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BUSINESS RESTRUCTURING REVIEW

U.S. SUPREME COURT BANKRUPTCY ROUNDUP

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SUPREME COURT UNANIMOUSLY STRIKES DOWN 2017 U.S. TRUSTEE FEE HIKE AS UNCONSTITUTIONAL

On June 6, 2022, the U.S. Supreme Court issued a much-awaited decision, *Siegel v. Fitzgerald*, No. 21-441, ___. U.S. ___, 2022 WL 1914098 (U.S. June 6, 2022), holding unconstitutional certain aspects of Congress's 2017 amendment to 28 U.S.C. § 1930(a)(6) (the "2017 Amendment"). The 2017 Amendment dramatically increased the quarterly fees charged by the United States Trustee ("UST") in chapter 11 cases.

The roots of this dispute go back to the creation of the UST program in the U.S. Department of Justice in the mid-1980s. For political reasons, when Congress created the UST, it established the program in only 88 of the 94 judicial districts across the country ("UST districts"). In the six judicial districts in North Carolina and Alabama ("BA districts"), however, Congress continued to allow bankruptcy cases to be administered by Bankruptcy Administrators ("BAs"), which are a department of the Judicial Branch and overseen by the Judicial Conference.

In 2017, Congress sought to address funding problems with the UST program by enacting the 2017 Amendment, which raised the quarterly fees payable by large chapter 11 debtors in UST districts from a maximum of $30,000 per quarter per debtor to a maximum of $250,000 per quarter per debtor—an increase of more than 700%. In UST districts, the 2017 Amendment's fees took effect in both new and pending chapter 11 cases on January 1, 2018. However, in the six BA districts, the fees did not take effect until the Judicial Conference adopted them in September 2018. And even then, the Judicial Conference decided to apply the fees only prospectively for new chapter 11 cases filed after October 1, 2018. As a result, debtors whose cases were filed in a UST district prior to October 1, 2018, were required to pay significantly higher quarterly fees than they would have if their cases were pending in a BA district.

Several debtors in various UST districts who were required to pay the higher fees challenged the 2017 Amendment. Among their arguments was that by making debtors in UST districts pay significantly higher fees than similarly situated debtors in BA districts, the 2017 Amendment violated the Constitution's requirement that bankruptcy laws be geographically uniform throughout the country. The Fourth, Fifth, and Eleventh Circuits rejected

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the debtors' uniformity arguments, but the Second and Tenth Circuits agreed with the debtors and ordered a refund of fees. The Supreme Court granted *certiorari* in *Siegel* to resolve the circuit split.

In a 9–0 decision written by Justice Sotomayor, the Supreme Court determined that the 2017 Amendment violates Congress's constitutional authority under the "Bankruptcy Clause . . . to establish 'uniform Laws on the subject of Bankruptcies throughout the United States.' U. S. Const., Art. I, § 8, cl. 4" because while "[t]he Bankruptcy Clause affords Congress flexibility to 'fashion legislation to resolve geographically isolated problems,' . . . the Clause does not permit Congress to treat identical debtors differently based on an artificial funding distinction that Congress itself created." *Siegel*, 2022 WL 1914098 at *3, *8 (citation omitted).

In reaching this decision, the Court rejected the argument advanced by the UST that the fee increase was not a "law on the subject of Bankruptcies," and instead held (in agreement with all courts to have considered the question) that the 2017 Amendment affects the "'substance of debtor-creditor relations'" because "[i]ncreasing mandatory fees paid out of the debtor's estate decreases the funds available for payment to creditors." *Id.* at *6.

The decision also repudiated the UST's argument, embraced by some courts below, that the geographical disparity was justified by the need to address a shortfall in UST funding that did not exist in BA districts. The Court noted that this difference "existed only because Congress itself had arbitrarily separated the districts into two different systems with different cost funding mechanisms, requiring Trustee Program districts to fund the Program through user fees while enabling Administrator Program districts to draw on taxpayer funds by way of the Judiciary's general budget." *Id.* at *8. The Court likewise rejected the UST's attempt to shift blame from Congress to the Judicial Conference for the unequal fee structure, noting that "prior to the 2021 amendment, the fee statute did not require the Judicial Conference to impose an equivalent increase. It is that congressional decision that led to the disparities at issue here." *Id*. at n. 2.

The Court's decision in *Siegel* brings finality to the question of whether the 2017 Amendment violates the uniformity requirement of the Bankruptcy Clause. However, the Court left open two key questions for future cases.

First, the Court's reasoning strongly suggested, but did not hold, that the dual UST/BA system for administering bankruptcy cases itself may violate the uniformity requirement. Future debtors could seek to challenge the dual system itself, which has been in place since 1986. However, a hurdle for any such challenges will be identifying a concrete way in which case administration by a UST is more or less beneficial than administration by a BA. Second, the Court declined to take up the UST's argument that, even if the law was unconstitutional, the appropriate remedy would not be a refund. *Id.* at *9. Observing that the court below "has not yet had an opportunity to address these issues or their relevancy to the proper remedy," the Court remanded this issue for further proceedings. *Id.*

LAWYER SPOTLIGHT: BRUCE BENNETT

Bruce Bennett, a partner in the Los Angeles and New York offices, has been at the helm of many of the largest corporate reorganizations in the United States. He has acted as counsel for major creditors in the chapter 11 cases for iHeart Communications, Caesars Entertainment Operating Corp., Energy Future Holdings, and General Motors; and in out-of-court negotiations and in insolvency cases for instrumentalities of Puerto Rico. He was also co-lead counsel for the City of Detroit in its historic chapter 9 debt adjustment cases.

In 2021, Bruce was honored with the "Mega Company Turnaround/Transaction of the Year" award by the Turnaround Management Association. He was selected for his role as a principal member of the team of legal counsel and financial advisors who represented holders of approximately 40% of the equity interests of PG&E Corp., the owner of Pacific Gas and Electric Company ("PG&E") in connection with their chapter 11 reorganization cases. PG&E is the largest utility in California and one of the largest public utilities in the United States, and the bankruptcy cases were among the largest in U.S. history.

Bruce recently stepped down as Global Practice Leader of the Firm's Business Restructuring & Reorganization Practice, a role in which he had served since 2016, now held by Heather Lennox. He continues to advise clients as a partner in the practice.

Assuming the Fourth Circuit awards a refund, the practical impact of the decision is likely to be limited. For one, *Siegel* applies only to chapter 11 debtors in UST districts whose cases were pending before October 1, 2018, and who paid fees on disbursements exceeding $1 million. This is necessarily a limited group of debtors, many of whose chapter 11 cases may already have been closed. Moreover, *Siegel* permits those debtors to recover only excess fees charged between January 1, 2018 and March 31, 2021, when a new law imposing a uniform fee structure went into effect. Finally, even if a debtor is eligible for a refund, it will need to determine whether the costs of seeking a refund justify the amount of excess fees it would stand to recover. That calculus is unlikely to justify a refund in many cases. Still, for chapter 11 debtors in UST districts whose cases were pending before October 1, 2018, and who paid significant excess fees in a Circuit that permits a refund, *Siegel* could allow those debtors to recover some of the fees paid to the UST during the nonuniform period.

Two petitions for *certiorari* filed by the UST squarely raised the "remedy" question in seeking review of the decisions by the Second and Tenth Circuits, which had ordered refunds to debtors for excess fees paid during the period from January 1, 2018, through March 31, 2021, when the non-uniform fee schedule was in effect. *See William K. Harrington, United States Trustee, Region 2, Petitioner v. Clinton Nurseries, Inc.*, No. 21-1123 (U.S. 2021); *Office of the United States Trustee v. John Q. Hammons Fall 2006, LLC*, No. 21-1078 (U.S. 2021).

On June 13, 2022, the Supreme Court issued a "Summary Disposition" of the *John Q. Hammons* petition that granted *certiorari*, vacated, and remanded for further consideration in light of *Siegel*. The *Clinton Nurseries* petition is still pending.

An earlier article discussing in more detail the chapter 11 fee structure and circuit court opinions addressing its constitutionality is available here.

RULINGS ON *CERTIORARI* PETITIONS IN OTHER BANKRUPTCY CASES

Exceptions to Bankruptcy Discharge. On May, 2, 2022, the U.S. Supreme Court granted a petition for *certiorari* in *Bartenwerfer v. Buckley*, No. 21-908 (U.S. May 2, 2022), where it will have an opportunity to resolve a circuit split regarding whether a debt based on fraud committed by, or a false representation made by, the debtor's partner or agent is nondischargeable in the debtor's bankruptcy case. Under section 523(a)(2)(A) of the Bankruptcy Code, a discharge of debts under section 727 and parallel sections of other chapters of the Bankruptcy Code does not apply to "any debt . . . for money . . . obtained by . . . false pretenses, a false representation, or actual fraud."

Although *liability* for fraud committed by a partner or agent can be imputed to other partners or a principal, the circuits and lower courts have long disagreed as to whether a debtor must have some degree of scienter (i.e., the debtor knew or should have known of its partner's or agent's fraud or false representation) before the debt based on that liability is deemed nondischargeable in the debtor's bankruptcy. *See generally* Collier on Bankruptcy ¶ 523.08[3] (16th ed. 2022) (discussing cases beginning with the Supreme Court's decision in *Strang v. Bradner*, 114 U.S. 555 (1885), under the since-repealed Bankruptcy Act of 1867).

Mootness of Appeals. On June 6, 2022, the Court declined to review an Eleventh Circuit decision dismissing appeals of bankruptcy court orders disallowing through estimation a secured claim and confirming a chapter 11 plan under the doctrines of constitutional and equitable mootness. *See KK-PB Financial LLC v. 160 Royal Palm LLC*, No. 21-1197 (U.S. June 6, 2022).

However, on June 27, 2022, the Court granted a petition to review the Second Circuit's 2021 decision dismissing an appeal brought by Mall of America challenging the bankruptcy court's assignment of Mall of America's lease to an affiliate of Transform Holdco, the purchaser of bankrupt retailer Sears's assets. See *MOAC Mall Holdings LLC v. Transform Holdco LLC (In re Sears Holdings Corp.)*, 2021 WL 5986997 (2d Cir. Dec. 17, 2021), *cert. granted*, No. 21-1270 (U.S. June 27, 2022). In its decision, the Second Circuit agreed with the district court below, which concluded that Mall of America's appeal was moot under section 363(m) of the Bankruptcy Code because it failed to obtain a stay of the bankruptcy court order approving the assignment.

Both of these cases involve different types of "mootness" that arise frequently in bankruptcy appeals. Mootness is a doctrine that precludes a reviewing court from reaching the underlying merits of a controversy. An appeal can be either constitutionally, equitably, or statutorily moot. The *KK-PB Financial* case involved constitutional and equitable mootness. Constitutional mootness is derived from Article III of the U.S. Constitution, which limits the jurisdiction of federal courts to actual cases or controversies and, in furtherance of the goal of conserving judicial resources, precludes adjudication of cases that are hypothetical or merely advisory.

The court-fashioned remedy of "equitable mootness" bars adjudication of an appeal when a comprehensive change of circumstances has occurred such that it would be inequitable

for a reviewing court to address the merits of the appeal. In bankruptcy cases, appellees often invoke equitable mootness as a basis for precluding appellate review of an order confirming a chapter 11 plan that has been "substantially consummated."

An appeal can also be rendered moot (or otherwise foreclosed) by statute—the issue presented in *Sears Holdings*. For example, sections 363(m) and 364(e) provide that a bankruptcy court order approving an asset sale to a good-faith purchaser or postpetition financing provided by a good-faith lender, respectively, cannot be reversed or modified on appeal absent a stay of the order pending the appeal. *Sears Holdings* involves the application of section 363(m) to the lease assignment transaction at issue.

Standard for Imposing Contempt Sanctions. On June 13, 2022, the Court denied a petition for review of a 2021 decision in which a divided panel of the U.S. Court of Appeals for the Second Circuit ruled that the "fair ground of doubt" standard articulated by the Court in *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), for imposing contempt sanctions due to a violation of the bankruptcy discharge injunction, also applied to contempt sanctions imposed for repeated violations of bankruptcy court orders declaring a home mortgage current. *See PHH Mortgage Corp. v. Sensenich (In re Gravel)*, 6 F.4th 503 (2d Cir. 2021), *petition for cert. denied*, No. 21-1322 (U.S. June 13, 2022).

In a decision discussed elsewhere in this edition of the *Business Restructuring Review—Beckhart v. Newrez LLC*, 2022 WL 1122534 (4th Cir. Apr. 15, 2022)—the Fourth Circuit ruled that "*Taggart* also applies when a court is considering whether to hold a creditor in civil contempt for violating a plan of reorganization of debts entered under Chapter 11." More broadly, the Fourth Circuit wrote, "Nothing about the Supreme Court's analysis in *Taggart* suggests it is limited to violations of Chapter 7 discharge orders . . . or that the Court's decision turned on considerations unique to the Chapter 7 context."

BUYER'S BAD FAITH IN FAILING TO INFORM COURT OF RIGHT OF FIRST REFUSAL PRECLUDES STATUTORY MOOTNESS OF BANKRUPTCY SALE

T. Daniel Reynolds • Mark G. Douglas

The finality of asset sales in bankruptcy is an indispensable feature of U.S. bankruptcy law designed to maximize the value of a bankruptcy estate as expeditiously as possible for the benefit of all stakeholders. To promote the finality of bankruptcy sales, section 363(m) of the Bankruptcy Code prohibits reversal or modification on appeal of an order approving a sale to a good-faith purchaser unless the party challenging the sale obtains a stay pending appeal. Section 363(m) has also been read broadly to protect the interests of any good-faith purchaser in the purchased assets.

