marshaling objections of both debtor and junior lienholder); *cf.* Moses Lachman, *Marshaling Assets in Bankruptcy: Recent Innovations in the Doctrine*, 6 CARDOZO L. REV. 671, 671 (1985) (suggesting traditional marshaling doctrine is properly limited to protection of secured creditors).

[27] As noted above, section 502(e) requires that claims for reimbursement, contribution and indemnity be disallowed unless timely fixed. *See supra* note 15. The proposal in the text is to similarly limit the holder of claims against affiliated debtors to asserting one claim at a time and require that the creditor "fix" its deficiency against its first-choice obligor before seeking distributions from the next in line. *See supra* note 24. The Supreme Court considered but did not adopt a marshaling solution at the time it reified the chancery rule. *Merrill*, 173 U.S. at 138; *see also supra* note 24. Professor Dunham has suggested a complex concurrent estimation procedure allocating the liability between two insolvent co-debtors through the formula $T_A = M(f_A)(1 - .5f_B)$ where T_A is the distribution from the first estate, M is the creditor's total claim, f_A is the estimated dividend rate on unsecured claims from the first estate and f_B is the estimated dividend rate on unsecured claims from the second estate. Dunham, *supra* note 7, at 317 n.72. The administrative difficulties in apportioning the liability in this way, however, may outweigh the utility of the apportionment. The effect of this formula in comparison to the marshaling solution described in the text would be to reallocate liability away from the more solvent estates and towards the less solvent estates. *See id.* at 317 (defending apportionment rule). If there is one relatively solvent estate and many grossly insolvent ones, query whether apportionment by this formula accomplishes much other than greatly complicate administration of the

No court has reached that solution, or otherwise determined how liability might be allocated among multiple insolvent estates,[28] and so we are left with *Ivanhoe* which, subject to its no-more-than-a-single-satisfaction qualification, arguably allows the full amount of the debt to be asserted at face value against each co-liable entity even after collection of proceeds from one or another of the entities.

Substantive consolidation has proven to be the saving grace.[29] Invariably, upon a substantive consolidation, multiple claims (and any related intercompany claims

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creditor's claim. Nevertheless, either the apportionment solution or the marshaling solution appear superior to extending *Ivanhoe*'s chancery rule into this context. *See id.* at 318 n.73 (arguing *Ivanhoe* should be overruled and replaced by apportionment rule); *cf. Merrill*, 173 U.S. at 138. Additional complexity arises if one considers rights of contribution among the co-liable affiliated debtors. The short answer, I believe, is that such inter-company claims generally should be disallowed under section 502(e) as contingent or otherwise subordinated to third-party claims. *See* 11 U.S.C. §§ 502(e), 510(c) (2006) & *supra* notes 15 & 26. In the usual case, affiliated debtors confirm a joint plan, or, if there are separate plans, they are confirmed and become effective concurrently. Procedurally, upon the debtors' (or other estate representative's or party in interest's) objection to duplicative claims filed against concurrently administered affiliated estates, the creditor would be required to elect which one of the duplicative claims it wished to pursue and the others would be summarily disallowed. If the only issued raised in the objection were the existence of multiple claims against related estates, prompt allowance of the remaining claim would follow as a matter of course. Other objections asserted against that remaining claim would be adjudicated in the usual way. The claims allowance process, however, generally takes place over an extended period of time post-confirmation and it is at least possible that multiple claims against unconsolidated estates may be determined and allowed sequentially. In the usual case, however, as suggested above, the claimant may well be practically required to elect which of its multiple claims it will pursue, and would not have the ability to assert multiple claims sequentially subject to the marshaling principle suggested here; nor would the related contribution claims be allowable. Even so, the claimant would fare better under the marshaling approach which allows it to assert its claim against the most solvent of the related entities than under a substantive consolidation that would limit it to a single claim against the consolidated whole.

[28] *See* Dunham, *supra* note 7, at 310 & n.48, 311.

