Asset Sales/Real Estate

Don't Restrict My Sale: The Enforceability of Restrictive Covenants and Easements in Asset Sales in Bankruptcy

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SALES FREE AND CLEAR OF NON-MONETARY INTERESTS IN REAL PROPERTY*

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Introduction

Sales free and clear of liens are commonplace in bankruptcy, and not without controversy. In particular, there are two schools of thought construing the meaning of "value"[1] in the authorizing provision when the "price at which such property is to be sold is greater than the aggregate value of all liens on such property."[2] It should not be surprising that sales free and clear of interests that are not liens engender their own controversy. Beyond the authorization to sell there remain the difficulties associated with providing adequate protection of such interests when demanded by the holders of such interests.[3] This article will provide an overview of the relevant controversies and then apply this overview to sales free and clear of non-monetary interests in real property, such as easements, restrictive covenants, licenses and leases.

Authorization for a Free and Clear Sale

The five alternative grounds in section 363(f) of the Bankruptcy Code upon which property of the estate may be sold free and clear of an interest in such property held by an entity other than the estate are:

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[1] "Value" has been interpreted to be either consistent with the meaning ascribed in 11 U.S.C. § 506(a), that is to say with reference to what the collateral is worth, *see, e.g., In re Beker Indus. Corp.*, 63 B.R. 474, 476 (Bankr. S.D.N.Y. 1986); or the aggregate dollar amount of liens irrespective of what the collateral is worth, *see Clear Channel Outdoor, Inc. v. Knupfer (In re PW, LLC)*, 391 B.R. 25, 40 (B.A.P. 9th Cir. 2008).

[2] 11 U.S.C. § 363(f)(3).

[3] 11 U.S.C. § 363(e).

(1) applicable non bankruptcy law permits sale of such property free and clear of such interest;

(2) such entity consents;

(3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;

(4) such interest in in bona fide dispute; or

(5) such entity could be compelled in a legal or equitable proceeding, to accept a money satisfaction of such interest.[4]

The third ground, which concerns liens, is not relevant to this discussion.

The first ground invokes nonbankruptcy law. The standard example of a nonbankruptcy law that authorizes sales of property free and clear of the interests of others is article 9 of the Uniform Commercial Code, which authorizes sales free and clear of security interests in inventory to buyers in the ordinary course of the seller's business.[5] As discussed below, this ground may be employed in real property sales when the interest at issue is revocable by the property owner or an unenforceable restraint on alienation.

The second ground is consent. Ostensibly, this is noncontroversial. Nevertheless, some courts have considered the failure to object after having received appropriate notice to constitute consent.[6] The issue of what constitutes appropriate notice, especially whether the specific

[4] 11 U.S.C. § 363(f).

[5] U.C.C. § 9-320(a); *see id.* § 1-201(9) (definition of "buyer in ordinary course of business"). Some courts have rejected arguments that this provision could be read to refer to foreclosure sales, holding instead that it refers to voluntary sales. *Dishi & Sons v. Bay Condos LLC*, 510 B.R. 696, 709-10 (S.D.N.Y. 2014); *In re Jaussi*, 488 B.R. 456, 458-59 (Bankr. D. Colo. 2013).

[6] *Futuresource LLC v. Reuters Ltd.*, 312 F.3d 281, 285-86 (7th Cir. 2002), *cert. denied*, 538 U.S. 962 (2003); *In re Christ Hosp.*, 502 B.R. 158, 174-75 (Bankr. D.N.J. 2013), *aff'd*, 2014 WL 4613316 (D.N.J. Sept. 12, 2014); *In re Borders Grp., Inc.*, 453 B.R. 477, 484 (Bankr. S.D.N.Y. 2011). *Contra In re DeCelis*, 349 B.R. 465, 466-67 (Bankr. E.D. Va. 2006); *In re Roberts*, 249 B.R. 152, 154-57 (Bankr. W.D. Mich. 2000).

interests that are intended to be the subject of the free and clear sale must be expressly identified, may engender litigation even in jurisdictions that allow silence to equal consent.[7]

The fourth ground is bona fide dispute. Such a dispute exists if there is an objective basis for either a legal or factual dispute as to the validity of the interest at issue. The court is not required to resolve the dispute or determine its probable outcome, but merely to ascertain that such a dispute exists.[8] With respect to non-monetary interests in real property, the finding of a bona fide dispute may not resolve the permissibility of a free and clear sale, since adequate protection of such interests may not be accomplished through the conventional method of having such interests attach to the proceeds of sale.[9]

The fifth ground, compelling the interest holder in a legal or equitable proceeding to accept a money satisfaction of the interest, is also controversial. Assuming that satisfaction does not require payment in full,[10] there is nevertheless a split in the case law about which kinds of proceedings qualify. If an eminent domain proceeding may be invoked, then all interests are

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[7] *See In re Crumbs Bake Shop, Inc.*, 522 B.R. 766, 777 (Bankr. D.N.J. 2014) (holding that notice was inadequate to find that non-objecting interest holders consented to free and clear sale). *Compare* Robert M. Zinman, Precision *in Statutory Drafting: The* Qualitech *Quagmire and the Sad History of § 365(h) of the Bankruptcy Code*, 38 J. MARSHALL L. REV. 97, 120 & n.75 (2004) (questioning the constitutional adequacy of notices of free and clear sales in apprising interest holders) *with* FED. R. BANKR. P. 6004(c) (requiring that the motion for a free and clear sale be served on parties who have interests in the property to be sold and the notice of a free and clear sale include only the date of the hearing on the motion and the deadline for objections).

[8] *IDEA Boardwalk, LLC v. Revel AC, Inc. (In re Revel AC, Inc.)*, 2015 WL 268816 at *11 (D.N.J. Jan. 21, 2015) (*hereinafter Revel D. Ct. I*), *rev'd on other grounds*, 2015 WL 500704 (3d Cir. Feb. 6, 2015) (unpublished order) (*hereinafter Revel Ct. App.*); *In re Taylor*, 198 B.R. 142, 162 (Bankr. D.S.C. 1996).

[9] *See Dishi & Sons v. Bay Condos LLC*, 510 B.R. at 711-12 (affirming bankruptcy court's determination that even if real property could be sold free and clear of leasehold, adequate protection of such interest would be the lessee's continued possession of the real property); *In re Haskell LP*, 321 B.R. 1, 10 (Bankr. D. Mass. 2005) (to similar effect, noting that first mortgagee's lien would exhaust the net proceeds of sale).