The U.S. Court of Appeals for the Seventh Circuit recently examined the scope of 363(m) in *Archer-Daniels-Midland Co. v. Country Visions Cooperative*, 29 F.4th 956 (7th Cir. 2022). The court of appeals affirmed lower court rulings denying a motion to bar an entity holding a right of first refusal on property purchased from a debtor "free and clear" of all interests pursuant to section 363(f) from continuing state court litigation seeking to enforce its right. In doing so, the Seventh Circuit appears to have placed an affirmative obligation on asset purchasers to notify the bankruptcy court of any notice deficiencies discovered during the sale process. According to the Seventh Circuit, because the buyer had actual and constructive knowledge of a right of first refusal held by a party who had not received notice of the bankruptcy, yet never informed the bankruptcy court, the buyer had not acted in good faith and was not entitled to the protections of section 363(m).

THE BREADTH OF SECTION 363(M)

Section 363(m) of the Bankruptcy Code is a powerful protection for good-faith purchasers because it limits appellate review of a consummated sale irrespective of the legal merits of the appeal. *See Made in Detroit, Inc. v. Official Comm. of Unsecured Creditors of Made in Detroit, Inc. (In re Made in Detroit, Inc.)*, 414 F.3d 576 (6th Cir. 2005); *see also In re Palmer Equip., LLC*, 623 B.R. 804, 808 (Bankr. D. Utah 2020) (section 363(m)'s protection is vital to encouraging buyers to purchase the debtor's property and thus ensuring that adequate sources of financing are available).

Section 363(m) has also been read to go further than simply limiting appellate review— broadly protecting the interests of any good-faith purchaser by subjecting any collateral attack made against a section 363 sale to a good-faith purchaser to the requirements of Rule 60(b) of the Federal Rules of Civil Procedure, which governs motions for reconsideration of or relief from prior court judgments or orders. *See In re Edwards*, 962 F.2d 641 (7th Cir. 1992) (holding that a collateral attack on sale to a good-faith purchaser must be made pursuant to Fed. R. Civ.

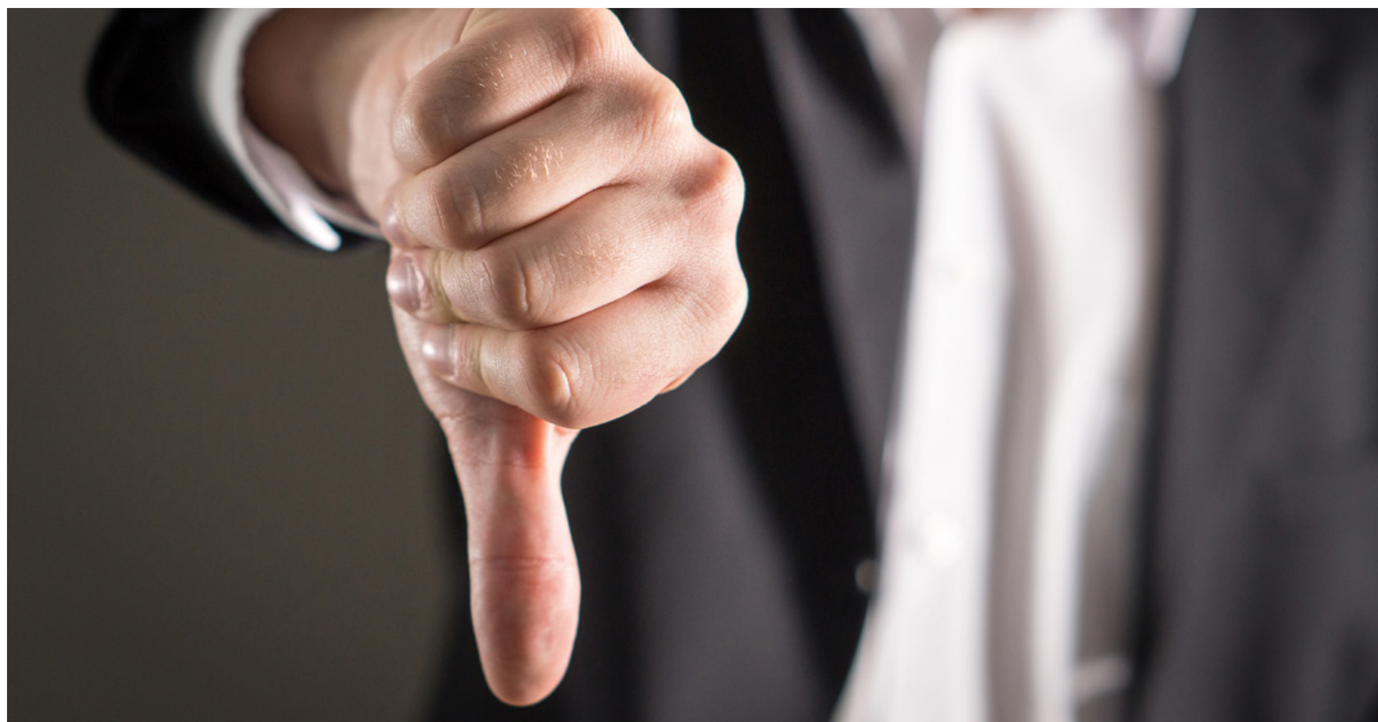
Proc. 60(b)); *In re Veg Liquidation, Inc.*, 572 B.R. 725, 737 (Bankr. W.D. Ark. 2017) ("To the extent the trustee is alleging that fraud was involved, his remedy is under Rule 60, not [section] 363(m)."), *aff'd*, 583 B.R. 203 (B.A.P. 8th Cir. 2018), *aff'd*, 931 F.3d 730 (8th Cir. 2019); *see also In re Alan Gable Oil Dev. Co.*, 978 F.2d 1254 (4th Cir. 1992) ("[T]hough section 363(m) does not in the strictest sense apply to [a movant›s] 60(b) motion, the policy favoring protection of good faith purchasers of estate property does. Not only does [the movant] bear the burden of establishing that the district court abused its discretion, he must do so in light of the strong policy favoring good faith purchasers of bankruptcy assets.»); *In re Nilhan Devs., LLC*, 631 B.R. 507, 534 (Bankr. N.D. Ga. 2021) ("Sale orders in bankruptcy cases are accorded a high level of finality and, accordingly 'collateral attacks on sale orders should generally be prohibited.'") (*quoting In re CHC Indus., Inc*., 389 B.R. 767, 774 (Bankr. M.D. Fla. 2007)).

GOOD FAITH

The Bankruptcy Code does not define "good faith." Courts have adopted various definitions, many of which are substantially similar. *See generally* COLLIER ON BANKRUPTCY ("COLLIER") ¶ 363.11 (16th ed. 2022). For example, the U.S. Court of Appeals for the Fifth Circuit has defined a "good faith purchaser" for purposes of section 363(m) as "'one who purchases the assets for value, in good faith, and without notice of adverse claims.'" *Hsin Chi Su v. C Whale Corp. (In re C Whale Corp.)*, 2022 WL 135125, *3 (5th Cir. Jan. 13, 2022) (quoting *In re TMT Procurement Corp.*, 764 F.3d 512, 521 (5th Cir. 2014)); *accord In re Mark Bell Furniture Warehouse, Inc.*, 992 F.2d 7, 8 (1st Cir. 1993). Lack of good faith is commonly manifested by "fraud, collusion between the purchaser and other bidders or the trustee, or an attempt to take grossly unfair advantage of the other bidders." *TMT Procurement*, 764 F.3d at 521; *accord In re Ewell*, 958 F.2d 276, 279 (9th Cir. 1992); *In re Abbotts Dairies, Inc.*, 788 F.2d 143, 147 (3d Cir. 1986); *Hoese Corp. v. Vetter Corp. (In re Vetter Corp.)*, 724 F.2d 52, 56 (7th Cir. 1983); *Badami v. Burgess (In re Burgess)*, 246 B.R. 352, 356 (B.A.P. 8th Cir. 2000); *In re General Motors Corp.*, 407 B.R. 463, 494 (Bankr. S.D.N.Y. 2009).

Some courts—principally in the Third Circuit—require a finding of good faith at the time the bankruptcy court approves a sale or lease of property under section 363. *See Abbotts Dairies, Inc.*, 788 F.2d at 149–50; *In re Perona Bros., Inc.*, 186 B.R. 833, 839 (D.N.J. 1995); *In re Primel*, 629 B.R. 790, 799 (Bankr. W.D. Pa. 2021); *In re Hereford Biofuels, L.P.*, 466 B.R. 841, 860 (Bankr. N.D. Tex. 2012). Other courts do not. *See, e.g., In re Zinke*, 97 B.R. 155, 156 (E.D.N.Y. 1989) (declining to adopt the *Abbotts Dairies* rule); *In re M Cap. Corp.*, 290 B.R. 743, 748 (B.A.P. 9th Cir. 2003) ("Because findings of 'good faith' made at the time of the sale may be premature because they are made before the really interesting facts emerge, the Ninth Circuit does not require that a finding of 'good faith' be made at the time of sale and has rejected the Third Circuit's contrary rule.").

Courts also disagree as to whether any entity asserting a lien on, or other interest in, property to be sold free and clear under section 363(f) of the Bankruptcy Code must be provided with advance notice of the sale for the purchaser of the property to be entitled to the protection of section 363(m). *See generally* COLLIER at ¶ 363.11 ("The protection afforded by section 363(m) has been held not to protect even an otherwise good faith purchaser when no notice was given to the lienholder, resulting in the purchaser taking the property subject to the lien."). *Compare*



United States v. Moberg Trucking, Inc. (In re Moberg Trucking, Inc.), 112 B.R. 362 (B.A.P. 9th Cir. 1990) (section 363(m) requires that a sale be authorized under section 363(b), which specifically requires notice and a hearing; thus, section 363(m) mootness is not applicable when the appellant seeks to attack the section 363 sale of estate property on the grounds of improper notice) *with In re Edwards*, 962 F.2d 641 (7th Cir. 1992) (a purchaser at a section 363(b) sale took clear title even though the lienholder did not receive notice at the time of the sale); *In re Motors Liquidation Co.*, 529 B.R. 510 (Bankr. S.D.N.Y. 2015) (lack of notice will not invalidate a sale, unless party can show prejudice).

ARCHER-DANIELS

In 2007, Olsen Brothers Enterprises, LLP ("OBC") granted a 10-year right of first refusal on a Wisconsin grain facility to the predecessors in interest of Country Visions Cooperative (collectively, "CVC"). CVC duly recorded the right in the local real estate records. OBC dissolved shortly afterward and distributed its assets to its partners (brothers Paul and David Olsen), an event that neither triggered nor dissolved the right of first refusal according to its terms.

In 2010, the Olsen brothers and their spouses filed for chapter 11 protection in the Eastern District of Wisconsin. Their chapter 11 plan provided for the sale of the grain-facility property to Archer-Daniels-Midland Co. ("Archer") free and clear of all liens under section 363(f). In performing its due diligence, Archer acquired a copy of a title report for the property that disclosed CVC's right of first refusal. Archer was also aware that CVC was not a party to the bankruptcy case, and Archer had in fact been contacted by CVC's counsel about protecting its interest in the property. Archer never brought any of this to the attention of the bankruptcy court. In 2011, the bankruptcy court confirmed the plan and authorized the sale. CVC was never notified of the bankruptcy filing, the chapter 11 plan, or the sale.

In 2015, after Archer arranged to sell the property to another entity, CVC sued Archer in state court demanding compensation for the abrogation of its right of first refusal. Archer then asked the bankruptcy court to reopen the case and, relying on section 363(m), to issue an order enforcing the free and clear sale of the property and barring CVC from seeking any remedy in state court.

The bankruptcy court reopened the case, but declined to grant the relief requested by Archer. The district court affirmed on appeal. Both courts ruled that Archer had not acquired the property in good faith because it knew of the existence of CVC's right of first refusal, yet failed to alert the bankruptcy court. Given the failure of the debtors and Archer to disclose what they knew about CVC's right of first refusal, the bankruptcy court considered vacating the sale as a fraud on the court, but instead merely denied Archer's motion for an order enjoining the state court litigation. Archer appealed to the Seventh Circuit.

THE SEVENTH CIRCUIT'S RULING

A three-judge panel of the Seventh Circuit affirmed. According to U.S. Circuit Judge Frank H. Easterbrook, "it seem[ed] clear" that the Olsen brothers proceeded in bad faith because: (i) they knew of CVC's right of first refusal, yet failed to notify CVC of their bankruptcy filing and the proposed sale of the property, for which they were obligated to give CVC at least 21 days' notice under Rule 2002(f) of the Federal Rules of Bankruptcy Procedure; and (ii) they failed to inform the bankruptcy court of CVC's interest.

However, Judge Easterbrook explained, the dispute at issue was between CVC and Archer, and "[t]he question is whether [Archer] bought the parcel in good faith, not whether the Olsens sold it in bad faith." "[O]n that score," he wrote, "it is impossible to disagree with the bankruptcy and district judges that someone who has both actual and constructive knowledge of a competing interest, yet permits the sale to proceed without seeking the judge's assurance that the competing interest-holder may be excluded from the proceedings, is not acting in good faith." *Archer-Daniels,* 29 F.4th at 959.

