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Client Alert

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Egg On Their Face: Eleventh Circuit Dismisses Bankruptcy Appeal from Jefferson County Bankruptcy Plan Confirmation

The U.S. Court of Appeals for the Eleventh Circuit Court upheld a bankruptcy court's order retaining supervisory authority over Jefferson County, Alabama's sewer rates for the next forty years. Extending a line of cases holding that once a bankruptcy reorganization plan has been consummated, "the eggs are scrambled," the Eleventh Circuit held that the doctrine of equitable mootness warranted dismissal of the appeal. The Court suggested that the objecting parties should have expedited their appeal so that it could be heard before the plan became effective. The Eleventh Circuit's decision underscores the importance of obtaining a stay of the bankruptcy confirmation order and expediting the appeal before the plan is substantially consummated.

BACKGROUND AND BANKRUPTCY COURT DECISION

The case, styled *Andrew Bennett et al. v. Jefferson County, Alabama*, grew out of the financial meltdown of Alabama's most populous county during the Great Recession. Jefferson County had issued $3.2 billion in sewer-related debt instruments. Unable to afford payments on the debt, the County filed a Chapter 9 municipal bankruptcy case in 2011. After 18 months of negotiations with creditors, the County proposed a largely consensual reorganization plan that exchanged the $3.2 billion debt for a reduced amount of $1.8 billion in new sewer debt. In return for the write-down, Jefferson County agreed to phase in agreed-upon sewer rate increases over the next 40 years to pay off the new debt. The plan gave the bankruptcy court jurisdiction to adjudicate lawsuits relating to the county's implementation of the plan – including the provision requiring phased-in sewer rate increases – during that 40-year period.

A group of sewer ratepayers objected to the plan, arguing that it illegally gave the bankruptcy court the power to set sewer rates in Jefferson County for the next four decades. The bankruptcy court confirmed the plan and granted the County's unopposed request to waive the usual 14-day stay of

a plan confirmation order. Two days before the plan went into effect, the ratepayers filed an appeal of the bankruptcy court's order. They did not ask for a stay of the confirmation order pending appeal, nor did they ask the district court to expedite the appeal. On the day the plan became effective, the County issued the new sewer debt instrument in the reduced amount.

FIRST STOP: THE DISTRICT COURT REJECTS EQUITABLE MOOTNESS

At the U.S. District Court for the Northern District of Alabama, the County argued that the ratepayer's appeal should be dismissed because, among other things, the issue was moot: The plan went into effect as scheduled and the new, 40-year debt instruments had been issued to investors. The County invoked the doctrine of "equitable mootness," a judge-made rule under which appellate courts reject appeals of bankruptcy plans that have gone into effect and would be extremely hard to undo. Noting that the doctrine had not been widely applied in Chapter 9 municipal reorganization cases, the district court rejected the County's argument, but allowed the County to present its case to the Eleventh Circuit.

THE ELEVENTH CIRCUIT REFUSES TO UNSCRAMBLE THE EGGS

The Eleventh Circuit concluded that the plan had gone too far to be reversed at such a late date. Applying the doctrine of equitable mootness to a municipal Chapter 9 case for the first time, the court refused to create a black-letter rule. Instead, it articulated guidelines for lower courts to follow. It held that where third-parties rely on the bankruptcy court's unstayed plan; where the plan is complex and a long time has passed since confirmation; or where the objecting parties make no effort to promptly seek a stay to appeal, the less likely an appellate court will be to require "the pains that attend any effort to unscramble an egg."

In the *Jefferson County* case, the Eleventh Circuit noted that the ratepayers never asked for a stay of the plan's implementation while they appealed. Neither did they object to the County's motion to waive the automatic 14-day stay of a confirmation order. Nor did they ask to have their appeal expedited. "The County and others have taken significant and largely irreversible steps in reliance on the unstayed plan confirmed by the bankruptcy court," the court observed. If the bankruptcy court's rate supervisory authority were excised from the plan, there would be uncertainty over its provisions that could affect innocent investors in the new debt instruments, who invested their money more than a year before the case reached the Eleventh Circuit. The eggs had not just been scrambled; they had been cooked and largely eaten by the time the appeal was finally resolved.

WIDER IMPLICATIONS OF *JEFFERSON COUNTY* FOR BANKRUPTCY PARTIES

Jefferson County serves as a stark reminder to parties objecting to reorganization plans, whether corporate (Chapter 11), personal (Chapter 13), or municipal (Chapter 9): Time is of the essence, and vigilance in pursuing remedies is critical. To preserve appeal remedies against the doctrine of equitable mootness, a party should object to any waiver of the standard 14-day stay on appeal. It should seek a longer stay pending appeal, or ask the district court to expedite the appeal. Otherwise, the plan could be fully cooked, leaving the objecting party with egg on its face.

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