[10] *See Clear Channel*, 391 B.R. at 42-43 (construing provision to mean less than full payment); *In re Hassen Imports P'ship*, 502 B.R. 851, 860-61 (C.D. Cal. 2013) (requirement at least some payment; a proposed payment of zero is not authorized by the provision).

susceptible to a free and clear sale,[11] because every sort of interest may be taken by the government in an eminent domain proceeding.[12] Consequently, there must be some limitation on the kinds of proceedings that qualify.[13] Some courts allow sales free of subordinate interests if the foreclosure of a senior interest would relegate the junior interest holder to a claim against the foreclosure proceeds.[14] Other courts limit the available proceedings to those that could be brought by the trustee or debtor in possession, and not by other, foreclosing creditors.[15] What does not seem controversial is a proceeding to enforce a debtor's right to buy out the interest.[16]

Right of Interest Holders to Adequate Protection

Notwithstanding the ability of the trustee or debtor in possession to sell free and clear of non-monetary interests, the holders of such interest have the right to demand and receive adequate protection of their interests.[17] What is critical is that the holders of such interests must affirmatively request adequate protection.[18] The failure to request it in advance of the sale will result in the loss of such right.[19] Although with monetary interests the typical method of

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[11] *See Dishi & Sons v. Bay Condos LLC*, 510 B.R. at 711; *Haskell*, 321 B.R. at 10.

[12] *United States v. Gen'l Motors Corp.*, 323 U.S. 373, 377 (1945).

[13] Some courts allow cram down proceedings under 11 U.S.C. § 1129(b)(2) to qualify; some do not. *See Clear Channel*, 391 B.R. at 46 (not permitting such proceedings to qualify and collecting cases). Irrespective of this controversy, cram down proceedings are not available to affect non-monetary interests, and therefore, are not pertinent to the present discussion.

[14] *In re Boston Generating, LLC*, 440 B.R. 302, 333 (Bankr. S.D.N.Y. 2010); *In re Jolan, Inc.*, 403 B.R. 866, 869-70 (Bankr. W.D. Wash. 2009).

[15] *Dishi & Sons v. Bay Condos LLC*, 510 B.R. at 711; *Haskell*, 321 B.R. at 9.

[16] *Pac. Capital Bancorp, N.A. v. E. Airport Dev., LLC (In re E. Airport Dev., LLC)*, 443 B.R. 823, 830-31 (B.A.P. 9th Cir. 2011); *Clear Channel*, 391 B.R. at 43.

[17] 11 U.S.C. § 363(e).

[18] This is to be contrasted with the requirement to provide adequate protection prior to the court's authorization of the use of cash collateral. 11 U.S.C. § 363(c)(2)(b)-(3), (e).

[19] *Precision Indus., Inc. v. Qualitech Steel SBQ, LLC*, 327 F.3d 537, 548 (7th Cir. 2003).

providing adequate protection to have the interests attach to the proceeds of sale,[20] this method may not be appropriate for dealing with non-monetary interests. For example, some courts have held that even if a free and clear sale of a lease could be authorized, the only appropriate method of adequately protecting the leasehold was the preservation of the lessee's right to possession.[21] Beyond the question of determining adequate protection lies the risk that such determination turns out to be inadequate, resulting in the possibility of the interest holder's having a superpriorty claim.[22]

The Controversy Concerning the Interaction of Sections 363(f) and 365(h)

When the trustee or debtor in possession is a landlord and rejects an unexpired lease of real property, the tenant has the right under section 365(h) of the Bankruptcy Code to remain in possession for the duration of the lease term and any enforceable rights of renewal or extension.[23] When instead of rejecting the lease, the trustee or debtor in possession proposes to sell the real property free and clear of the lease under section 363(f), the question is presented whether the tenant's right to remain in possession under section 365(h) takes precedence. Many courts preserve the lessee's right to remain in possession, relying on the rule of statutory construction that the specific takes precedence over the general, and the importance of preserving the lessee's estate, which should not circumvented by utilizing another provision of the Code.[24]

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[20] *See In re Murel Holding Corp.*, 75 F.2d 941, 942 (2d Cir. 1935) (discussing requirements of adequate protection when property is sold under a plan under section 77B of the Bankruptcy Act of 1898).

[21] *Dishi & Sons v. Bay Condos LLC*, 510 B.R. at 711-12; *In re Haskell LP*, 321 B.R. at 10. *But see Qualitech Steel*, 327 F.3d at 548.

[22] 11 U.S.C. § 507(b).

[23] 11 U.S.C. § 365(h)(1)(A)(ii).

[24] *In re Zota Petroleus, LLC*, 482 B.R. 154, 161-62 (Bankr. E.D. Va. 2012); *Haskell*, 321 B.R. at 9; *In re Taylor*, 198 B.R. 142, 165-66 (Bankr. D.S.C. 1996).

The only court of appeals to address the question is the Seventh Circuit, which held that the two provisions address different events, and in a sale of real property, section 363(f) may be employed to deliver the premises free and clear of a leasehold.[25] The court relied on the plain meaning of section 363(f), which contains no limitation, and the obligation to construe statutes to avoid conflict.[26] Courts in other districts have adopted this view.[27] At least one court has avoiding permanently choosing sizes, and instead determined that the section that prevails in any given situation depends on "a case-by-case, fact-intensive, totality of the circumstances, approach."[28]

Application to Non-Monetary Interests

Leases

The issues concerning leases of real property have played out dramatically this year in connection with the proposed sale of the Revel casino in Atlantic City. The bankruptcy court approved a sale of the casino free and clear of existing leaseholds. The lessees appealed and sought a stay on several grounds: (1) that their right to continued possession protected by section 365(h) took precedence over the debtor's ability to sell free and clear under section 363(f); (2) that there was no bona fide dispute concerning a lease to enable a sale under section 363(f)(4); and (3) that even if a free and clear sale could be authorized, the only appropriate adequate protection under section 363(e) was the lessee's continued possession of the premises.[29]

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[25] *Qualitech Steel*, 327 F.3d at 548.

[26] *Id.* at 544-45.