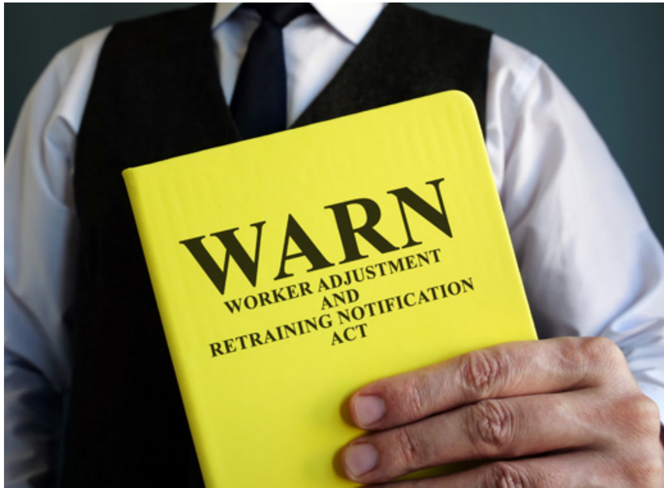
Had CVC been made a party to the proceedings, Judge Easterbrook noted, it would have been in a position to appeal an order approving the sale over its objection. But it was not, he wrote, "and a non-party cannot be expected to appeal." *Id.*

The Seventh Circuit accordingly ruled that Archer was not a good-faith purchaser and that it was therefore obligated to defend the state court litigation.

OUTLOOK

The finality of bankruptcy asset sales is an essential aspect of the American bankruptcy system. It is designed to promote the expeditious administration of bankruptcy estate assets and bring an element of certainty to purchasers, without which they might be either disinclined to participate in the sale process or unwilling to offer a fair price. Section 363(m) essentially cuts off most challenges to a court-approved sale, but *Archer-Daniels* illustrates that the provision has limitations. One of them is that the purchaser—as distinguished from the debtor or the trustee—must have acted in good faith to qualify for its protections.

In many respects, the facts in *Archer-Daniels* presented an easy case because it was clear that both the purchaser and the debtor purposefully concealed information from the bankruptcy court. In addition to the direct inquiry from counsel to CVC, the purchaser had actual and constructive knowledge based upon the fact that the title report for the property listed the right of first refusal. Potential bankruptcy asset purchasers should heed *Archer-Daniels*'s warning: In order to protect one's status as a "good-faith purchaser," a buyer must act as if it has an affirmative obligation to fully diligence the marketed asset and inform the court of any notice deficiencies that may exist.



LIQUIDATING CHAPTER 11 DEBTOR EXCUSED FROM PROVIDING WARN ACT NOTIFICATION OF EMPLOYEE LAYOFFS DUE TO PANDEMIC NATURAL DISASTER

Daniel J. Merrett • Mark G. Douglas

Large employers intending to lay off a significant number of their employees are required by the Worker Adjustment and Retraining Notification Act of 1988 (the "WARN Act") to give the targeted employees 60 days' advance notice of the layoffs. However, there are certain exceptions to the notice requirement in cases where the employer is a "faltering business" or a "liquidating fiduciary," or where "unforeseeable business circumstances" or a "natural disaster" make it impracticable or impossible to provide 60 days' advance notice of a mass layoff.

The U.S. Bankruptcy Court for the District of Delaware recently examined the scope of these exceptions in a case involving mass layoffs by a company that filed for chapter 11 protection to liquidate its assets at the beginning of the COVID-19 pandemic. In *In re Art Van Furniture, LLC*, 638 B.R. 523 (Bankr. D. Del. 2022), the court ruled that, although a debtor-employer did not qualify as a liquidating fiduciary because it continued operating after the petition date, the debtor was excused from full compliance with the WARN Act notification requirement due to the COVID-19 pandemic, which represented both an unforeseeable business circumstance and a natural disaster.

THE WARN ACT

Enacted in 1988, the WARN Act protects workers, their families, and communities by requiring most employers with 100 or more employees to provide notification of plant closings and mass layoffs 60 calendar days prior to the event. *See* 29 U.S.C. § 2102(a).

U.S. Department of Labor ("DOL") regulations prescribe when an employer must give WARN Act notice, whom the employer must notify, how the employer must give notice, and what information the notice must contain. *See* 20 C.F.R. §§ 639 *et seq*.

According to 29 U.S.C. § 2104(a), an employer failing to give WARN Act notice is liable to each aggrieved employee who suffers an employment loss as a result of a plant closing or mass layoff for, among other things, back pay for each day during the period of the violation.

However, if an employer can prove that it shut down operations because either it was a "faltering company" or the shutdown was due to business circumstances "that were not reasonably foreseeable," it need not comply with the WARN Act's 60-day notice provisions. *See* 29 U.S.C. §§ 2102(b)(1) and (b)(2)(A); 20 C.F.R. § 639.9. In particular, 29 U.S.C. § 2102(b)(1) and (2)(A) provide as follows:

> (1) An employer may order the shutdown of a single site of employment before the conclusion of the 60-day period if as of the time that notice would have been required the employer was actively seeking capital or business which, if obtained, would have enabled the employer to avoid or postpone the shutdown and the employer reasonably and in good faith believed that giving the notice required would have precluded the employer from obtaining the needed capital or business.
>
> (2)(A) An employer may order a plant closing or mass layoff before the conclusion of the 60-day period if the closing or mass layoff is caused by business circumstances that were not reasonably foreseeable as of the time that notice would have been required.

Also, 29 U.S.C. § 2102(b)(2)(B) provides that "[n]o notice under [the WARN Act] shall be required if the plant closing or mass layoff is due to any form of natural disaster, such as a flood, earthquake, or the drought currently ravaging the farmlands of the United States."

The WARN Act defines an "employer" as "any business enterprise that employs: (i) 100 or more employees, excluding part-time employees; or (ii) 100 or more employees who in the aggregate work at least 4,000 hours per week (exclusive of hours of overtime)." 29 U.S.C. § 2101(a)(1).

DOL commentary to WARN Act regulations (the "DOL Commentary") addresses whether a debtor in bankruptcy qualifies as an "employer" under the WARN Act:

> [T]he term "business enterprise" used in the statute includes public and quasi-public entities which engage in business (*i.e.*, take part in a commercial or industrial enterprise; supply a service or good on a mercantile basis, or provide independent management of public assets, raising revenue and making desired investments). . ..
>
> [T]he Department does not think it appropriate to [exclude all debtors in bankruptcy from the definition of "employer"]. Further, DOL agrees that a fiduciary whose sole function

> in the bankruptcy process is to liquidate a failed business for the benefit of creditors does not succeed to the notice obligations of the former employer because the fiduciary is not operating a "business enterprise" in the normal commercial sense. In other situations, where the fiduciary may continue to operate the business for the benefit of creditors, the fiduciary would succeed to the WARN obligations of the employer precisely because the fiduciary continues the business in operation.

54 Fed. Reg. 16042, 16044-45 (Apr. 20, 1989).

This language is the genesis of a court-fashioned "liquidating fiduciary" exception, which provides that a liquidating fiduciary in a bankruptcy case (e.g., a trustee or other estate representative) does not fit the definition of "employer" for purposes of the WARN Act. *See Official Comm. of Unsecured Creditors of United Healthcare Sys., Inc. v. United Healthcare Sys., Inc. (In re United Healthcare Sys., Inc.)*, 200 F.3d 170 (3d Cir. 1999) (a health care debtor that filed for chapter 11 as a business liquidating its affairs rather than a business operating as a going concern was not an "employer" under the WARN Act, even though it retained its 1,200 employees for 16 days after the petition date); *Conn v. Dewey & LeBoeuf LLP (In re Dewey & LeBoeuf LLP)*, 487 B.R. 169 (Bankr. S.D.N.Y. 2013).

The Third Circuit explained the parameters of the exception in *United Healthcare* as follows:

> [W]hether a bankrupt entity is an "employer" under the WARN Act depends on the nature and extent of the entity's business and commercial activities while in bankruptcy, and not merely on whether the entity's employees continue to work "on a daily basis." The more closely the entity's activities resemble those of a business operating as a going concern, the more likely it is that the entity is an "employer"; the more closely the activities resemble those of a business winding up its affairs, the more likely it is the entity is not subject to the WARN Act.

United Healthcare, 200 F.3d at 178.

In order to satisfy the "unforeseeable business circumstances" exception, the employer must demonstrate that: (i) the business circumstances causing the layoff were not reasonably foreseeable; and (ii) those circumstances caused the layoff. *See Calloway v. Canaco Pharm. Labs., Ltd.*, 800 F.3d 244 (6th Cir. 2015); 20 C.F.R. § 639.9(b).

Under DOL regulations, closings and layoffs are not foreseeable when "caused by some sudden, dramatic, and unexpected action or condition outside the employer's control." 20 C.F.R. § 639.9(b)(1). The regulations also provide that, in assessing the foreseeability of business circumstances, the focus should be "on an employer's business judgment" and that an employer is required only to "exercise such commercially reasonable business judgment as would a similarly situated employer in predicting the demands of its particular market." 20 C.F.R. § 639.9(b)(2).

Six circuit courts of appeals have ruled that, in order to be "reasonably foreseeable" as this phrase is used in the WARN Act, an event must be probable rather than merely possible. *See Varela v. AE Liquidation, Inc. (In re AE Liquidation, Inc.)*, 866 F.3d 515, 531-32 (3d Cir. 2017) (upholding lower court rulings that a chapter 11 debtor-employer could rely on the WARN Act's "unforeseeable business circumstances" exception because a proposed sale of the company as a going concern under section 363(b) of the Bankruptcy Code collapsed due to the failure of a Russian bank to honor its commitment to provide the buyer with acquisition financing); *United Steel Workers of Am. Local 2660 v. U.S. Steel Corp.*, 683 F.3d 882, 887 (8th Cir. 2012) (an employer's knowledge that an economic downturn would hurt demand for its product did not preclude the unforeseeable business circumstances exception because "[n]othing in the record suggests that the extent of the economic downturn and its effects on the steel industry were probable any time before [the time notice was given]"); *Gross v. Hale-Halsell Co.*, 554 F.3d 870, 876 (10th Cir. 2009) ("[W]e do not rely on the mere possibility that layoffs will occur, but rather look for their probability"); *Roquet v. Arthur Andersen LLP*, 398 F.3d 585, 589 (7th Cir. 2005) (ruling that although it was "[c]ertainly possib[le]" that the accounting firm rather than its individual officers would be indicted, that possibility never rose to the level of "probable," and thus the unforeseeable business circumstances exception applied); *Watson v. Mich. Indus. Holdings, Inc.*, 311 F.3d 760, 765 (6th Cir. 2002) (adopting the probability standard and noting that "WARN was not intended to force financially fragile, yet economically viable, employers to provide WARN notice . . . when there is a *possibility* that the business may fail at some undetermined time in the future"); *Halkias v. General Dynamics Corp.*, 137 F.3d 333, 336 (5th Cir. 1998) (noting that anything less than probability would be "impracticable" and reasoning that, if the mere possibility of layoffs were enough to trigger the WARN Act, contractors "would be put to the needless task of notifying employees of possible contract cancellation and concomitant lay-offs" every time cost overruns caused the cancellation of contracts, even though layoffs were not likely).

Even if one of the exceptions in 29 U.S.C. § 2102(b)(1) and (b)(2)(A) applies, an employer is not completely relieved of its obligation to notify employees. The employer can give less than 60 days' WARN Act notice, provided that the notice contains certain "basic" information (*see* 20 C.F.R. § 639.7) and the reasons the employer could not provide the full 60 days' notice. *See* 29 U.S.C. § 2102(b)(3).

If an employer is selling all or part of its business, the WARN Act provides that the seller is responsible for providing employees with notice of any mass layoff "up to and including the effective date of the sale," after which that responsibility shifts to the buyer. 29 U.S.C. § 2101(b)(1). If the sale is on a going-concern basis, it is presumed that the sale "involves the hiring of the seller's employees unless something indicates otherwise," whether or not the

sale agreement expressly provides for retention of the seller's employees. *Wilson v. Airtherm Prods., Inc.*, 436 F.3d 906, 912 (8th Cir. 2006).

The Delaware bankruptcy court addressed the liquidating fiduciary, unforeseeable business circumstances and natural disaster exceptions in *Art Van*.

ART VAN

After defaulting on one of its secured loans in the wake of a 2017 leveraged buyout and failing to obtain alternative financing or attract a going-concern buyer, brick-and-mortar furniture and mattress retailer Art Van Furniture, LLC (together with its affiliates, "AVF") announced that it was liquidating on March 5, 2020. The same day, AVF issued a WARN Act notice to approximately 1,400 employees in its 169 stores located in Michigan, Indiana, Ohio, Illinois, Pennsylvania, Maryland, Missouri, and Virginia. The notice informed employees that their employment would terminate on May 5, 2020, or within two weeks thereafter. From March 5 to March 8, 2020, AVF conducted going-out-of-business ("GOB") sales at certain stores.

AVF filed for chapter 11 protection on March 8, 2020, in the District of Delaware, citing extreme market conditions for the filing and listing more than $200 million in secured debt. The company filed for bankruptcy with plans to shutter all but 44 of its stores and to sell the remaining stores as a going concern.

However, AVF closed all 169 of its retail locations on March 19, 2020, after the governors of Michigan, Maryland, Pennsylvania, and certain other states imposed restrictions on the operation of nonessential businesses in an effort to slow the advance of COVID-19. The shutdowns stopped the store-closing sales, and AVF abandoned its plan for a going-concern sale.

Also on March 19, 2020, AVF issued a second WARN Act notice to some of its employees stating in part that, due to "unforeseen events" precipitated by the pandemic, "the Company can no longer support the wind-down of its retail operations through the originally projected termination date" and that all employees would be terminated as of March 20, 2020 (the "March 20, 2020 layoff").

On March 23, 2020, two former AVF employees filed a class action adversary proceeding in the bankruptcy court alleging that AVF failed to comply with the WARN Act when it terminated its employees as part of the March 20, 2020, layoff.