[29] Statutory authority for substantive consolidation, to the extent it exists, resides in section 1123(a)(5)(C) and the "all writs" provision of section 105(a). 11 U.S.C. § 105(a) (2006) ("The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]."); 11 U.S.C. § 1123(a)(5)(C) (2006) ("[A reorganization] plan shall . . . provide adequate means for the plan's implementation, such as . . . merger or consolidation of the debtor with one or more persons . . . ."). *But see In re* Owens-Corning, 419 F.3d 195, 208–09 (3d Cir. 2005) (suggesting substantive consolidation not affirmatively authorized by Bankruptcy Code); *In re* Combustion Eng'g, Inc., 391 F.3d 190, 236 (3d Cir. 2004) ("The general grant of equitable power contained in § 105(a) . . . must be exercised within the parameters of the Code itself"). In the case law, the substantive consolidation doctrine is generally traced to Sampsell v. Imperial Paper & Color Corp., 313 U.S. 215, 219–21 (1941). *See In re* NM Holdings Co., 407 B.R. 232, 273–74 (Bankr. E.D. Mich. 2009) (tracing substantive consolidation doctrine *Sampsell*); *see also* Seth D. Amera & Alan Kolod, *Substantive Consolidation: Getting Back To Basics*, 14 AM. BANKR. INST. L. REV. 1, 3 (2006) (remarking *Sampsell* only time Supreme Court has considered substantive consolidation doctrine). The full history of the doctrine is set out at length in Mary Elisabeth Kors, *Altered Egos: Deciphering Substantive Consolidation*, 59 U. PITT. L. REV. 381, 386–97 (1998). *See also* Reider v. FDIC (*In re* Reider), 31 F.3d 1102, 1105–06 (11th Cir. 1994) (tracing history of substantive consolidation). More recently, in a few cases where the parties perceive legal obstacles to substantive consolidation, bankruptcy courts have approved plan settlements providing for "stipulated asset allocation" which may mimic the effects of substantive consolidation. *See, e.g., In re* Am. Home Mortgage Holdings, Inc., Bankr. Case No. 07-11047-CSS (Bankr. D. Del. *filed* Aug. 6, 2007) *discussed in* Dennis J. Connolly, et al., *Current Ap-*

for contribution, reimbursement, and subrogation) are eliminated and C, like all other creditors, may assert only a single claim against the consolidated pool.[30] If upon combining the assets and liabilities of all the entities, the consolidated estate will distribute pro rata dividends of forty cents on the dollar to unsecured claims, then C will receive the same pro rata share as all other general unsecured creditors, to wit $40.

Under the Bankruptcy Code, over the futile resistance of most of the courts of appeals,[31] substantive consolidation has become common in large chapter 11 cases.[32] This practice mitigates untoward multiplication of claims that otherwise might occur under an expansive reading of *Ivanhoe*. Interestingly, however, the effect of

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proaches to Substantive Consolidation: Owens-Corning *Revisited*, *in* 2009 NORTON ANN. SURV. BANKR. LAW, Part I, 27, at nn. 142–45 (William L. Norton ed., 2009); *see also*, Patrick A. Jackson, James L. Patton, Jr. & Sean M. Beach, *The "Stipulated Asset Allocation" Model For A Non-consolidated Liquidating Chapter 11 Plan*, 28 AM. BANKR. INST. J. 54 (Sept. 2009) (explaining stipulated asset allocation model). No plan has yet been confirmed in the *American Home Mortgage Holdings* case. Another interesting variation on the theme occurred in the *Enron* chapter 11 case. The principal debtors in that case, Enron Corporation (Enron) and Enron North America (ENA), were administratively but not substantively consolidated. Creditors whose claims against ENA were guaranteed by Enron (or vice-versa) received a specially calculated recovery based on their status as the holders of multiple claims, to wit 70% of the distribution the claimant would be entitled to in the absence of substantive consolidation plus 30% of the distribution such claimant would be entitled to if the estates were substantively consolidated and the holder's allowed guaranteed claims allowed in one-half their amount. This unique formula represents a heavily negotiated intermediate result between applying *Ivanhoe* to allow assertion of multiple claims and using substantive consolidation to disallow all duplicative claims. This ad hoc compromise significantly simplified administration of one of the most complex chapter 11 cases ever filed. *See Disclosure Statement for Fifth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code* at 341–44, *In re* Enron Corporation, Case No. 01-16034 (AJG) (Dkt. No. 15,303 entered Jan. 9, 2004) (describing compromise relating to holders of multiple claims).