[27] *Dishi & Sons v. Bay Condos LLC*, 510 B.R. at 707; *S. Motor Co. v. Carter-Pritchett-Hodges, Inc. (In re MMH Automotive Grp., LLC)*, 385 B.R. 347, 367 (Bankr. S.D.Fla. 2008); *Hill v. MKBS Holdings, LLC (In re Hill)*, 307 B.R. 821, 825-26 (Bankr. W.D. Pa. 2004).

[28] *In re Spanish Peaks Holdings II LLC,* 2014 WL 929701, at *18 (Bankr. D. Mont. Mar. 10, 2014).

[29] *Revel D. Ct. I*, 2015 WL 268816 at *9-14.

Initially, the district court denied the stay,[30] but the court of appeals reversed with respect to one lessee in an unpublished order stating that opinion would follow.[31] On remand, the district court granted a stay for all lessees, focusing on whether the bankruptcy court had sufficiently considered the bona fide dispute and adequate protection.[32]

Licenses

Licenses to occupy real property are generally considered to be permissions to do what otherwise would be considered illegal, especially trespassing.[33] They are not considered interests in property, are not transferrable, and do not run with the land.[34] Consequently, a sale free and clear of a license ought not to present a problem. Unfortunately, things are not so simple. That licenses are not considered interests in property under nonbankruptcy law does not mean they are not interests for purposes of section 363(f). Courts have recognized that interests for this purpose are not limited to traditional in rem interests, and held that successor liability claims constitute interests in property and therefore subject to free and clear sales.[35] If a successor liability claim is an interest for purposes of section 363(f), it is certainly plausible to contend that a license is likewise such an interest. If a license is an interest, is it one susceptible to a free and clear sale? And if so, what adequate protection may be demanded?

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[30] *Id.* at *17.

[31] *Revel Ct App.*, 2015 WL 500704, at *1. At the time of this writing, the court of appeals has not issued its opinion.

[32] *ACR Energy Partners LLC v. Revel AC, Inc. (In re Revel AC, Inc.)*, 2015 WL 567015, at *6 (D.N.J. Feb. 10, 2015).

[33] *Dore v. Wormley*, 690 F. Supp. 2d 176, 184 (S.D.N.Y. 2010).

[34] *See Todd v. Krolick*, 466 N.Y.S.2d 788, 790 (N.Y. App. Div. 1983).

[35] *In re Trans World Airlines, Inc.*, 322 F.3d 283, 289-90 (3d Cir. 2003); *In re Leckie Smokeless Coal Co.*, 99 F.3d 573, 582 (4th Cir. 1996).

Assuming that the license itself is not subject to a bona fide dispute and the licensee does not consent, the only possible authorization for a free and clear sale is either subsection (1), that applicable nonbankruptcy law authorizes such a sale, or subsection (5), that the licensee can be compelled in a legal or equitable proceeding to accept a money satisfaction of the license. Here subsection (1) should supply the answer. If the interest is not considered an interest in real property, and is traditionally viewed as terminating when the property is sold,[36] then the real property may be conveyed free of it, and no adequate protection would be necessary. Of course, this assumes that the interest actually is a license. Something called a license may actually be something else, such as a lease. The essential difference between a license and a lease is that a license grants a non-exclusive privilege to occupy real property and a lease grants exclusive possession of real property.[37] Something referred to as a license can be held to be a lease instead.[38] Moreover, something called a license can be held to be an easement.[39]

Easements

Express easements, the right granted by an owner to use the owner's land,[40] unless subject to a bona fide dispute, are generally impossible to remove via a free and clear sale.[41]

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[36] *De Haro v. United States*, 72 U.S. 599, 627 (1866); *Baltic Inc. Co. v. Perkins*, 475 F.2d 964, 966 (D.C. Cir. 1973); *Fletcher v. Del., Lackawanna & W. R.R. Co.*, 79 F.2d 306, 309 (2d Cir. 1935); *Felker v. Stewart Title Guar. Co. (In re Felker)*, 211 B.R. 165, 169 (Bankr. M.D. Pa. 1997); *Chevy Chase Land Co. v. United States*, 37 Fed. Cl. 545, 593 (Fed. Cl. 1997), *aff'd*, 230 F.3d 1375 (Fed. Cir. 1999) (table) (following answer of question certified to Md. Ct. App.).

[37] *Wattson Pac. Ventures v. Valley Fed. Sav. & Loan (In re Safeguard Self-Storage Trust)*, 2 F.3d 967, 972 (9th Cir. 1993); *In re Daben Corp.*, 469 F. Supp. 135, 142-143 (D.P.R. 1979); *In re Caribbean Petroleum Corp.*, 444 B.R. 263, 270-71 (Bankr. D. Del. 2010); *In re Yachthaven Restaurant, Inc.*, 103 B.R. 68, 73 (Bankr. E.D.N.Y. 1989).

[38] *Safeguard Self-Storage Trust*, 2 F.3d at 972.

[39] *Closson Lumber Co. v. Wiseman*, 507 N.E.2d 974, 976 (Ind. 1987).

[40] These are to be distinguished from implied easements or easements of necessity, which may well be subject to a bona fide dispute.

Nevertheless, that which is called an easement, if it is related to a lease, terminable when the lease terminates, and rent is paid, may be construed to be an unexpired lease, and hence rejectable.[42] In such circumstances, the lack of a possessory right in favor of the interest holder means there is no right to remain in possession under section 365(h).

Restrictive Covenants

The first question regarding restrictive covenants is whether they can be rejected as executory contracts. Depending on the nature of the particular covenant, courts have reached different conclusions.[43] If the covenant is rejectable, the non-debtor parties are relegated to a pre-petition claim for damages.[44] The next question is whether any of the five grounds for authorization of a free and clear sale is available. The unenforceability of a restrictive covenant under applicable nonbankruptcy law as an impermissible restraint on alienation, including unenforceability in light of changed circumstances, provides grounds under section 363(f)(1).[45] A bona fide dispute regarding the enforceability of a covenant may also permit a free and clear sale under section 363(f)(4).[46] The final relevant ground other than consent is whether the

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[41] *Koepp v. Holland*, 688 F. Supp. 2d 65, 92 (N.D.N.Y 2010), *aff'd on other grounds*, 2014 WL 6600418 (2d Cir. Nov. 21, 2014) (summary order); *Silverman v. Ankari (In re Oyster Bay Cove, Ltd.)*, 196 B.R. 251, 255-56 (E.D.N.Y. 1996).