In early April 2020, AVF filed a motion seeking conversion of its chapter 11 cases to chapter 7, stating that, although it initially wished to seek court authority "to 'mothball' [its] remaining assets and operations and to suspend substantially all activity in these chapter 11 cases until such time as the broader economic and public safety situations stabilized and hopefully improved," AVF abandoned this course of action after "no viable path forward in chapter 11 emerged that would garner the support of [AVF's] senior secured lenders and certain other stakeholders." The bankruptcy court granted the conversion motion on April 6, 2020.

The chapter 7 trustee moved for summary judgment against the plaintiffs in the WARN Act adversary proceeding. He argued that: (i) at the time of the layoffs, AVF was a "liquidating fiduciary" and therefore not an "employer" under WARN Act regulations subject to WARN Act liability; or (ii) either the "unforeseen business circumstances" or the "natural disaster" exception to WARN Act liability applied. The plaintiffs countered that AVF operated as an "employer" under the WARN Act by using its employees to hold postpetition GOB sales or to keep certain stores operating pending a bulk sale, and that there were disputed issues of material fact concerning the cause of the layoffs that precluded summary judgment.

THE BANKRUPTCY COURT'S RULING

The bankruptcy court granted the trustee's motion for summary judgment.

U.S. Bankruptcy Judge Christopher S. Sontchi explained that applying the liquidating fiduciary exception in a chapter 11 case "requires careful analysis of the particular facts and circumstances . . . to determine whether the entity's activities resemble a business enterprise operating as a going concern or a business enterprise engaged in the winding-up of its affairs." *Art Van*, 638 B.R. at 535. Although AVF announced its intention to liquidate prior to filing for chapter 11 protection, Judge Sontchi noted, it continued operating after the petition date for the benefit of creditors. Guided by the Third Circuit's decision in *United Healthcare* and the DOL Commentary, he accordingly ruled that AVF did not qualify for the liquidating fiduciary exception and was therefore subject to an employer's WARN Act notice obligations.

However, Judge Sontchi concluded that the unforeseen business consequences exception did apply. He explained that it was undisputed that: (i) AVF was in dire financial straits leading up to the bankruptcy filing and filed for chapter 11 to pursue an "orderly wind down" of operations and liquidation of assets; and (ii) in mid-March 2020, the pandemic caused several states where AVF operated to issue "stay at home" or "shelter in place" orders that unquestionably impacted AVF's operations. Given these undisputed facts, Judge Sontchi wrote, the plaintiff's argument that the pandemic "was merely a pretext for the mass layoffs is tenuous at best." *Id.* at 539. He concluded that "COVID-19 was the proverbial 'straw that broke the camel's back' and caused the March 20, 2020 layoff." *Id*. Judge Sontchi also found that the second WARN Act notice sent by AVF adequately described the reason for the March 20, 2020, layoff and the abbreviated notice.

Finally, Judge Sontchi held that the natural disaster exception also applied to the case before him. He explained that several other courts have concluded that COVID-19 qualifies as a natural disaster. Judge Sontchi declined to decide whether a "proximate cause" standard or a less-stringent "but for" standard applied

in this case, but he noted that, even under the more stringent standard, "[t]he undisputed facts in this case support the finding that the COVID-19 was an immediate cause of the March 20, 2020 layoff." *Id.* at 542.

OUTLOOK

Art Van provides important guidance on the impact of a chapter 11 filing on a debtor-employer's obligation to satisfy the WARN Act's notification requirements, particularly when mass layoffs are caused entirely or in part by the COVID-19 pandemic or analogous situations. The exceptions to that obligation—the faltering company, unforeseeable business circumstances, liquidating fiduciary, and natural disaster exceptions—are premised on the idea that WARN Act notification, either timely or at all, may simply not be possible under certain circumstances. This represents a balance between the goal of protecting the rights of employees and recognition of the difficulties faced by many employers confronting financial distress or cataclysmic events that render compliance impracticable or impossible.

The Delaware bankruptcy court's decision in *Art Van* also illustrates that determinations regarding the satisfaction of any of these exceptions depend on the facts of each particular case. In fact, the court recognized that not all debtors operating in liquidating chapter 11 cases will be subject to WARN Act notification obligations. Instead, it noted that "[e]ach case must be evaluated on its own merits," and in a case in a Third Circuit jurisdiction, the facts and circumstances "must be evaluated in light of *United Healthcare* to determine whether there is an immediate shutdown and the fiduciary's sole function is liquidation." *Id.* at 536 n.86.

FLORIDA BANKRUPTCY COURT: CHAPTER 11 CREDITORS' COMMITTEE HAS NO UNCONDITIONAL RIGHT TO INTERVENE IN ADVERSARY PROCEEDING

Dan T. Moss • Mark G. Douglas

Bankruptcy and appellate courts disagree over whether a creditors' committee has the unconditional right to intervene in an adversary proceeding commenced during a chapter 11 case. The issue has created a split among the circuit courts of appeals, a majority of which have concluded that the Bankruptcy Code does provide for such a right.

The U.S. Bankruptcy Court for the Southern District of Florida recently weighed in on the controversy in *Dillworth v. Diaz (In re Bal Harbour Quarzo, LLC)*, 638 B.R. 660 (Bankr. S.D. Fla. 2022). The court rejected the majority approach, ruling that a creditors' committee established under a chapter 11 liquidating trust did not have an unconditional right to intervene in an adversary proceeding commenced by the liquidating trustee to avoid fraudulent transfers. The court also denied the committee's request for permissive intervention, finding that the committee's interests as well as the interests of the trust's beneficiaries were adequately represented by the trustee in the litigation.

RIGHT TO BE HEARD IN A CHAPTER 11 CASE

Section 1109(b) of the Bankruptcy Code provides that "[a] party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter."

This provision expressly provides any party in interest, including a creditors' committee, with an unconditional right to participate in a chapter 11 "case." "Case" refers to "litigation commenced by the filing with the bankruptcy court of a petition under the appropriate chapter of Title 11." *Term Loan Holder Comm. v. Ozer Grp., L.L.C. (In re Caldor Corp.)*, 303 F.3d 161, 167 (2d Cir. 2002) (internal quotation marks and citations omitted). By contrast, an "adversary proceeding" in bankruptcy is discrete litigation commenced during a bankruptcy case to, among other things: recover money or property (e.g., avoid fraudulent or preferential transfers); determine the validity, priority, or extent of a lien or other interest in property; revoke an order confirming a chapter 11 plan; or obtain injunctive relief. *See* Fed. R. Bankr. P. 7001.

INTERVENTION

"Intervention" is a procedure that permits a nonparty to join ongoing litigation, either as a matter of right or at the discretion of the court, without the permission of the original litigants, generally because a judgment in the case may impact the rights of the nonparty intervenor. The ability to intervene in federal litigation is generally governed by Fed. R. Civ. P. 24, which is made

applicable in its entirety to adversary proceedings commenced in a bankruptcy case by Fed. R. Bankr. P. 7024.

Fed. R. Civ. P. 24(a) provides that, on timely motion, the court *must* permit anyone to intervene who:

(1) is given an unconditional right to intervene by a federal statute; or
(2) claims an interest relating to the property or transaction that is the subject of the action, and is so situated that disposing of the action may as a practical matter impair or impede the movant's ability to protect its interest, unless existing parties adequately represent that interest.

Pursuant to Fed. R. Civ. P. 24(b), the court *may* permit anyone to intervene who:

(A) is given a conditional right to intervene by a federal statute; or
(B) has a claim or defense that shares with the main action a common question of law or fact.

Fed. R. Bankr. P. 2018 governs permissive intervention in a bankruptcy "case." It provides in part that "[i]n a case under the Code, after hearing on such notice as the court directs and for cause shown, the court may permit any interested entity to intervene generally or with respect to any specified matter."

Because section 1109(b) says nothing about "proceedings," some courts, noting the general distinction between cases and proceedings in the Bankruptcy Code and other federal statutes, have concluded that the provision applies only to bankruptcy cases and does not create an unqualified right to intervene in adversary proceedings. *See Fuel Oil Supply & Terminaling v. Gulf Oil Corp.*, 762 F.2d 1283 (5th Cir. 1985). Two other circuits have, in *dicta*, suggested that they agree with the *Fuel Oil* approach. *See Richman v. First Women's Bank (In re Richman)*, 104 F.3d 654, 658 (4th Cir. 1997); *Vermejo Park Corp. v. Kaiser Coal Corp. (In re Kaiser Steel Corp.)*, 998 F.2d 783, 790 (10th Cir. 1993).

However, the First, Second, and Third Circuits have rejected the reasoning in *Fuel Oil*, ruling instead that section 1109(b) provides a statutory right to intervene in adversary proceedings for purposes of Fed. R. Civ. P. 24(a)(1). *See Assured Guaranty Corp. v. Fin. Oversight & Mgmt. Bd. for Puerto Rico*, 872 F.3d 57 (1st Cir. 2017); *Caldor*, 303 F.3d at 176; *Phar-Mor, Inc. v. Coopers & Lybrand*, 22 F.3d 1228, 1240 (3d Cir. 1994); *see also Smart World Techs., LLC v. Juno Online Servs., Inc. (In re Smart World Techs., LLC)*, 423 F.3d 166, 180–81 (2d Cir. 2005) (although a creditors' committee has an unconditional right to intervene in an adversary proceeding, that right does not extend to settlement of the proceeding). *See generally* COLLIER ON BANKRUPTCY **¶ 1109.04 (16th ed. 2022) (discussing controversy).**

In *Caldor*, the Second Circuit explained that "the plain text of § 1109(b) does not distinguish between issues that occur in . . . different types of proceedings within a Chapter 11 case" and concluded that the provision applies to adversary proceedings as well as bankruptcy cases. *Caldor*, 303 F.3d at 169. According to the Second Circuit, "[a]lthough the bankruptcy rules and the [accompanying] advisory committee notes envision separate formalities for intervening in cases and adversary proceedings, they do not necessitate that the term 'case' in § 1109(b) be construed to exclude adversary proceedings." *Id.* at 173.

In *Phar-Mor*, the Third Circuit held that, consistent with its previous ruling in *In re Marin Motor Oil*, *Inc.*, 689 F.2d 445 (3d Cir. 1982),

cert. denied, 459 U.S. 1207 (1983), in which it held section 1109(b) gives a creditors' committee an unconditional right to intervene in an adversary proceeding, the provision "allows creditors' committees to intervene in non-core, 'related to' proceedings pending in a bankruptcy court." According to the Third Circuit, "interests of efficiency and fair play underlie § 1109(b), and the driving force behind the *Marin* decision was the belief that allowing intervention into adversary proceedings would best serve those interests." *Phar-Mor*, 22 F.3d at 1240. Moreover, the court wrote, "[t]here is no reason to think that the interests underlying § 1109(b) are limited or should be limited by the jurisdictional limitations imposed on the bankruptcy courts" by the U.S. Supreme Court's decision in *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), where the Court held that the existing grant of jurisdiction to bankruptcy courts, including the power to decide proceedings "related to those arising under the bankruptcy laws," violated Article III of the Constitution.

In *Assured Guaranty*, the First Circuit abandoned its prior citation in *dicta* to *Fuel Oil* in *Kowal v. Malkemus (In re Thompson)*, 965 F.2d 1136 (1st Cir. 1992), for the proposition that section 1109(b) does not afford a right to intervene under Fed. R. Civ. P. 24(a)(1). It ruled that section 1109(b) gave an unsecured creditors' committee appointed in the quasi-bankruptcy cases filed on behalf of certain Puerto Rico instrumentalities an unconditional

right to intervene, within the meaning of Fed. R. Civ. P. 24(a)(1), in an adversary proceeding commenced during a case filed pursuant to the Puerto Rico Oversight, Management, and Economic Stability Act. The First Circuit explained that the text of section 1109(b) applies generally to "cases," a term that encompasses all litigation commenced by the filing of a chapter 11 petition. It agreed with a leading commentator that, "[b]ecause every issue in a case may be raised and adjudicated only in the context of a proceeding of some kind, it is apparent that the reference . . . to 'any issue in a case' subsumes issues in a proceeding." *Assured Guaranty*, 872 F.3d at 63 (citing COLLIER ON BANKRUPTCY **¶ 1109.04[1][a][ii] (16th ed. 2016)).**

BAL HARBOUR

In February 2018, a receiver for Florida luxury hotel development company Bal Harbour Quartzo LLC ("BHQ") filed a chapter 11 petition on BHQ's behalf in the Southern District of Florida. The bankruptcy court confirmed a liquidating chapter 11 plan for BHQ in April 2019. For the benefit of BHQ's creditors, the plan created a liquidating trust to which the estate's causes of action were transferred. The plan also created a post-confirmation creditors' committee (the "committee") to "represent the interests of the Trust Beneficiaries during the existence of the Trust."

In 2020, the liquidating trustee (the "trustee") commenced an adversary proceeding against various defendants seeking, among other things, to avoid certain fraudulent transfers. Two years afterward, the committee moved to intervene in the adversary proceeding under section 1109(b) of the Bankruptcy Code and Fed. R. Civ. P. Rules 24(a) and 24(b). According to the committee, as interpreted by the courts in *Assured Guaranty*, *Caldor*, *Marin*, and various lower courts, section 1109(b) gave it an unconditional right to intervene.

THE BANKRUPTCY COURT'S RULING

The bankruptcy court denied the committee's motion to intervene.

U.S. Bankruptcy Judge Scott M. Grossman explained that the question was whether the phrase "in a *case* under this chapter" in section 1109(b) means only a main chapter 11 case or also encompasses adversary proceedings within a main chapter 11 case.