[30] *See* Amera & Kolod, *supra* note 29, at 3 (explaining consolidation pools assets and liabilities of debtors); Kors, *supra* note 29, at 381–85 (noting substantive consolidation consolidated debtor and entities into single estate with single pool of assets); William H. Widen, *Report to The American Bankruptcy Institute: Prevalence of Substantive Consolidation in Large Public Company Bankruptcies from 2000 to 2005*, 16 AM. BANKR. INST. L. REV. 1, 24 (2008) (same).

[31] The Courts of Appeals have generally claimed that substantive consolidation is an extraordinary remedy available only in exceptional circumstances and should be employed "sparingly." *E.g.*, *In re Owens-Corning*, 419 F.3d at 208–09; Alexander v. Compton (*In re* Bonham), 229 F.3d 750, 767 (9th Cir. 2000); *In re* Augie/Restivo Baking Co., 860 F.2d 515, 518 (2d Cir. 1988). *But see* Eastgroup Props. v. S. Motel Assoc., 935 F.2d 245, 248–49 (11th Cir. 1991) (noting modern shift toward allowing substantive consolidation); Auto-Train Corp. v. Midland-Ross Corp. (*In re* Auto-Train Corp.), 810 F.2d 270, 276 (D.C. Cir. 1987) ("[C]ourts may order consolidation by virtue of their general equitable powers.").

[32] *See* Widen, *supra* note 30, at 6, 8 ("[A] majority of large public company bankruptcy cases are substantive consolidation cases"); William H. Widen, *Corporate Form and Substantive Consolidation*, 75 GEO. WASH. L. REV. 237, 252–53 (2007) (finding eleven of largest twenty-one and eight of largest ten bankruptcies between 2000 and 2004 invoked substantive consolidation); *see also* Connolly, et al., *supra* note 29, at 27; Douglas G. Baird, *Substantive Consolidation Today*, 47 B.C. L. REV. 5, 13 (2006) (noting "natural tendency" to employ substantive consolidation in chapter 11 cases); ("Although characterized by the courts as a remedy to be rarely invoked, substantive consolidation and analogous remedies are frequently used . . . .").

substantive consolidation is not only to undo the multiplication of claims caused by *Ivanhoe,* but to also undo any benefit to C of having multiple entities co-liable on its obligation. Substantive consolidation makes it irrelevant that a more solvent debtor is co-liable on C's claim.[33] Moreover, not only is C denied the right to assert that portion of its claim that has been satisfied by another, it is denied the right to separately assert any part of the deficiency. Partial satisfaction by the consolidated whole becomes C's only remedy.[34]

CONCLUSION

The *Ivanhoe* rule does not yield sensible results, certainly not if reimbursement and subrogation claims, whether contingent or fixed, are allowed. Even if we continue to tolerate *Ivanhoe* in the context of partial guarantees from solvent non-debtors, its extension to permit multiplication of liability among related insolvent estates is entirely unwarranted. But using substantive consolidation to correct the problems caused by extending *Ivanhoe* is firing an elephant gun to kill a fly. A substantive consolidation is a general pooling of assets and liabilities that thoroughly reorders the substantive rights of all the parties of all the consolidated entities in derogation of what is likely to have been a carefully constructed corporate structure premised upon principles of separateness and limited liability.[35]

On the other hand, if we consistently consider the multiple claims arising out of a single transaction or obligation to be interdependent and of a piece (as the parties themselves did when entering into the relationship and as the single-satisfaction rule has always recognized in the limiting case) we can get to sensible results.