[42] *In re Nevel Props. Corp.*, 2012 WL 528179, at *10 (Bankr. N.D Iowa Feb. 17, 2012); *aff'd*, 2012 WL 6588546 (N.D. Iowa Dec. 12, 2012), *aff'd*, 765 F.3d 846 (8th Cir. 2014).

[43] *Compare Gouveia v. Tazbir*, 37 F.3d 295, 298-99 (7th Cir. 1994) (restriction limiting buildings to no more than one story in a residential development not executory; debtor had no affirmative performance requirement); *with Steffan v. McMillan (In re Coordinated Fin. Planning Corp.)*, 65 B.R. 711, 713-14 (B.A.P. 9th Cir. 1986) (right of first refusal to purchase real property, although a covenant running with the land under California law, was executory and rejectable).

[44] 11 U.S.C. §§ 365(g)(1), 502(g)(1).

[45] *In re Daufuskie Island Props., LLC*, 431 B.R. 626, 644-45 (Bankr. D.S.C. 2010); *see In re TOUSA, Inc.*, 393 B.R. 920, 923-24 (Bankr. S.D. Fla. 2008).

[46] *Daufuskie Island Props.*, 431 B.R. at 646; *cf. In re Southcreek Dev., LLC*, 2011 WL 44703, at *2 (Bankr. C.D. Ill. Jan. 6, 2011) (discussing the reversal of an order authorizing a sale free and clear of a restrictive covenant based on the reversal of a finding of a bona fide dispute).

interest holder can be compelled to accept a money satisfaction under section 363(f)(5). Often this is not possible and a proposed free and clear sale will fail.[47] Nevertheless, to the extent that the restrictive covenant is cash convertible, a free and clear sale of such a covenant is possible.[48]

Conclusion

Conveying property free and clear of non-monetary interests in real property presents very different challenges from those confronted in sales free and clear of liens or claims. Leases present the issue whether the right to remain in possession of premises following the rejection of an expired lease takes precedence over the right to sell free and clear of the leasehold interest. True licenses are not agreements that run with the land, so they are easily suitable to be removed in a free and clear sale. Nevertheless, agreements called licenses may be construed to be leases or easements. Express easements not subject to a bona fide dispute may well be impossible to remove, but just as with licenses, things called easements may be other sorts of interests. Restrictive covenants may be rejectable as executory contracts, or removable if they are appropriately enforceable through damages, or stated differently, cash convertible. But if subordinate to a foreclosable lien, a covenant that would not receive any payment from the proceeds of sale may still remain a valid encumbrance after a sale. Moreover, even if susceptible to a free and clear sale, all such interests present the issue whether an interest in the proceeds of sale suffices as adequate protection. In sum, the determination whether the sale free and clear of non-monetary interests can be accomplished requires much more focused analysis on the rights of the parties under nonbankruptcy than does a sale free and clear of a lien or claim.

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[47] *Gouveia v. Tazbir*, 37 F.3d at 299-300; *see Hassen Imports P'ship*, 502 B.R. at 862 (even if the foreclosure of a senior lien would eliminate the restrictive covenant at issue, that no payment at all would be forthcoming prevents the use of the provision that requires a money satisfaction).

[48] *In re Signature Devs., Inc.*, 348 B.R. 758, 763-65 (Bankr. E.D. Mich. 2006) (distinguishing *Gouveia v. Tazbir* and finding covenant requiring the use of a particular builder to be cash convertible).

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On the Edge

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How Problem Easements Can Limit Sale Rights

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It is well settled in the bankruptcy context that a debtor in possession (DIP) may — in its attempt to reorganize or liquidate — reject a disadvantageous executory contract and may also sell property free and clear of all nondebtor interests. Indeed, §§ 365 and 363 of the Bankruptcy Code are among the two most powerful tools given a debtor, allowing it to pare, shape and mold its assets into a more valuable whole.

However, what if a debtor's efforts to shed itself of unneeded property could be hamstrung? What if a debtor was not allowed to reject a disadvantageous agreement, or could only sell property subject to certain restrictive interests in that property? Would those limitations challenge the debtor's efforts at reorganization or efficient liquidation? The answer is, "Absolutely." These theoretical limitations become very real when dealing with easements, covenants running with the land and other restrictive covenants. Failing to understand the effects of these types of interests can potentially derail a case — especially when it is centered around complex real-property transactions — and cost parties-in-interest significant value.

Can Easements and Other Restrictive Covenants Be Rejected?

Section 365(a) states, in part, that a DIP may, with the court's approval, "assume or reject any executory contract ... of the debtor."[1] The question remains whether an easement, covenant running with the land or other restrictive covenant constitutes an "executory contract." If so, they (along with their restrictions) can be rejected by a debtor. If not, a debtor or its successor might be stuck with their restrictions, and any detriment to asset values those restrictions might cause.

The question of whether an easement and other covenants that run with the land constitute an "executory contract" is largely settled. While the Bankruptcy Code fails to define what contracts may be considered "executory," most courts follow the well-known Countryman definition: An executory contract is one where "the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other."[2] "The time for testing whether there are material unperformed obligations on both sides is when the bankruptcy petition is filed."[3]

Generally speaking, courts have found that easements and other covenants that run with the land are not executory in nature because reciprocal duties are not owed; therefore, the agreements cannot be rejected pursuant to § 365.[4] However, the Seventh Circuit seems to have gone a bit fur-

1 11 U.S.C. § 365(a).

2 *See* Countryman, "Executory Contracts in Bankruptcy: Part I," 57 *Minn. L. Rev.* 439, 460 (1973); *see also In re Murexco Petroleum Inc.*, 15 F.3d 60 (5th Cir. 1994); *In re Texscan Corp.*, 976 F.2d 1269 (9th Cir. 1992); *U.S. v. Floyd*, 882 F.2d 235 (7th Cir. 1989); *Sharon Steel Corp. v. Nat. Fuel Gas Distrib. Corp.*, 872 F.2d 36, 39 (3d Cir. 1989); *In re Speck*, 798 F.2d 279, 279-80 (8th Cir. 1986); *Gloria Mfg. Corp. v. Int'l Ladies Garment Workers' Union*, 734 F.2d 1020, 1022 (4th Cir. 1984); *In re Chateaugay Corp.*, 130 B.R. 162, 164 (S.D.N.Y. 1991); *but see In re Magness*, 972 F.2d 689, 693 (6th Cir. 1992) (court looked to "functional approach" to determine whether contract was executory in nature).