Judge Grossman respectfully disagreed with the majority approach exemplified by *Caldor*. Instead, he concluded that the Fifth Circuit's reasoning in *Fuel Oil* was both more persuasive and supported by the language of section 1109(b). He reached this determination in part on the basis of "another provision of the Bankruptcy Code which clearly shows that Congress knows how to distinguish between a case and a proceeding." In particular, he explained, section 307, which is similar but not identical to section 1109(b), provides that "[t]he United States Trustee may raise and may appear and be heard on any issue *in any case or proceeding under this title* but may not file a plan pursuant to section 1121(c) of this title." *Bal Harbour*, 638 B.R. at 666 (citing 11 U.S.C. § 307 (emphasis added)).

Accordingly, Judge Grossman wrote, "this Court concludes that section 1109(b) does not create an unconditional right to intervene by a creditors' committee." *Id.*

He noted that practical considerations support the minority view:

> Under the majority view, any creditor, equity security holder, or other party in interest would have the unconditional right to intervene in any adversary proceeding associated with a chapter 11 case. This could result in erosion of the procedural due process protections afforded to litigants in an adversary proceeding, wreak havoc on any efforts at efficient case management, and ultimately render an adversary proceeding virtually indistinguishable from a main bankruptcy case.

Id. at 666 n.41. Judge Grossman also explained that creditors, committees, and other stakeholders are not without recourse if a debtor or trustee is unwilling or unable to prosecute an adversary proceeding because they can: (i) seek derivative standing to do so on the estate's behalf; or (ii) support a chapter 11 plan that transfers causes of action to a post-confirmation entity and negotiate to have a fiduciary selected who will prosecute those claims. *Id.* at 666 n.42.

Judge Grossman also denied the committee's motion for intervention under Fed. R. Civ. P. 24(a)(2). According to the judge: (i) the committee's motion was not timely (having been filed more than two years after commencement of the adversary proceeding); (ii) while the creditor beneficiaries of the trust had an economic interest in the outcome of the litigation, the committee itself did not, nor did it have any "legally cognizable interest" because those rights were specifically given to the trustee under the plan and the liquidating trust agreement, and the committee sought to intervene merely to oversee and consult with the trustee (although it reserved the right to take positions on any issues that might arise during the litigation); and (iii) because the trustee was the plaintiff, the committee could not show that its interest or the interests of the creditor beneficiaries would not be represented adequately.

In addition, Judge Grossman concluded that the committee failed to demonstrate that permissive intervention was warranted under Fed. R. Civ. P. 24(b)(1)(B). Among other things, he found that the committee had "no claim or defense in its own right that it share[d] with the adversary proceeding as a common question of law or fact." *Id.* at 669.

Finally, Judge Grossman held that the committee failed to comply with Fed. R. Civ. P. 24(c), which requires that a motion

to intervene be accompanied by a pleading that sets forth the claims or defenses for which intervention is sought.

OUTLOOK

Bal Harbour indicates that the dispute regarding whether section 1109(b) creates an unconditional right to intervene in an adversary proceeding is alive and well. The arguments on both sides of the issue are persuasive and have been fully developed by the courts in thoughtful opinions. The resulting circuit split on the issue could be an invitation to Congress or the U.S. Supreme Court to resolve the issue.

The parade of horribles alluded to by the bankruptcy court in *Bal Harbour* and *Fuel Oil* regarding the risk that adherence to the majority view could open the intervention floodgates is likely overstated. In the majority of chapter 11 cases and related adversary proceedings, committees and other stakeholders would have little incentive to burden the estate with additional expense by intervening in litigation commenced by an estate fiduciary.

Finally, as noted by the *Bal Harbour* court, stakeholders in venues embracing the minority view on intervention have other recourse if an estate fiduciary is either unwilling or unable to prosecute estate causes of action.

ANOTHER CIRCUIT RULES THAT *TAGGART* STANDARD FOR CONTEMPT APPLIES BEYOND VIOLATIONS OF BANKRUPTCY DISCHARGE INJUNCTION

Daniel B. Prieto • Mark G. Douglas

In a decision that could have significant ramifications in bankruptcy cases, a divided panel of the U.S. Court of Appeals for the Second Circuit ruled in 2021 that the standard articulated by the U.S. Supreme Court in *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), for the imposition of contempt sanctions due to a violation of the bankruptcy discharge injunction in a chapter 7 case, also applied to contempt sanctions imposed for repeated violations of bankruptcy court orders declaring a home mortgage current. *See PHH Mortgage Corp. v. Sensenich (In re Gravel)*, 6 F.4th 503 (2d Cir. 2021), *reh'g en banc denied*, No. 20-1 (2d Cir. Nov. 1, 2021), *petition for cert. denied*, No. 21-1322 (U.S. June 13, 2022).

In 2022, the Fourth Circuit expanded the reach of *Taggart* even further. In *Beckhart v. Newrez LLC*, 31 F.4th 274 (4th Cir. 2022), a three-judge panel of the Fourth Circuit ruled that "*Taggart* also applies when a court is considering whether to hold a creditor in civil contempt for violating a plan of reorganization of debts entered under Chapter 11." More broadly, the court wrote, "Nothing about the Supreme Court's analysis in *Taggart* suggests it is limited to violations of Chapter 7 discharge orders . . . or that the Court's decision turned on considerations unique to the Chapter 7 context."

Given these holdings, two circuit courts of appeals have now concluded that *Taggart* casts a wider net in bankruptcy than the language of that opinion might have suggested.

TAGGART

In *Taggart*, the Supreme Court ruled that a bankruptcy court may hold a creditor in civil contempt for attempting to collect on a debt that has been discharged in bankruptcy "if there is no fair ground of doubt as to whether the [discharge] order barred the creditor's conduct." *Taggart*, 139 S. Ct. at 1801.

Taggart left open the question of whether the "fair ground of doubt" standard should apply to violations of other bankruptcy court orders or provisions of the Bankruptcy Code, such as a chapter 11 plan confirmation order, a discovery order, or the automatic stay. Many courts have weighed in on the issue, with mixed outcomes. *See, e.g., Deutsche Bank Trust Co. Americas v. Gymboree Group, Inc.*, 2021 WL 3618229, *11 (E.D. Va. Aug. 16, 2021) ("Because there is fair ground for doubt concerning the requirements of the 2017 Plan and related disbursements, the record does not warrant a finding of contempt"); *In re Jeong*, 2020 WL 1277575 (B.A.P. 9th Cir. Mar. 16, 2020) (applying the *Taggart* standard in upholding a bankruptcy court order granting a chapter 7 trustee's request for contempt sanctions for a willful violation of the stay); *In re GL Master Inc*., 2022 WL 34686, *2 (Bankr. C.D. Cal. Jan. 3, 2022) (applying the *Taggart* standard in ordering contempt sanction for willful and repeated violations of discovery orders); *In re GYPC, INC.*, 634 B.R. 983, 991 (Bankr. S.D. Ohio 2021) ("The court will apply the *Taggart* standard in determining whether any stay violations committed by Eastport entitle GYPC to damages under a civil contempt theory"); *Tate v. Fairfax Village I Condominium*, 2020 WL 634293 (Bankr. D.D.C. Feb. 10, 2020) (citing *Taggart* in finding a willful violation of the stay in a chapter 13 case and imposing sanctions under section 362(k)(1) of the Bankruptcy Code). *But see In re Franklin*, 614 B.R. 534, 546 n.19 (Bankr. M.D.N.C. 2020) (in a chapter 13 case involving a request for automatic stay violation sanctions under section 362(k), noting the distinction between a discharge injunction and the automatic stay and stating that "[e]ven if the standard in *Taggart* applied to § 362(k), no reasonable creditor objectively could have believed [the creditor's] actions in this case did not violate the automatic stay"); *In re Spiech Farms, LLC*, 603 B.R. 395, 408 n.22 (Bankr. W.D. Mich. 2019) (in a chapter 7 case, stating that "[t]his court does not read *Taggart* to change the Sixth Circuit's standard for determining whether a creditor can be held in contempt for violating the automatic stay"); *see also Fid. & Deposit Co. of Maryland v. TRG Venture II, LLC*, 2022 WL 952737, *2 n.1 (N.D. Ill. Mar. 30, 2022) (declining to address whether the *Taggart* standard should apply to contempt for violation of an injunction in a chapter 11 plan and a confirmation order where the issue was not raised on appeal).

GRAVEL

Gravel involved debtors in three separate chapter 13 cases filed in the U.S. Bankruptcy Court for the District of Vermont and the company originating and servicing the home mortgages (the "originator") for all of those debtors. The originator repeatedly violated Rule 3002.1 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"), which requires a mortgage lender to file a notice itemizing all fees, expenses, or charges incurred in connection with a mortgage during a bankruptcy case.

In two of the three Vermont cases, the bankruptcy court had entered an order (a "current order") declaring that the debtors were current on all pre- and post-bankruptcy payments, fees, and charges. Less than a month after the court issued the current orders, however, the originator began listing in the debtors' statements fees allegedly incurred during the periods encompassed by the orders, but did not include those fees in the amounts due. In those two cases, the originator had not filed the notices required by Bankruptcy Rule 3002.1. There was no current order in the third case, but the originator listed fees in that debtor's statements (but did not include the fees in the amount due), without filing a Bankruptcy Rule 3002.1 notice.

For violating the rule, the bankruptcy court imposed $75,000 (i.e., $1,000 for each of the 25 violations in all three cases) in sanctions under Bankruptcy Rule 3002.1. In addition, invoking its "authority . . . to impose punitive sanctions on parties who violate court orders," the court imposed a total of $300,000 in sanctions for violation of the two current orders. Reasoning that it "may hold a creditor in contempt for that party's violation of an injunction order," the court applied the *Taggart* contempt standard and "impos[ed] punitive sanctions" on the originator for its violation of the orders.

The district court reversed on appeal, ruling that the $375,000 in sanctions exceeded the bankruptcy court's "statutory and inherent powers." The district court remanded the case to the bankruptcy court, which later imposed the same $75,000 in sanctions for violating Bankruptcy Rule 3002.1, but reduced the punitive sanctions for violating the current orders to $225,000.

The Second Circuit granted the originator's request for a direct appeal of the second sanctions order. A divided three-judge panel of the Second Circuit vacated and reversed the second sanctions order.

Initially, the majority explained that a bankruptcy court's "narrowly circumscribed" contempt power derives from a court injunction—an equitable remedy—and section 105(a) of the Bankruptcy Code, which authorizes the court to issue "any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]."

The majority concluded that the originator "did not, as a matter of law, violate" the current orders because those orders specifically prohibited the originator "from disputing that the debtors are current (as set forth herein) in any other proceeding" but "did not enjoin the recording of expired fees on the statements" sent to the debtors. *Gravel*, 6 F.4th at 511.

In so ruling, the majority applied the contempt standard established in *Taggart*. "Without an express injunction [barring the

originator from sending out statements reflecting expired fees],” the majority wrote, there was a “fair ground of doubt as to whether the listed fees can form the basis for contempt.” *Id.* According to the majority, the bankruptcy court “could have crafted an order that would have forbidden the conduct” at issue. *Id.* at 513.

The majority also held that the $75,000 sanction for failure to file Bankruptcy Rule 3002.1 notices “went beyond the relief authorized by that rule,” and that, given the absence of any finding of bad faith below, it was “dubious” whether the bankruptcy court “could exercise its inherent power to do that which is unavailable under powers expressly defined” in Bankruptcy Rule 3002.1. *Id.* at 516.

The dissent agreed with the majority's holding that the current orders “did not clearly and unambiguously prohibit” the originator's conduct for which the bankruptcy court imposed $225,000 in sanctions, but disputed vacatur of the $75,000 sanction, reasoning that either Bankruptcy Rule 3002.1 or the bankruptcy court's inherent powers authorized the sanction.

On April 4, 2022, the chapter 13 trustee filed a petition seeking U.S. Supreme Court review of the Second Circuit's decision. The Supreme Court denied the petition on June 13, 2022. *See Sensenich v. PHH Mortgage Corp.*, No. 21-1322 (U.S. June 13, 2022).

BECKHART

In August 2009, Gordon and Stella Beckhart (the “debtors”) filed for chapter 11 protection in the Eastern District of North Carolina. At the time of the bankruptcy filing, the debtors were in arrears to the tune of nearly $23,000 under a loan secured by real property owned by them in North Carolina.

The debtors proposed a chapter 11 plan under which the mortgage loan would be reinstated. The servicer of the loan (together with its successor, the “servicer”) objected to the plan, stating that it failed to make any provision for the payment of prepetition arrearages or the application of postpetition principal or interest payments. The servicer also voted to reject the plan, but the bankruptcy court confirmed the plan over its objection.

The confirmation order provided that, “[e]xcept as modified herein, the [debtors] shall continue to pay the creditor's claim according to the original loan terms.” The order specified the date on which the first payment would be due after confirmation, but did not state the amount or how it would be calculated. The order also provided that, in the event of a default, the debtors would be entitled to 10 days' written notice before the lender could exercise its state court remedies with respect to the property. The servicer did not appeal the confirmation order.

The debtors began making the monthly payments on the date specified in the confirmation order and continued to do so in accordance with the terms of the mortgage. Nearly four years after confirmation of the plan, the servicer informed the debtors that their account was past due in the amount of approximately $50,000. After several attempts to resolve the dispute over the course of the next five years failed, the servicer served the debtors with a notice of foreclosure in January 2020.

The debtors then filed a motion in the bankruptcy court for civil contempt and sanctions against the servicer and the lender (collectively, the “defendants”). After an evidentiary hearing, the bankruptcy court entered an order finding the defendants to be in civil contempt and directing them to pay monetary sanctions in the amount of approximately $115,000 to the debtors.

