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Sotomayor Helps Puerto Rico Argue Its Bankruptcy Case.

Before Tuesday, I'd have said that Puerto Rico had no chance to win its legal fight to let its municipalities and utilities declare bankruptcy. That's how the island hopes to resolve its overwhelming debt problems, but the federal bankruptcy code says that it can't.

That's what the U.S. Court of Appeals for the First Circuit held last summer, unanimously. The statute seemed so clear that even Judge Juan Torruella, the appellate court's only Puerto Rican member, concurred in an outraged separate opinion criticizing the federal law.

Then Sonia Sotomayor stepped in. Oral arguments before the Supreme Court rarely change the outcome of a case, yet Tuesday's session may turn out to be the exception. In a fascinating and unusual argument, Justice Sotomayor, who is herself of Puerto Rican descent, spoke by my count an astonishing 45 times. Sotomayor left no doubt that she was speaking as an advocate.

The interpretation of the law she favored would make the system fairer to Puerto Rico, allowing the commonwealth to create its own emergency bankruptcy measures outside federal law. But it depends on a highly doubtful reading of the statute, one that stretches credulity when read into the text. Ideally, Congress will hear what happened at the oral argument and pass one of the reform proposals it's currently considering that would spare the court from having to decide the case.

First, Sotomayor walked Puerto Rico's attorney, Christopher Landau, through his own argument with a precision that exceeded his own. She answered other justices' hostile questions for him, better than he did. Then she dominated Matthew McGill, the lawyer for the creditors of Puerto Rico's electrical utility, who are fighting the bankruptcy bid. In the second half of the argument, the other justices mostly stood by and let her go at him.

Sotomayor's position, borrowed from Landau's creative brief, was that the federal bankruptcy law doesn't mean what the appeals court considered obvious. The law says that Puerto Rico is to be considered a state for purposes of the bankruptcy code, except that, unlike a state, it may not authorize its municipalities (and by extension, its utilities) to resolve debts under Chapter 9 of the code.

According to the interpretation favored by Sotomayor, this provision does indeed mean that Puerto Rico can't use federal bankruptcy law to let its electrical utility go into default. But at the same time, she clearly believes, the same law should be interpreted to allow Puerto Rico to create its own bankruptcy laws, under which it might be able to do just that.

The appeal of this interpretation is that it spares Puerto Rico the indignity of the First Circuit's interpretation. According to that court, Puerto Rico is prohibited from having its own bankruptcy laws, just as the 50 states are prohibited. But uniquely (along with Washington, D.C.), Puerto Rico can't enable municipalities or utilities to enter Chapter 9 bankruptcy.

The drawback of this reading is that by implication it gives Puerto Rico a power that no state has had for many decades - the power to create its own bankruptcy code. It seems extraordinarily

unlikely that Congress really meant to give it that power, and no one has thought it did until now.

What was even more remarkable than Sotomayor's dominance of the argument was the effect it seemed to have on her liberal colleagues. Justice Elena Kagan did something that's rare in an oral argument: She announced that Landau (speaking under Sotomayor's tutelage) had clarified her view. "I think I get what you're saying now, which I didn't when I started," Kagan told Landau. Initially, Kagan had seemed skeptical that Puerto Rico's argument could be made to fit the statutory text. Now she was claiming to see the light.

Later Kagan made the point more explicit. "I came in here thinking your best argument is straight on the text," she told McGill. "But now I have a better understanding of Mr. Landau's interpretation of the text."

Justice Stephen Breyer, who had seemed skeptical of Landau's position, also appeared to change sides, or at least to be considering doing so.

The case, *Puerto Rico v. Franklin California Tax-Free Trust*, will be decided by seven justices, since the late Justice Antonin Scalia hasn't been replaced and Justice Samuel Alito is recused. That means Sotomayor would need four votes to win. Chief Justice John Roberts spoke briefly, expressing skepticism about Puerto Rico's position. Justice Clarence Thomas was silent. So was Justice Anthony Kennedy.

That leaves Justice Ruth Bader Ginsburg, who could conceivably provide a fourth liberal vote in favor of Puerto Rico. She spoke sparingly, but pointedly. When Landau first stood up, she asked him if Puerto Rico would be allowed to let its electrical utility default on its debt, or whether that would violate the provision of the Constitution that says states may not impair the obligation of contracts.

Technically, not all of the Constitution applies to Puerto Rico, and Landau declined to say that Puerto Rico would be barred from a default that abrogated the utility's contractual obligations in its debt contracts. In practice, however, there's little doubt that the contracts clause of the Constitution would indeed apply to Puerto Rico. Ginsburg knows that perfectly well.

That's important. She almost certainly asked her question to signal that allowing Puerto Rico to engage in some sort of emergency default wouldn't actually sink the creditors' real-world claims. This is as close as Ginsburg gets to hinting that she might be prepared to hold for the commonwealth.

The silent participant in this entire unusual argument is Congress, which is considering legislation that would give Puerto Rico some way to restructure its utilities' debts. The liberal justices are telling Congress that if it doesn't help Puerto Rico bail itself out, they may do it themselves.

I'm sure all four liberals hope that Congress was listening. A holding like the one Sotomayor was pushing would be good policy, but would push the envelope of statutory interpretation. Congress should resolve this issue soon, before June, so that a hard case doesn't make questionable law.

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Bloomberg View

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