3 *Glosser v. Maysville Reg'l Water Dist.*, 174 Fed. Appx. 34, 36 (3d Cir. March 9, 2009) (quoting *In re Columbia Gas Sys. Inc.*, 50 F.3d 233, 240 (3d Cir. 1995).

4 *See Glosser v. Maysville Reg'l Water Dist.*, 174 Fed. Appx. at 38-39 (holding that easement created by deed, but never independently recorded or developed, did not constitute on executory contract because "outstanding duties" to record additional documentation in chain of title were "not material" and were "ministerial" in nature; thus, easement could not be assumed and assigned under § 365); *In re Copper Creek Estates-Grand Island LLC*, Case No. BK11-40496-TJM, 2011 Bankr. LEXIS 2666 (Bankr. D. Neb. July 8, 2011) (holding that builder who placed restrictive covenant on vacant lots in exchange for providing landowner with $1 million in financing had no ongoing obligations under agreement, and that agreement was not executory in nature; thus, restrictive covenant ran with land and could not be rejected through bankruptcy); *In re Three A's Holdings LLC*, 364 B.R. 550 (Bankr. D. Del. 2007) (holding that covenants, conditions and restrictions that governed and the limited lease ran with the land under California law, and any assumption and assignment of that lease to party that did not qualify as tenant under terms of covenants, conditions and restrictions would violate California law); *In re Arden & Howe Assocs.*, 152 B.R. 971, 976 (Bankr. E.D. Cal. 1993) (court found that tenant could not "shed restrictive use covenants except by vacating. If the debtor tenant wants to stay in possession of the property, it must assume the lease, including all restrictive use provisions").

ther in holding that even though "almost all agreements to some degree involve unperformed obligations on either side," restrictive covenants do not fall within the purview of § 365 because they grant a present right of enjoyment, are traditionally treated as running with the land and are often recorded "on the title of the encumbered property."[5] The Ninth Circuit Bankruptcy Appellate Panel (BAP) recently agreed with the Seventh Circuit's reasoning in *Gouveia v. Tazbir*, in which the court held that restrictive covenants were not "executory contracts" under § 365, even where they required the debtors to perform a number of duties, and required nondebtor landowners to keep their boats insured and abide by certain bylaws (all of which the court seemed to view as *de minimis* obligations).[6]

However, exceptions do exist. Recently, the U.S. Bankruptcy Court for the Northern District of Iowa considered whether a "Deep Water Well Lease — Water Line and Access Easement" was actually an easement subject to the provisions of § 365.[7] The court concluded that while the agreement was a "temporary easement," it was the "functional equivalent of a lease" and could be rejected pursuant to § 365. The court further concluded that rejection damages should be computed according to the "fair rental value methodology."[8]

Similarly, the Ninth Circuit BAP was tasked with determining whether a right of first refusal/purchase option that existed in an "ownership agreement" was an executory contract subject to a § 365 rejection or was a covenant running with the land.[9] The court found that (1) the right of first refusal was a "pre-emption agreement" under California state law, (2) such agreements "are consistently found to be covenants running with the land," (3) such "covenants are not a property interest but are viewed as physically attached to the land," and (4) such covenants are "enforceable against successors in interest" under contract law.[10] Despite this, the court stated that executory contracts were defined under federal, rather than state, law and — referencing a Florida case that held that a recorded options contract was executory — found that the right of first refusal qualified as an "executory contract" that could be rejected under § 365, even though it was a covenant running with the land.[11]

Can Property Be Sold Free and Clear of Easements under § 363(f)(1)?

While the majority of courts have found that a debtor may not reject an easement or covenant running with the land under § 365 of the Bankruptcy Code, this has not stopped debtors from attempting to sell property free and clear of such encumbrances through § 363(f)(1). The language of § 363(f)(1) is relatively clear: A trustee or DIP

> may sell property ... free and clear of any interest in such property of an entity other than the estate, only if
>
> 1. applicable nonbankruptcy law permits sale of such property free and clear of such interest.[12]

Unfortunately for debtors and prospective purchasers — but fortunately for those possessing these rights — many courts have shown a willingness to maintain covenants and other rights that run with the land in a § 363(f)(1) sale context, unless a party can demonstrate a specific state or federal law provision that mandates that they be released.[13] Even property interests not specifically labeled as "restrictive covenants" or "easements" have been determined by courts to "run with the land" and therefore be immune to effective dissolution under § 363(f)(1).

Recently, the Fifth Circuit found that a natural gas pipeline system could not be sold free and clear of an entity's right to transportation fees tied to the operation of the pipeline system and its consent rights to the sale or assignment of the pipeline because both were covenants that ran with the land.[14] The court in *Dundee Equity Corp.* also found that a settlement agreement between a property owner and a group of tenants to repair property that "touched and concerned the land" must be considered a covenant running with the land, and could not be disposed of through § 363(f)(1).[15]

Similarly, the court in *Pintlar Corp.* preserved ASARCO's right to deposit mining tailings into the rivers and waterways of the Coeur d'Alene River Valley — which it recognized was an essentially worthless right in light of current environmental laws forbidding such actions — absent a showing by the Environmental Protection Agency (EPA) that a law existed that specifically *severed* such rights from the property.[16] The Eighth Circuit views easement rights and other similar covenants as so inviolable that it recognized and supported a state court decision finding that a bankruptcy sale pursuant to § 363(f) could not have severed an implied covenant between the owner of the property and neighboring residents that the property be maintained as a golf course.[17]

However, some courts have been creative in finding that "nonbankruptcy law" authorizes the severance of a covenant. The U.S. Bankruptcy Court for the District of South Carolina recognized that under the doctrine of "changed circumstances" — wherein the property had deteriorated well past the point where the restrictive covenants could protect those holding that interest in the land — the restrictive covenants could be invalidated, and a sale free and clear of those covenants would be allowed pursuant to § 363(f)(1).[18] The U.S. District Court for the Western District of Missouri acted

5 *Gouveia v. Tazbir*, 37 F.3d 295, 299 (7th Cir. 1994).