The defendants appealed the contempt order to the district court, which reversed. According to the district court, the defendants "established a fair ground of doubt with regard to the unclear terms of the confirmation order, and the bankruptcy court's contempt order falls far short of meeting the *Taggart* standard for imposing the serious finding of civil contempt against appellants." *Newrez, LLC v. Beckhart*, 2021 WL 3361707, *2 (E.D.N.C. July 6, 2021), *vacated and remanded*, 31 F.4th 274 (4th Cir. 2022). Notably, the district court stated:

> The Court is not convinced by [the debtors'] argument that the discharge order referenced in *Taggart* is different from the confirmation order at issue here, thus making the case inapplicable here. Regardless of the name of the document, both orders concern payment or repayment with regards to the declaration of bankruptcy and an outstanding amount owed at the time of the filing, and the similarities between the documents far outweigh the differences.

Id. According to the district court, the confirmation order was confusing because it did not expressly address what amount the debtors would owe on the loan as of the confirmation date or how the pre- and postpetition arrearages would be repaid, if at all. In addition, the court noted, by adopting a reading that seemed consistent with the contractual terms of the loan and that was objectively reasonable, the defendants acted in good faith. Finally, the district court stated that the defendants "were repeatedly advised by counsel that they could collect the amounts due from appellees under the original mortgage contract." *Id.* at *3.

The debtors appealed to the Fourth Circuit.

THE FOURTH CIRCUIT'S RULING

A three-judge panel of the Fourth Circuit held that the standard adopted in *Taggart* applies when a court is considering whether to hold a creditor in civil contempt for violating a chapter 11 plan of reorganization. Because it concluded that neither the bankruptcy court nor the district court properly applied the *Taggart* standard, the panel vacated the district court's ruling and remanded the case below.

Writing for the panel, U.S. Circuit Court Judge Toby Heytens explained that, because the Supreme Court's analysis was based on "traditional principles of equity practice" that have "long governed how courts enforce injunctions," the scope of *Taggart* is clearly not limited to violations of chapter 7 discharge orders and "governs civil contempt under Chapter 11 of the Bankruptcy Code as well." *Beckhart*, 31 F.4th at 277 (citations omitted). He acknowledged that chapter 11 reorganizations differ in many ways from chapter 7 liquidations but wrote that "a bankruptcy court's authority to enforce its own orders—regardless of which chapter of the Bankruptcy Code those orders were issued under—derives from the same statutes and the same general principles the Supreme Court relied on in *Taggart*." *Id.* at *3.

According to Judge Heytens, the bankruptcy court did not apply the *Taggart* standard at all but, rather, a four-factor test for civil contempt articulated in a Fourth Circuit nonbankruptcy decision that long predated *Taggart*. The Fourth Circuit panel went on to state that the district court misapplied the *Taggart* standard in overturning the bankruptcy court's contempt order. In particular, the district court erroneously granted controlling weight to the defendants' reliance on the advice of counsel as a sufficient defense to civil contempt. According to Judge Heytens, this is contrary to long-standing Fourth Circuit law as well as the Supreme Court's statement in *Taggart* that "'[t]he absence of willfulness does not relieve from civil contempt.'" *Id.* (quoting *Taggart*, 139 S. Ct. at 1802). Judge Heytens noted, however, that "while relying on the advice of outside counsel is not a complete defense in and of itself, it may still be considered in appropriate circumstances as a relevant factor under the *Taggart* standard." *Id.* at *3 n.*.

Having concluded that both lower courts "erred in analyzing the threshold question of whether [the defendants] may be held in civil contempt at all," the Fourth Circuit held that the district court's ruling should be vacated and the case should be remanded to the bankruptcy court "to reconsider the contempt motion under the correct legal standard." *Id.*

OUTLOOK

In *Gravel* and *Beckhart*, two circuit courts of appeals appear to have definitively answered a major question left unanswered by *Taggart*—namely, whether the "fair ground of doubt" standard applies to contempt for violation of bankruptcy court orders other than orders discharging chapter 7 debtors. Other lower courts have also adopted this expansive interpretation of *Taggart*. By declining to review the Second Circuit's ruling in *Gravel*, the Supreme Court passed up the opportunity to weigh in on the issue.

JUDGMENT CLAIM AND LIEN SECURING IT WERE PROPERLY SUBORDINATED UNDER SECTION 510(B) OF THE BANKRUPTCY CODE

Oliver S. Zeltner • Mark G. Douglas

Section 510(b) of the Bankruptcy Code provides a mechanism designed to preserve the creditor/shareholder risk allocation paradigm by categorically subordinating claims asserted against a debtor by equity holders arising from the purchase or sale of securities of the debtor or an affiliate of the debtor. The purpose of this provision is to ensure that creditors are paid before equity holders, including in situations where an equity holder asserts a claim for damages related to the purchase or sale of the debtor's (or an affiliate's) stock. Section 510(b) implicitly recognizes that, as compared with creditors, equity holders bargained for potentially greater returns in exchange for greater risk, and it is designed to preserve that risk allocation between creditors and shareholders in bankruptcy. However, courts do not always agree on the scope of the provision in attempting to implement its underlying policy objectives.

A bankruptcy appellate panel for the Ninth Circuit ("BAP") recently examined this issue in *Kurtin v. Ehrenberg (In re Elieff)*, 637 B.R. 612 (B.A.P. 9th Cir. 2022). The panel affirmed a bankruptcy court order categorically subordinating secured judgment claims asserted against the debtor by an individual with whom the debtor co-owned certain investments. The BAP agreed with the bankruptcy court that the claims, although transformed into a secured judgment, were for damages arising from the purchase or sale of the securities of the debtor or an affiliate and were therefore properly subordinated under section 510(b). The BAP further held that the liens securing the claims should also have been subordinated under section 510(b).

SUBORDINATION IN BANKRUPTCY

The concept of claim, debt, or lien subordination is well recognized under federal bankruptcy law. A bankruptcy court's ability to reorder the relative priority of claims or debts under appropriate circumstances is part and parcel of its broad powers as a court of equity. The statutory vehicle for applying these powers in bankruptcy is section 510 of the Bankruptcy Code.

Section 510(a) makes an otherwise valid contractual subordination agreement enforceable in a bankruptcy case to the same extent that it would be enforceable outside bankruptcy.

Section 510(b) generally subordinates claims arising from the purchase or sale of a security of the debtor or an affiliate of the debtor to all claims that are senior or equal to the claim or interest represented by the security.

Finally, section 510(c) provides that misconduct that results in injury to creditors or shareholders can, "[n]otwithstanding subsections (a) and (b) of this [section 510]," result in the "equitable" subordination of a claim or interest or the issuance of an "order that any lien securing such a subordinated claim be transferred to the estate."

SUBORDINATION OF CLAIMS UNDER SECTION 510(B)

Section 510(b) provides as follows:

> For the purpose of distribution under this title, a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under section 502 on account of such a claim, shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security, except that if such security is common stock, such claim has the same priority as common stock.

The purpose of section 510(b), consistent with the Bankruptcy Code's "absolute priority" rule, is to prevent the bootstrapping of equity interests into claims that are on a par with other creditor claims. According to this rule, unless creditors are paid in full or agree otherwise, shareholders cannot receive any distribution from a bankruptcy estate. *See generally* Collier on Bankruptcy ¶ 510.04[1] (16th ed. 2022).

Interest holders have resorted to a wide array of devices and/or legal arguments in an effort to overcome the effect of section 510(b), including contractual provisions purporting to entitle them to damages upon the issuer's breach of a stock purchase agreement and alternative theories of recovery, such as unjust enrichment and constructive trust. *See generally Stucki v. Orwig*, 2013 WL 1499377 (N.D. Tex. Apr. 12, 2013) (discussing case law).

In deciding cases under section 510(b), some courts have highlighted the traditional allocation of risk between a company's shareholders and its creditors. Under this policy-based analysis, shareholders are deemed to undertake more risk in exchange for the potential to participate in the profits of the company, whereas creditors can expect only repayment of their fixed debts. Accordingly, shareholders, and not creditors, assume the risk of a wrongful or unlawful purchase or sale of securities. This risk allocation model is sometimes referred to as the "Slain/Kripke theory of risk allocation," as described in a 1973 law review article written by Professors John J. Slain and Homer Kripke titled "The Interface Between Securities Regulation and Bankruptcy—Allocating the Risk of Illegal Securities Issuance Between Securityholders and the Issuer's Creditors," 48 N.Y.U. L. Rev. 261 (1973). *See, e.g., In re SeaQuest Diving LP*, 579 F.3d 411, 420 (5th Cir. 2009); *In re Betacom of Phoenix, Inc.*, 240 F.3d 823, 829 (9th Cir. 2001); *In re Granite Partners, L.P.*, 208 B.R. 332, 336 (Bankr. S.D.N.Y. 1997).

Because of the parties' differing expectations for risk and return, it is perceived as unfair to allow a shareholder to recover from the limited assets of a debtor as a creditor by "converting" its equity stake into a claim through the prosecution of a successful securities lawsuit. The mechanism by which such a conversion is thwarted is subordination of the shareholder's claim under section 510(b).

Notwithstanding general agreement regarding the policy underlying section 510(b), many courts have found the statutory language to be ambiguous. *See SeaQuest*, 579 F.3d at 421. In *In re Am. Hous. Found.*, 785 F.3d 143 (5th Cir. 2015), the Fifth Circuit concluded that a claim should be subordinated under section 510(b) if: (i) the claim is for "damages"; (ii) the claim involves "securities"; and (iii) the claim "arise[s] from" a "purchase or sale." With respect to the third element, the court explained, "[f]or a claim to 'arise from' the purchase or sale of a security, there must be some nexus or causal relationship between the claim and the sale." *Id.* at 156 (quoting *SeaQuest*, 579 F.3d at 421) (internal quotation marks omitted). The Second Circuit applied a slightly different formulation of the test in *In re Lehman Bros. Holdings Inc.*, 855 F.3d 459, 472-78 (2d Cir. 2017), where it examined whether: (i) the claimant owns a security; (ii) the claimant acquired the security by means of a purchase or sale; and (iii) the claimant's damages arose from the purchase or sale of the security or the rescission of such a purchase or sale.

Section 101(49) of the Bankruptcy Code defines the term "security" broadly to "include" notes, stock, treasury stock, bonds, debentures, and an extensive catalogue of other investments. In addition, the definition contains a broad residual clause providing that a security also includes "any other claim or interest commonly known as [a] 'security.'" The scope of the residual clause is broad. *See SeaQuest*, 579 F.3d at 418.

The statutory definition also expressly excludes a number of items, including, among other things, currency, checks, drafts, bills of exchange, bank letters of credit, commodity futures contracts, forward contracts, options, and warrants.

Section 101(16) of the Bankruptcy Code defines an "equity security" to mean shares in a corporation or any "similar security," limited partnership interests, and certain warrants or rights.

In *Lehman Brothers*, the Second Circuit noted that "some interests will not perfectly match any of the specific examples in [the Bankruptcy Code's definition of security]," and that, should this be the case, it is of "most significance" that a claimant "ha[s] the same risk and benefit expectations as shareholders." *Lehman Brothers*, 855 F.3d at 473-74; *accord In re Linn Energy*, 936 F.3d 334, 344 (5th Cir. 2019) (even though the beneficiary of a stock trust did "not fit perfectly in the investor box," his claims should be subordinated under section 510(b) because his entitlement to "deemed dividends" originally arising from the trust "was certainly more like an investor's interest than a creditor's interest"); *In re WorldCom, Inc.*, 2006 WL 3782712, at *6 (Bankr. S.D.N.Y. Dec. 21, 2006) ("The form in which the equity interest is held is ultimately irrelevant. So long as the claimant's interest enabled him to participate in the success of the enterprise and the distribution of profits, the claim will be subordinated pursuant to section 510(b).").

The Bankruptcy Code does not define "damages." However, many courts have reasoned that "the concept of damages under Section 510(b) has the connotation of some recovery *other than* the simple recovery of an unpaid debt due on an instrument." *American Housing*, 785 F.3d at 153-54 (internal quotation marks omitted) (citing cases and ruling that claims seeking compensation for fraud or breach of fiduciary duty are claims for damages under section 510(b) as well as claims "predicated on post-issuance conduct," including breach of contract claims).

ELIEFF

Beginning in the early 1990s, Bruce Elieff (the "debtor") and Todd Kurtin ("Kurtin") were partners or joint venture owners in a series of real estate investment and development projects in California (the "joint entities"). In 2003, Kurtin sued the debtor and certain separately owned entities in state court asserting claims for breach of contract, breach of fiduciary duty, conversion, embezzlement, constructive fraud, and related claims. The parties settled the litigation in 2005. Under the settlement agreement, Kurtin agreed to surrender his interests in the joint entities to the debtor in exchange for approximately $50 million payable in four installment during the next year. The debtor and the joint entities were liable for the initial $21 million installment, but only the joint entities were liable for the remainder.

The settlement agreement granted Kurtin a lien on the projects owned by the joint entities to secure the settlement payment obligation. It also prohibited the debtor from taking any distribution from the any of the joint entities if it would prevent the joint entities from paying the settlement debt. In the event of a default,

Kurtin was entitled to a judgment from the state court against the joint entities in the amount of the payment shortfall. The settlement agreement provided that any disputes regarding its terms were subject to arbitration.

After the joint entities defaulted on the third installment, Kurtin sought entry of a judgment against them in the amount of $22.5 million, but the court denied the request because the joint entities were not parties to the state court litigation.

Kurtin commenced an arbitration proceeding seeking reformation of the settlement agreement to add "material terms." The arbitrator ruled that the agreement should be amended to provide that, if the default was not cured by June 30, 2007, the debtor was obligated to transfer his interests in the joint entities to Kurtin. However, Kurtin never elected to enforce the provision.