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[33] Kors, *supra* note 29, at 382 & n.10 (noting substantive consolidation places creditors of all debtors on equal footing, regardless of debtor solvency).

[34] *See* Chem. Bank New York Trust Co. v. Kheel (*In re* Seatrade Corp.), 369 F.2d 845, 847 (2d Cir. 1966) (substantive consolidation may "reach a rough approximation of justice to some rather than deny any to all"); *In re* Comm. Envelope Mfg. Co., No. 76 B 2354, 1977 WL 182366, at *9 (Bankr. S.D.N.Y. Aug. 22, 1977) (holding substantive consolidation may adversely affect some creditors); Kors, *supra* note 29, at 382 n.9 ("[B]ecause every entity is likely to have a different debt-to-asset ratio, consolidation almost invariably redistributes wealth among the creditors of the various entities." (quoting *In re Auto-Train Corp.,* 810 F.2d at 276)).

[35] *See, e.g., In re Owens-Corning*, 419 F.3d at 205 ("Substantive consolidation, a construct of federal common law, emanates from equity. It 'treats separate legal entities as if they were merged into a single survivor left with all the cumulative assets and liabilities (save for inter-entity liabilities, which are erased). The result is that claims of creditors against separate debtors morph to claims against the consolidated survivor.' Consolidation restructures (and thus revalues) rights of creditors and for certain creditors this may result in significantly less recovery." (quoting Genesis Health Ventures, Inc. v. Stapleton (*In re* Genesis Health Ventures, Inc.), 402 F.3d 416, 423 (3d Cir. 2005))); *In re Augie/Restivo Baking Co.*, 860 F.2d at 518 ("[S]ubstantive consolidation 'is no mere instrument of procedural convenience . . . but a measure vitally affecting substantive rights' to 'be used sparingly.'" (quoting Flora Mir Candy Corp. v. R.S. Dickson & Co. (*In re* Flora Mir Candy Corp.), 432 F.2d 1060, 1062 (2d Cir. 1970) and *In re Seatrade Corp.*, 369 F.2d at 847); Kors, *supra* note 29, at 381, 383–84 (arguing substantive consolidation, which pools assets and liabilities, contravenes creditors' expectations under limited liability).

Nothing on the face of the Bankruptcy Code requires that credit for collections from non-estate sources be denied or that creditors should be permitted to assert multiple claims against related insolvent estates for the same liability; the Code will work better if *Ivanhoe* is not applied in this way; and, pressure to substantively consolidate will be reduced.

Even if *Ivanhoe*'s narrow holding survived enactment of the Bankruptcy Code—there's no particular reason to think that it did or didn't as *Ivanhoe* is neither codified nor expressly overruled by the Code nor mentioned in the legislative history—we have seen that the *Ivanhoe* rule fails to apportion liability properly when allowable reimbursement or subrogation claims exist against the estate in respect of a limited recourse guarantee. Applying *Ivanhoe* in that circumstance does not make sense. But worse is extending *Ivanhoe* to Case 5 to permit C to concurrently assert multiple claims at face against related insolvent estates without regard to collections. *Ivanhoe* (if not consigned to oblivion as an anachronism) is properly limited to its facts which involve a limited recourse nondebtor primary obligor with no reimbursement or subrogation claims against the bankruptcy estate. Outside that narrow context, marshaling (as described above)[36] should be required and credit should be given for non-debtor collections on account of multiple related claims, especially if those claims are asserted against related insolvent estates. If *Ivanhoe* is not so limited, substantive consolidation may remain the only practical response, at least until the Supreme Court or the Congress expressly rejects a decision that never made much sense and that causes more mischief now than when decided given the bolstered legal position of the holders of reimbursement and indemnity claims under the Bankruptcy Code and the ever-increasing complexity of the corporate structure of large enterprises.

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[36] *See supra* notes 24–27 and accompanying text.