6 *Water Ski Mania Estates Homeowners Ass'n v. Hayes*, 2008 Bankr. LEXIS 4668, at *29-*34 (B.A.P. 9th Cir. March 31, 2008).

7 *In re Nevel Props. Corp.*, Bankr No. 09-00415, 2012 Bankr. LEXIS 551, at *25 (Bankr. N.D. Iowa Feb. 17, 2012).

8 *Id.* at *25-26.

9 *In re Coordinated Fin. Planning Corp.*, 65 B.R. 711, 713 (B.A.P. 9th Cir. 1986).

10 *Id.* at 712-13.

11 *Id.* at 713 (citing *In re Waldron*, 36 B.R. 633 (Bankr. S.D. Fla. 1984)). The Ninth Circuit has since reversed a later decision stating that all options contracts were executory, but technically left intact the BAP's decision in *Coordinated Financial Planning. See Unsecured Creditors' Comm. v. Southmark Corp.*, 139 F.3d 702, 706 (9th Cir. 1998).

12 11 U.S.C. § 363(f)(1).

13 *Mancuso v. Meadowbrook Mall Co. Ltd. P'ship*, 2007 U.S. Dist. LEXIS 23308, at *29-30 (Bankr. N.D. W.Va. March 28, 2007) (holding that certain "use covenants" governing what type of restaurant and signage could be utilized on certain parcel of land were restrictions that ran with land, and that debtor could not sell property free and clear of these covenants pursuant to § 363(f)(1), even though purchaser attempted to show that covenants could be avoided under "nonbankruptcy law" governing eminent domain, and reasoning that "the mere possibility of eminent domain does not authorize a trustee sale free and clear under the narrow conditions listed in § 363(f)"); *In re 523 E. Fifth St. House Preservation Dev. Fund Corp.*, 79 B.R. 568, 574-75 (Bankr. S.D.N.Y. 1987) (holding that deed restriction requiring that property be used for low-income housing was a covenant that ran with land, and that property could not be sold free and clear of such restriction through § 363(f)(1)); *In re Inwood Heights Hous. Dev. Fund Corp.*, Case No. 11-13322 (MG), 2011 Bankr. LEXIS 3251(Bankr. S.D.N.Y. Aug. 25, 2011) (holding that debtor could not use § 363(f)(1) "to obviate compliance with any sale restrictions contained in the Deed" granted by city of New York to debtor, including restriction that property could not be sold for certain number of years without city's consent).

14 *Newco Energy v. Energytec Inc.*, 739 F.3d 215 (5th Cir. 2013) (holding that sale free and clear of these interests under § 363(f)(1) was not possible).

15 *In re Dundee Equity Corp.*, 1992 Bankr. LEXIS 436 (Bankr. S.D.N.Y. March 6, 1992).

16 *In re Pintlar Corp.*, 187 B.R. 680, 682 (Bankr. D. Idaho 1995).

17 *Mid-City Bank v. Skyline Woods Homeowners Ass'n*, 636 F.3d 467 (8th Cir. 2011) (stating Nebraska Supreme Court decision that property could not have been sold free and clear of implied covenant that it be maintained as golf course had preclusive effect on bankruptcy court, and bankruptcy court was within its discretion to refuse to reopen case to allow an attack on Nebraska Supreme Court decision).

18 *In re Daufuskie Island Props. LLC*, 431 B.R. 626, 642-45 (Bankr. D.S.C. 2010).

similarly in ruling that Missouri law would allow a trustee to sell real property free and clear of a life estate pursuant to § 363(f)(1), as long as certain proceeds from the sale were apportioned to the holder of that estate.[19] However, the trend toward creativity has not been extended to the doctrine of eminent domain, as the court in *Mancuso* specifically found that the latent threat of eminent domain, where no proceeding had been initiated, was insufficient to allow a sale under § 363(f)(1) because that possibility exists in almost every case, and at all times.[20]

How Can Parties Protect Themselves?

If courts in most jurisdictions find that easements, covenants that run with the land and other restrictive-use covenants cannot be rejected, and that property cannot be sold free and clear of such interests under § 363(f)(1), what is a debtor to do? Simply put, there is little that can be done if an easement or other similar covenant finds its way into an agreement and the party granting the interest ends up in bankruptcy. Property owners must proactively manage their restrictive covenant portfolio, work to limit those covenants in time and scope, or avoid granting them altogether. It appears that once one is granted, the only way to sever such interests may be through a mutual agreement of the parties.

Similarly, potential purchasers of property must be very proactive in performing due diligence prior to a § 363 sale proceeding. Performing thorough title searches and reviewing all deeds and other agreements related to the property — whether or not they are recorded — should be standard procedure for any entity attempting a § 363 purchase of real estate. The failure to discover an interest running with the land could have dire financial ramifications — as with the substantial transportation fee at issue in *Newco Energy*. In this sense, an ounce of prevention can really be worth a pound of cure. abi

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19 *In re Rose*, 113 B.R. 534, 538-39 (W.D. Mo. 1990).
20 *Mancuso*, 2007 U.S. Dist. LEXIS 23308, at *29-30.

Feature

By Risa Lynn Wolf-Smith

Shedding Burdensome Restrictive Covenants in Real Estate Sales

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Real property sales in bankruptcy are often saddled by burdensome restrictive covenants, a legally enforceable promise to do or not do something to a piece of real property. In essence, covenants are private agreements among landowners that dictate how a property can or cannot be used that are intended to "run with" the property from landowner to landowner.

Covenants can range from trivial to oppressive and come in all varieties: requiring land to be used for agricultural purposes; specifying setbacks a certain distance from property boundaries; limiting the height or number of stories of buildings; restricting rental of property; mandating certain types of businesses or prohibiting commercial use altogether; and/or requiring stucco, brick or a certain color of paint. In many cases, these covenants may reduce the value of the property to be sold or impede its sale altogether. However, a bankruptcy filing presents an opportunity to shed burdensome covenants, especially those that constitute unreasonable restraints on the alienation of the property. This article explores the circumstances under which a bankruptcy court may order a sale of real property free of these so-called equitable restrictions.