Instead, in December 2007, Kurtin commenced a second lawsuit in state court against the debtor and the joint entities for breach of the settlement agreement and approximately $25 million in damages. Among other claims, the complaint alleged that the debtor breached the settlement agreement by taking distributions from the joint entities even though they failed to make the last installment payment.

A jury awarded Kurtin approximately $25 million. The award was later increased to nearly $34 million after a series of appeals and a new trial. In September 2019, Kurtin recorded his judgment against the debtor and two entities that the state court adjudged to be his alter egos.

In October 2019, the debtor and various affiliates (other than the joint entities) filed separate chapter 11 cases in the Central District of California. The following month, the debtor commenced an adversary proceeding against Kurtin seeking, among other things, subordination of his secured claims under section 510(b), transfer of Kurtin's judgment liens to the estate under section 510(c)(2), and avoidance of Kurtin's lien as a preferential and fraudulent transfer. Kurtin moved to dismiss.

The bankruptcy court declined to dismiss the debtor's subordination claims under section 510(b) and his avoidance claims. However, it dismissed the section 510(c)(2) claim, ruling that section 510(c)(2) does not apply to claims subordinated under section 510(b), but only to claims equitably subordinated under section 510(c)(1).

According to the bankruptcy court:

> [T]he plain language of § 510(c)(2) does not support Plaintiffs' interpretation that the lien transfer provision of § 510(c)(2) applies to § 510(b). Significantly, § 510(b), which governs mandatory subordination *includes its own remedy* within the subjection, to wit, for distribution purposes, "a claim arising from damages from the purchase or sale of a security . . . *shall be subordinated to all claims or interests that are senior . . .*" § 510(b) (emphasis added). Section 510(c), therefore, cannot logically be read as providing both a duplicative remedy (subordination for distribution purposes) and an extra remedy (lien transfer) for § 510(b) claims.

Elieff v. Kurtin (In re Elieff), No. 19-ap-01205-ES (Bankr. C.D. Cal. Jan. 26, 2021), at pp. 28-29.

In June 2020, the bankruptcy court substantively consolidated the cases and appointed a chapter 11 trustee. The court later converted the case to a chapter 7 liquidation.

After conversion, the bankruptcy court considered Kurtin's motion for summary judgment on the remaining claims stated in the complaint (now being prosecuted by the chapter 7 trustee) complaint. Kurtin argued that most of the rights and obligations exchanged under the settlement agreement had little or nothing to do with his transfer of interests in the joint entities to the debtor and that, because the value of the joint entities was less than the debtor's initial $21 million settlement payment, none of the other installment payments had anything to do with the purchase or sale of securities within the meaning of section 510(b). However, he never submitted any evidence to support this allocation.

In January 2021, the bankruptcy court granted summary judgment to the trustee on the section 510(b) claim. It ruled that the plain terms of the settlement agreement established that the "crux" of the agreement involved the purchase and sale of securities of the debtor's affiliates (the joint entities) and that section 510(b) applied, even if some aspects of the agreement did not directly relate to the purchase or sale of securities. According to the court, section 510(b) relief is triggered whenever there is "some nexus" or "causal relationship" between the claim and the purchase or sale of securities of the debtor or its affiliates.

The bankruptcy court later clarified its ruling by issuing an order providing that, because Kurtin's judgment liens were "subsumed" within the term "claim" in section 510(b), the liens were subordinated for the same reasons and to the same extent that his claims had been subordinated. According to the bankruptcy court, "[b]oth the Kurtin Claim and the Kurtin Liens are subordinated by this relief because the term 'claim' referenced in § 510(b) includes both unsecured and secured, i.e., *in rem* lien rights to payment." *Elieff v. Kurtin (In re Elieff)*, No. 19-ap-01205-ES (Bankr. C.D. Cal. Apr. 5, 2021) (citing 11 U.S.C. §§ 101(5) and 510(b); *Johnson v. Home State Bank*, 501 U.S. 78, 84 (1991)).

Kurtin appealed to the BAP.

THE BANKRUPTCY APPELLATE PANEL'S RULING

The BAP affirmed.

Subordination of Claims. Writing for the panel, U.S. Bankruptcy Judge Gary A. Spraker emphasized that the Ninth Circuit has broadly interpreted the scope of section 510(b). *Elieff*, 637 B.R. at

622 (citing *Liquidating Tr. Comm. of the Del Biaggio Liquidating Tr. v. Freeman (In re Del Biaggio)*, 834 F.3d 1003, 1009 (9th Cir. 2016); *Pensco Tr. Co. v. Tristar Esperanza Props., LLC (In re Tristar Esperanza Props., LLC)*, 782 F.3d 492, 495 (9th Cir. 2015)). In *Del Biaggio*, he noted, the Ninth Circuit held that a claim "arises from" the purchase or sale of securities whenever it "shares a 'nexus or causal relationship' with the purchase or sale of securities." *Id.* (citing *Del Biaggio*, 834 F.3d at 1009).

According to the BAP, there were no material differences between this case and *Tristar*. In *Tristar*, Judge Spraker explained, one member of a limited liability company ("LLC") sought to withdraw from the LLC, and the other member invoked its right to purchase the membership interest, but the parties could not agree on its value. After arbitration, the prevailing member reduced its award to judgment in state court. The other member filed for chapter 11 bankruptcy and sought an order subordinating the judgment claim under section 510(b). The Ninth Circuit ultimately ruled that the claim should be subordinated because the claim "originat[ed] from the failed sale of [the] membership interest and [the other member's] breach of the operating agreement's provisions regarding repurchase of membership interests." *Tristar*, 782 F.3d at 497.

As in *Tristar*, Judge Spraker wrote, "Kurtin's claim[s] based on Elieff's breach of [the settlement agreement] share[] a direct causal link with the conveyance of his equity interests in the Joint Entities," and therefore the bankruptcy court correctly subordinated the claims under section 510(b). *Elieff*, 637 B.R. at 623. In so ruling, the BAP rejected Kurtin's argument that section 510(b) did not apply because his claims arose from Elieff's post-settlement diversion of the assets of the joint entities. Kurtin's judgment, Judge Spraker explained, "was based on Elieff's breach of the Settlement Agreement . . . [and thus,] it shared a direct causal link to Kurtin's sale of his interests in the Joint Entities made in that very same agreement." *Id.*

The BAP also rejected Kurtin's argument that, because the initial $21 million installment payment under the settlement agreement "fully paid the securities sale aspect" of the agreement, Kurtin's judgment claims for the remaining installments "cannot constitute damages that arise from the sale of his securities under § 510(b)." According to Judge Spraker, the plain language of the settlement agreement indicated no "distinction of purpose between any of the Settlement Payments" or that the payments "were severable rather than indivisible." *Id.* at 624.

Subordination of Liens. Next, the BAP ruled that the bankruptcy court properly subordinated Kurtin's judgment liens as well as his claims under section 510(b).

According to the panel, in keeping with its purpose to prevent an equity investor from sharing *pari passu* with creditors based on "transmutation of its investment from equity to debt whether consensually or by a court ruling, . . . [s]ection 510(b) subordinates the entirety of a claim, including the creditor's *in rem* right to payment." This, Judge Spraker noted, is consistent with section 101(5) of the Bankruptcy Code, which defines "claim" to include "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." *Id.* at 626-27. He further explained that this conclusion also comports with the Supreme Court's ruling in *Johnson*, where the Court held that the term "claim" in the Bankruptcy Code includes mortgage liens.

According to the BAP, Kurtin's narrow reading of section 510(b) would "lead to incongruous if not absurd results" because the retention of his lien priority would allow him to be paid ahead of the claims of the unsecured creditors to which his claims had been subordinated. "In short," Judge Spraker wrote, "§ 510(b) statutorily precludes Kurtin from collecting his damages until the unsecured creditors are paid." *Id.* at 627.

The BAP noted that its rationale does not conflict with other provisions of the Bankruptcy Code, including sections 725 and 726. Section 725 provides that, before a final distribution of estate property under section 726, the trustee "shall dispose of any property in which an entity other than the estate has an interest, such as a lien, and that has not been disposed of under another section of [the Bankruptcy Code]." Section 726 provides that, "[e]xcept as provided in section 510," property shall be distributed in accordance with the five categories of claims and the residual debtor's interest set forth in the provision. According to the panel, the legislative history of section 725, which gives bankruptcy courts broad authority to order "dispositions" of estate property in which third parties hold interests or liens, indicates that section 725 was enacted by lawmakers "'in lieu of a section that directs a *certain distribution to secured creditors*.'" *Id.* (quoting H.R. Rep. No. 95-595, 382-83 (with emphasis added)). Thus, the BAP noted, section 725 "is explicitly subject to the mandatory effect of subordination under the plain language of § 510(b)." *Id.*

The BAP also found no conflict between section 510(b) and section 725. The latter statute, he explained, obligates the trustee to dispose of encumbered property prior to the *final* distribution of estate property under section 726 only. Judge Spraker noted that, in this case, the estate was not ready for final distribution, and it appeared that the trustee sought subordination of Kurtin's liens so that he could liquidate the encumbered assets under section 363(f) (allowing a sale free and clear of any interest) and section 506(d) (voiding liens securing claims that are not allowed, with certain exceptions). According to the BAP, if the trustee did not administer the encumbered assets, they would be disposed of prior to the estate's final distribution. Thus, it reasoned, subordinating Kurtin's liens would not violate section 725. *Id.* at 628.

The BAP also rejected Kurtin's argument that, because section 510(c)(2) specifically authorizes the court to transfer a "lien" securing an equitably subordinated claim to the estate, whereas section 510(b) refers only to subordination of a "claim," Congress did not intend for subordination of liens under section 510(b). According to Judge Spraker, "[l]ien transfer is a

remedy distinct from lien subordination . . . and lien subordination under § 510(b) — and § 510(c)(1) — is nothing more than a recognition of the well-established proposition that a lien is an incident of the debt." *Id.*

In addition, the BAP rejected Kurtin's argument that interpreting section 510(b) to provide for lien subordination conflicts with the principle that liens generally pass through bankruptcy unaffected. In chapter 5 of the Bankruptcy Code alone, Judge Spraker explained, there are numerous provisions "that can drastically affect lien rights," indicating that Congress departed from this principle "when it perceive[d] a need and justification to affect such rights." *Id.* (citing 11 U.S.C. §§ 506(c), 506(d), 522(f), and 548). Given its conclusion that Congress intended for section 510(b) to extend to lien subordination, the BAP also found no merit to the contention that subordinating Kurtin's liens violated his due process rights.

Finally, the BAP rejected Kurtin's contention that, because the bankruptcy court did not avoid but merely subordinated his liens, any distribution of the proceeds of his collateral to other creditors would still be subject to his liens. This contention, the panel noted, ignores the fact that the bankruptcy court did not need to avoid Kurtin's subordinated liens because his claims were not entitled to payment from any source until unsecured creditors were paid in full.

OUTLOOK

The BAP's conclusion in *Elieff* that Kurtin's judgment claims were properly subordinated as claims for damages arising from the purchase or sale of the securities of the debtor's affiliates reinforces the broad scope of section 510(b), in keeping with its purpose to prevent the bootstrapping of equity interests into claims that are on a par with the claims of creditors. Given Kurtin's status as an interest holder and the nature of the dispute, the fact that he took the additional steps to transform his claims into secured judgment debts was irrelevant, and the BAP accordingly held that the claims retained their original priority on a par with equity interests.

The BAP's analysis concerning subordination of liens, as distinguished from claims, under section 510(b) is noteworthy, particularly because only a handful of other courts have addressed the issue in reported decisions, and none has explained its reasoning in such detail. *See, e.g., In re Barkats*, 2019 WL 3934799, at **7-8 (Bankr. D.D.C. Aug. 16, 2019) (unlike section 510(c), section 510(b) does not provide for the subordination of a lien); *In re JTS Corp.*, 305 B.R. 529, 546 (Bankr. N.D. Cal. 2003) (denying summary judgment and noting that "it appears that the Amber Group's assertion of its lien rights seeks to retrieve an investment loss and should be subordinated under § 510(b)").

The BAP's reasoning concerning the inseparability of a claim and a lien securing it and the consequences of *not* subordinating the lien securing a claim subordinated under section 510(b) would appear to be sound. If a lien securing a subordinated claim were unaffected by the claim's subordination, the creditor would still have a superior interest in its collateral vis-à-vis the creditors that section 510(b) was intended to benefit.

Moreover, if section 510(b) were not interpreted to provide for the subordination of a lien as well as the claim it secures, it is unclear what mechanism the trustee could rely on to subordinate or avoid the lien and fulfill section 510(b)'s purpose. The Bankruptcy Code's provisions dealing with the avoidance of liens do not contemplate avoidance under the circumstances addressed by section 510(b). *See* 11 U.S.C. §§ 506(d) (avoidance of claims that secure certain disallowed claims); 522(f) (avoidance of judicial liens on and nonpossessory nonpurchase money security interests in certain exempt property); 544(a)(1) (avoidance of liens that are voidable under applicable nonbankruptcy law); 545 (avoidance of certain statutory liens); 548 (avoidance of obligations incurred with actual or constructive fraud); and 724(a) (avoidance of liens securing certain fines, penalties, or forfeitures, or for multiple, exemplary, or punitive damages that are not compensation for actual pecuniary loss).

The BAP's conclusion, therefore, seems reasonable. Even so, we are left to speculate why Congress specifically mentioned liens in providing for equitable subordination in section 510(c)(2), yet omitted to do so in connection with categorical subordination under section 510(b).

FIRST CIRCUIT DEEPENS SPLIT ON WAIVER OF TRIBAL SOVEREIGN IMMUNITY IN BANKRUPTCY

Charles M. Oellermann • Mark G. Douglas

Recognized Native American tribes generally have inherent authority to govern themselves without interference by federal or state governments. An important element of this "tribal sovereignty" is immunity from lawsuits in federal, state, and tribal courts, or "tribal sovereign immunity." Under this principle, a tribe may be sued only if the tribe consents to being sued or if Congress has authorized such a suit. Otherwise, a court lacks subject matter jurisdiction over a tribe.

Whether Congress has authorized a waiver of tribal sovereign immunity in bankruptcy cases is disputed among the federal circuit courts of appeals. The U.S. Court of Appeals for the First Circuit recently deepened this split. In *Coughlin v. Lac du Flambeau Band of Lake Superior Chippewa Indians (In re Coughlin)*, 33 F.4th 600 (1st Cir. 2022), a divided First Circuit panel ruled as a matter of first impression that section 106(a) of the Bankruptcy Code expressly provides for a waiver of tribal sovereign immunity.

In so ruling, the First Circuit sided with the Ninth Circuit, which held in 2004 that section 106(a) abrogates tribal sovereign immunity. *See Krystal Energy Co. v. Navajo Nation*, 357 F.3d 1055, 1058 (9th Cir. 2004) ("[Ruling that, in sections 101(27) and 106(a),] Congress explicitly abrogated the immunity of any 'foreign or domestic government.' Indian tribes are domestic governments. Therefore, Congress expressly abrogated the immunity of Indian tribes."). However, the First Circuit rejected the contrary view

expressed by the Sixth Circuit in *In re Greektown Holdings, LLC*, 917 F.3d 451, 460-61 (6th Cir. 2019) (Congress did not unequivocally express an intent to abrogate Indian tribes' sovereign immunity from bankruptcy avoidance litigation even though tribes might possess the characteristics of domestic governments), *cert. dismissed sub nom. Buchwald Cap. Advisors LLC v. Sault Ste. Marie Tribe*, 140 S. Ct. 2638 (2020).

According to the First Circuit majority, "Like the Ninth Circuit, we hold that the Bankruptcy Code unequivocally strips tribes of their immunity."

The widening circuit split may be a compelling invitation to U.S. Supreme Court review.

WAIVER OF SOVEREIGN IMMUNITY IN THE BANKRUPTCY CODE

Section 106(a) of the Bankruptcy Code provides that a "governmental unit" is deemed to waive sovereign immunity in connection with disputes relating to many provisions of the Bankruptcy Code, including actions to enforce the automatic stay, preference, and fraudulent transfer avoidance actions and proceedings seeking to establish the dischargeability of a debt.

Furthermore, pursuant to section 106(b) of the Bankruptcy Code, a governmental unit that files a proof of claim in a bankruptcy case "is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which the claim of such governmental unit arose."

Section 101(27) of the Bankruptcy Code defines the term "governmental unit" as:

> United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States (but not a United States trustee while serving as a trustee in a case under this title), a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government.

COUGHLIN

In July 2019, Brian W. Coughlin (the "debtor") took out a $1,100 payday loan from Niiwin, LLC, d/b/a Lendgreen ("Lendgreen"), an indirect subsidiary of the Lac Du Flambeau Band of Lake Superior Chippewa Indians (the "Band"). Later that year, the debtor filed a chapter 13 petition in the District of Massachusetts. In his bankruptcy schedules, the debtor listed his debt to Lendgreen, which had grown to nearly $1,600, as a nonpriority unsecured claim, and his attorney mailed Lendgreen a copy of the proposed chapter 13 plan.

Despite the automatic stay, Lendgreen repeatedly contacted the debtor seeking repayment of the debt. In an effort to stop those collection efforts, the debtor sought an order from the

bankruptcy court enforcing the automatic stay against both Lendgreen and its corporate parents, including the Band. In response, the Band and its affiliates asserted tribal sovereign immunity and moved to dismiss the enforcement proceeding. The bankruptcy court agreed with the Band and granted the motion to dismiss. The First Circuit permitted a direct appeal from that decision.

THE FIRST CIRCUIT'S RULING

A divided three-judge panel of the First Circuit reversed on appeal.

Writing for the majority, U.S. Circuit Judge Sandra L. Lynch explained that Congress may abrogate tribal sovereign immunity if it "'unequivocally' express[es] that purpose." *Coughlin*, 33 F.4th at 604 (citations omitted). In determining whether the Bankruptcy Code unequivocally abrogates tribal sovereign immunity, she wrote, "we begin with the text" of section 106(a), the plain language of which "satisfies Congress' obligation to unequivocally express its intent to abrogate immunity for all governmental units." *Id.* According to the majority, the question is whether lawmakers intended to abrogate tribal sovereign immunity when they used the phrase "governmental unit."

The First Circuit majority concluded that they did. First, Judge Lynch explained that there is no real disagreement that a tribe is a government—tribes are not expressly excluded and "fall within the plain meaning of the term governments." *Id.* at 605. Second, she noted, tribes are domestic, rather than foreign, in accordance with the ordinary dictionary definition of "domestic" as "belonging or occurring within the sphere of authority or control or the . . . boundaries of" the United States. *Id.* (quoting *Webster's Third New International Dictionary* 671 (1961)). Accordingly, the majority determined that a tribe is a domestic government and therefore a "governmental unit." Moreover, it noted, based on the legislative history and historical context of the issue, "when Congress enacted §§ 101(27) [in 1978] and 106 [in 1994], it understood tribes to be domestic governments, and when it abrogated the sovereign immunity of domestic governments in § 106, it unmistakably abrogated the sovereign immunity of tribes." *Id.* at 607.

The First Circuit majority rejected the argument that the term "domestic government" in section 101(27) refers only to governments that arose under the U.S. Constitution. Rather, Judge Lynch wrote, "domestic refers to the territory in which the government exists." *Id.* at *6. She further noted that an "interpretation of the phrase 'domestic government' that excludes Indian tribes with no textual basis for so doing is implausible." *Id.* at 611.

The First Circuit majority therefore reversed the decision of the bankruptcy court dismissing the debtor's motion to enforce the automatic stay and remanded the case below for further proceedings.

In a 33-page dissenting opinion, Chief Judge David A. Barron wrote that, by failing to use the word "tribes" in section 101(27), lawmakers "did not use the surest means of clearly and unequivocally demonstrating that [tribes] are" governmental units. *Id.* at 613 (dissenting opinion). According to Judge Barron, "Congress has expressly named them when abrogating their sovereign immunity in every other instance in which a federal court has found that immunity to have been abrogated." *Id.* Judge Barron accordingly wrote that he had "no choice but to conclude that § 101(27) does not clearly and unequivocally include Indian tribes, because, as I have explained, its text plausibly may be read not to cover them." *Id.* at 625.

NEWSWORTHY

At the Berkshire Hathaway annual shareholders' meeting on April 30, 2022, Berkshire Vice Chairman Charlie Munger selected as his "Pick for 2022" *The Caesars Palace Coup: How a Billionaire Brawl Over the Famous Casino Exposed the Power and Greed of Wall Street*, by Sujeet Indap and Max Frumes (2021). The book chronicles what it describes as "the most brutal corporate restructuring in Wall Street history," the "bankruptcy brawl for the storied casino giant, Caesars Entertainment." The book summarizes how a team of Jones Day lawyers across many areas of practice—led by Business Restructuring & Reorganization partner ***Bruce Bennett*** ***(Los Angeles and New York)***—achieved a historic victory for clients Oaktree Capital, Appaloosa Management, and other second-lien lenders, who saw their recoveries increase from less than 10 cents on the dollar to more than 66 cents on the dollar in "one of the great upset victories in the history of Wall Street." The increase in recovery for Jones Day's clients totaled more than $3 billion. *Caesars Palace Coup* describes in detail "the six-month sweep by the second-lien group who had, against all odds, prevailed on virtually every crucial issue in the case." Jones Day's team, legal strategies, and courtroom prowess in achieving that result feature prominently in the book.

The restructuring of Avianca, the Latin American airline, received the Restructuring Deal of the Year award from *Latin Lawyer* at its 2022 Deals of the Year ceremony. Avianca emerged from chapter 11 in December 2021 with a more efficient business model and eliminated debt worth more than US$1 billion. Avianca, founded in 1919, is the second-largest airline in Latin America and the largest in Colombia. It provides air travel and cargo services in Latin America and globally. A team of lawyers from Jones Day's Mexico City Office that included ***Arturo de la Parra*** ***(Financial Markets; Mexico City)*** and ***Mariana de Maria*** ***(Financial Markets; Mexico City)*** advised Avianca on Mexican law.

Roger Dobson ***(Sydney)*** and ***Katie Higgins*** ***(Sydney)*** were recognized in the practice areas Banking and Finance Law and Insolvency and Reorganization Law in the 2023 edition of *The Best Lawyers in Australia*.™ Roger was also recognized in the practice area Distressed Investing & Debt Trading Practice.

Heather Lennox ***(Cleveland and New York)*** and ***Corinne Ball*** ***(New York)*** were named "Leading Individuals" in the field of "Finance—Restructuring (including bankruptcy): corporate" in *The Legal 500 United States* 2022. Heather was also named a "Next Generation Partner" in the field "Finance: Restructuring (including bankruptcy): municipal."

Bruce Bennett ***(Los Angeles and New York)*** was named a "Hall of Fame" lawyer in the fields "Finance—Restructuring (including bankruptcy): corporate" and "Finance—Restructuring (including bankruptcy): municipal" in *The Legal 500 United States* 2022.

Dan T. Moss ***(Washington)***, ***Ben Larkin*** ***(London)***, and ***Barnaby C. Stueck*** ***(London)*** participated in the INSOL International June 2022 World Congress Meeting held in London June 26–28, 2022.

Ben Larkin ***(London)*** was recognized in the practice area Insolvency & Restructuring Law in the 2023 edition of *The Best Lawyers in the United Kingdom*.™

Corinne Ball ***(New York)*** was among the "Senior Statespeople" named in *Chambers USA* 2022 and *Chambers Global* 2022 in the field of Bankruptcy/Restructuring.

Bruce Bennett ***(Los Angeles and New York)*** was designated an "Eminent Practitioner" in the field of Bankruptcy/Restructuring in *Chambers Global* 2022.

Heather Lennox ***(Cleveland and New York)***, ***Bruce Bennett*** ***(Los Angeles and New York)***, ***Kevyn D. Orr*** ***(Washington)***, ***Gregory M. Gordon*** ***(Dallas)***, ***Paul M. Green*** ***(Houston)***, ***Carl E. Black*** ***(Cleveland)***, ***Daniel J. Merrett*** ***(Atlanta)***, ***Robert W. Hamilton*** ***(Columbus)***, ***Corinne Ball*** ***(New York)***, ***Thomas M. Wearsch*** ***(Cleveland)***, ***James O. Johnston*** ***(Los Angeles)***, ***Brad B. Erens*** ***(Chicago)***, ***Jeffrey B. Ellman*** ***(Atlanta)***, ***Dan T. Moss*** ***(Washington)***, and ***Charles M. Oellermann*** ***(Columbus)*** were recognized in the area of Bankruptcy/Restructuring in *Chambers USA* 2022.

An article written by ***Corinne Ball*** ***(New York)*** titled "Seventh Circuit Permits Prior Interest Holder To Challenge 'Free and Clear' Sale After the Fact" was published in the April 27, 2022, edition of the *New York Law Journal*.

An article written by ***Chares M. Oellermann*** ***(Columbus)*** and ***Mark G. Douglas*** ***(New York)*** titled "A Look at Finality in Substantially Consummated Ch. 11 Plans" was published in the June 14, 2022, issue of *Law360*.

An article written by ***Corinne Ball*** ***(New York)***, ***Brett P. Barragate*** ***(New York)***, ***I. Lewis H. Grimm*** ***(London)***, ***Heather Lennox*** ***(New York and Cleveland)***, ***Dan T. Moss*** ***(Washington)***, and ***Kevyn D. Orr*** ***(Washington)*** titled "Recent Trends in Corporate Debt and Reorganizations: Laying The Groundwork for Future Large Chapter 11 Cases or Just More Runway?" was published in Vol. 35, No. 2 of the *AIRA Journal* (June 2022).

An article written by ***Corinne Ball*** ***(New York)*** titled "Third Circuit Confirms that Bankruptcy Code Governs Retention of Debtor's Counsel and Recognizes that Bankruptcy Court Has Considerable Discretion" was published in the June 22, 2022, edition of the *New York Law Journal*.

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An article written by ***Oliver S. Zeltner*** ***(Cleveland)*** and ***Mark G. Douglas*** ***(New York)*** titled "Fifth Circuit Weighs in on Bankruptcy Asset Sales Free and Clear of Leasehold Interests" was published on May 3, 2022, in *Lexis Practical Guidance*.

An article written by ***Corinne Ball*** ***(New York)***, ***Dan T. Moss*** ***(Washington)***, ***Michael C. Schneidereit*** ***(New York)***, ***Isel M. Perez*** ***(Miami)***, and ***Mark G. Douglas*** ***(New York)*** titled "Florida District Court: Foreign Debtor Need Not Have U.S. Residence, Assets or Place of Business to Be Eligible for Chapter 15 Recognition" was published on May 3, 2022, in *Lexis Practical Guidance*.

An article written by ***Daniel J. Merrett*** ***(Atlanta)*** and ***Mark G. Douglas*** ***(New York)*** titled "Delaware Bankruptcy Court Rejects Use of Tax Code Look-Back Period in Avoidance Action" was published on May 3, 2022, in *Lexis Practical Guidance*.

An article written by ***Paul M. Green*** ***(Houston)*** and ***Mark G. Douglas*** ***(New York)*** titled "Fifth Circuit Rules that Chapter 11 Debtors May Reject Filed-Rate Contracts Without FERC Permission" was published on May 3, 2022, in *Lexis Practical Guidance*.

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