General Treatment of Restrictive Covenants in Bankruptcy

A starting point in bankruptcy law is that real property may not be sold free and clear of recorded restrictive covenants, easements and other so-called "equitable servitudes" that run with the land.[1] This baseline rule relies on the principle that these types of property interests must be specifically enforced and that those who benefit from such "property interests" cannot be compelled to forego equitable relief.

In the often-cited *Gouveia v. Tazbir*, the Seventh Circuit Court of Appeals ruled that the debtor could not set aside a restrictive, reciprocal land covenant limiting property owners within a neighborhood to single-story residences.[2] The court reasoned that the interests of adjoining property owners were property rights that could not be extinguished in bankruptcy and that a monetary remedy would be inadequate.

However, the analysis of interests labeled as "restrictive covenants" or "restrictive easements" is not always so simple, and a court ought not abort its analysis of an agreement just because the parties have used the words "restrictive covenant." In many cases, a contract, even if recorded and labeled as a "restrictive covenant," might be something much more and might be susceptible to rejection as an executory contract or an interest for which a sale free and clear is warranted.

Rejection of Restrictive Covenants as Executory Contracts

Restrictive covenants, like restrictive easements, have traditionally been viewed as an encumbrance on a title. For a covenant to run with the land, the parties to the covenant must intend that it do so and the covenant must touch and concern the land.[3] Yet restrictive covenants are also contracts.[4] Moreover, land covenants come in two types: negative (or restrictive) and affirmative.[5] Affirmative covenants, which impose a duty on a landowner to perform an affirmative act in the future, are more narrowly construed, and the requirements for a covenant to run with the land are more strictly applied to affirmative covenants than negative covenants.[6] Further, affirmative covenants are disfavored in the law because of the fear that this type of obligation imposes an undue restriction on alienation or an onerous burden.[7]

For bankruptcy sales purposes, restrictive covenants may also be deemed executory contracts under the well-established "Countryman definition." Under that standard, an executory contract "is a contract under which the obligation of both the bank-

1 *See, e.g., Gouveia v. Tazbir*, 37 F.3d 295 (7th Cir. 1994); *In re 523 E. Fifth St. Housing Pres. Dev. Fund*, 79 B.R. 568 (Bankr. S.D.N.Y. 1987); *Skyline Woods Homeowners Ass'n Inc. v. Broekemeier*, 758 N.W.2d 376, 392 (Neb. 2008); *but see* Basil H. Mattingly, "Sale of Property of the Estate Free and Clear of Restrictions and Covenants in Bankruptcy," 4 *Am. Bankr. Inst. L. Rev.* 431 (1996).

2 *Gouveia*, 37 F.3d at 295 (7th Cir. 1994); *but see In re Signature Development Inc.*, 348 B.R. 758 (Bankr. E.D. Mich. 2006) (authorizing sale free and clear of recorded covenants under 11 U.S.C. § 363(f)(5) where court could compel damages in lieu of equitable enforcement and where restriction is more like executory contract).

3 *Restatement (Third) of Property (Servitudes)* § 1.3 (2000).

4 *Wright v. State Farm Fire & Cas. Co.*, 2014 U.S. App. LEXIS 3155, *7 (restrictive covenant is private agreement between property owner and some other person interested in property); *In re Coordinated Fin. Planning Corp.*, 65 B.R. 711, 712 (B.A.P. 9th Cir. 1986) ("Covenants are promises to do or refrain from doing certain things relating to the use of land."). *See also Beineke Chem. Waste Mgmt. of Ind. LLC*, 868 N.E.2d 534, 538 (Ind. Ct. App. 2007) (restrictive covenants are defined as contracts between private parties who, in exercise of their constitutional right of freedom of contract, can impose whatever lawful restrictions upon use of their lands that they deem advantageous or desirable); *May Dep't Stores v. Montgomery County*, 702 A.2d 988, 997 (Md. 1997); *aff'd as modified sub nom., Montgomery County v. May Dep't Stores Co.*, 721 A.2d 249 (Md. 1998) ("[C]ovenants were contractual obligations."); *Seabrook Island Prop. Owners Ass'n v. Pelzer*, 356 S.E.2d 411, 414 (S.C. 1987) ("Restrictive covenants are contractual in nature and bind the parties in the same manner as any other contract.").

5 *Restatement (Third) of Property (Servitudes)* § 1.3 (2000). *See also Hills v. Greenfield Village Homes Ass'n Inc.*, 956 S.W.2d 344 (Mo. Ct. App. 1997) (holding that affirmative covenant, as opposed to restrictive one, does not restrict use of land in question, but instead imposes duty on party to perform affirmative act).

6 *Midsouth Golf LLC v. Fairfield Harbourside Condominium Ass'n Inc.*, 187 S.E.2D 378, 385 (N.C. Ct. App. 2007); *McGinnis Point Owners Ass'n Inc. v. Joyner*, 152 S.E.2d 378 (N.C. Ct. App. 1999) ("Covenants [that] impose affirmative obligations on property owners are strictly construed.").

7 *Eagle Enter. Inc. v. Gross*, 349 N.E. 2d 816, 820 (N.Y. 1976).

rupt and other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing [the] performance of the other."[8] In *Gouveia*, the appellate court considered whether the covenant restricting neighborhood property to single-story residences constituted an executory contract. It observed that the covenant was not "the typical executory contract [in which] the Debtor's obligation is to do some affirmative act in the *future*" and that there was "nothing further to be done by either party, [as] the contract (if it be so characterized) was fully executed."[9]

However, other courts have treated restrictive covenants as executory contracts and permitted their rejection. For example, in *In re Coordinated Financial Planning Corp.*, the Ninth Circuit Bankruptcy Appellate Panel held that even though a recorded right of first refusal was a covenant running with the land and enforceable against the covenantors' successor-in-interest under California law, it was also an executory contract that was subject to rejection by the trustee.[10] Likewise, a restrictive-use covenant barring nightclubs that ran with the land was rejected by a chapter 7 trustee. Furthermore, the court held that § 365(h)(2) pre-empts all state remedies (an injunction, in this instance) for the breach of the restrictive-use covenant by the trustee and his successors.[11]

In another case, a right of first refusal contained in a recorded deed to property was rejected as an executory contract because it was deemed to be more in the nature of a personal contractual obligation.[12] Similarly, an easement in a document entitled "Well Lease and Easement" was determined to be a lease subject to rejection after an analysis of the "full economic substance of the transaction."[13] In short, whether a restrictive covenant is an "executory contract" for purposes of § 365 will be determined based on federal bankruptcy law — not state law. In addition, each contract must be analyzed based on its substance and individual characteristics and not just the labels assigned to it. Some covenants are executory, and some are not.

Sales Free of Restrictive Covenants under § 363(f)(1) and the Doctrine of Changed Circumstances

Section 363(f)(1) of the Bankruptcy Code permits a trustee or debtor in possession to sell property free and clear of an interest of another entity if applicable nonbankruptcy law permits the sale of the property free and clear of such interest. The doctrine of changed circumstances is recognized in most states to provide that a restrictive covenant may be determined to be unenforceable when circumstances have changed so that its enforcement no longer serves its intended purpose.[14] Further, under state law in most states, unreasonable restraints on the alienation of property are also unenforceable.[15]

Bankruptcy courts have adopted these state law doctrines to hold restrictive covenants unenforceable and to authorize sales free and clear of covenants under certain circumstances. Thus, in *In re Daufuskie Island Properties LLC*, a bankruptcy court determined that the trustee could sell the property free and clear of a repurchase right that was a restrictive covenant running with the land because the circumstances met the changed conditions doctrine under South Carolina law.[16] Further, the court opined that allowing the covenant to continue to block any proposed sale was an oppressive and unreasonable restriction, and was therefore unenforceable. In the same fashion, in *TOUSA*, a bankruptcy court authorized a sale free and clear of a restrictive covenant granting a property owner the right to insist that the debtor/developer not sell for a price of less than a certain minimum. The court reasoned that the restriction was an unreasonable restraint on the alienation of a property and that intervening circumstances rendered the covenant infeasible and unenforceable.[17]

Conclusion

Before jumping to conclusions based on the labels given to or contained in a contract, consider the true nature of the agreement in question. "Restrictive covenants" can in fact be rejected or extinguished under the right circumstances. Ask the following questions: Is the covenant more in the nature of an affirmative executory obligation than a restraint on the use of property? Have circumstances changed to make the covenant unreasonable, oppressive or a restraint on the alienation of the property?

If so, the restriction — even if it has been recorded and is intended to run with the land — may not be so ironclad after all. A bankruptcy sale free and clear of the restriction might not only be possible, but the best — or only — way to maximize the value of real property. abi

8 *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 522 n.6 (1984); *In re Johnson*, 501 F.3d 1163, 1174 (10th Cir. 2007); *Sharon Steel Corp. v. Nat'l Fuel Gas Distrib.*, 872 F.2d 36, 39 (3d Cir. 1989).
9 *Gouveia v. Tazbir*, 37 F.3d 295, 298 (7th Cir. 1994).
10 *In re Coordinated Fin. Planning Corp.*, 65 B.R. 711, 713 (B.A.P. 9th Cir. 1986).
11 *In re Arden & Howe, Assoc. Ltd.*, 152 B.R. 971, 976 (Bankr. E.D. Cal. 1993).
12 *In re Fleishman*, 138 B.R. 641, 644 (Bankr. D. Mass. 1992).
13 *In re Nevel Props. Corp.*, Bankr. No. 09-00415, 2012 Bankr. LEXIS 551 at *25 (Bankr. N.D. Iowa Feb. 17, 2012).
14 *Dunlap v. Beaty*, 122 S.E.2d 9, 15 (1961) (holding that under south Carolina law, when such significant change occurs with regard to servient property so as to render covenant valueless to covenantee and oppressive and unreasonable as to covenantor, it can be annulled, viewed as unenforceable, and determined ineffective and invalid); *Schneider v. Drake*, 44 P.3d 256, 261 (Colo. App. 2001) ("[A] court may exercise its equitable powers when a restrictive covenant no longer serves the purpose for which it was imposed or when the circumstances have changed and the enforcement would impose an oppressive burden."); *Zavislak v. Shipman*, 188; 362 P.2d 1053, 1055 (Colo. 1961) (holding that court may cancel restrictive covenants when they no longer serve purpose for which they were imposed); *Port St. Joe Dock & Terminal Railway Co. v. Maddox*, 191 So. 775, 116 (Fla. 1939) (holding that restrictive covenant relating to price floor on structural development would not be enforced because of certain changed circumstances).
15 *See, e.g., Iglehart v. Phillips*, 383 So.2d 610, 614-15 (Fla. 1980); *Malouff v. Midland Fed. Sav. and Loan Ass'n*, 509 P.2d 1240 (Colo. 1973).
16 *In re Daufuskie Island Properties LLC*, 2010 Bankr. LEXIS 5533, at *47-*55 (Bankr. D.S.C. 2010).
17 *In re TOUSA Inc.*, 393 B.R. 920, 924 (Bankr. S.D. Fla. 2008).

ABI 2015 ANNUAL SPRING MEETING

EQUITABLE MOOTNESS DEVELOPMENTS

By: Eric Walker, Partner, Perkins Coie LLP

- Equitable mootness is a prudential doctrine that allows an appellate court to decline reviewing the merits of a bankruptcy appeal despite clear statutory authority

- Recent decisions on equitable mootness highlight the different standards for Equitable Mootness in different circuits

    - **Second Circuit** - *In re BGI, Inc. v. BGI Creditors' Liquidating Trust*, 772 F.3d 102 (2d Cir. 2014) - Equitable mootness applies to Chapter 11 liquidating plans as well as Chapter 11 reorganization plans. Furthermore there is a presumption of equitable mootness if plan is substantially consummated that will only be rebutted if appellant can satisfy five factors established in *FritoLay, Inc. v. LTV Steel Co. (In re Chateaugay Corp.)*, 10 F.3d 944 (2d Cir. 1993)

    - **Third Circuit** - *In re SCH Corp*., 569 Fed. Appx. 119 (3d Cir. 2014) - Even if chapter 11 plan is substantially consummated, Court must still consider whether some form of equitable relief can be granted that will not completely upset the plan.

        - *In re Continental Airlines*, 91 F.3d 553 (3d Cir. 1996) (*en Banc*) - J. Alito analyzing the origins of the equitable mootness doctrine and questioning its legitimacy

    - **Ninth Circuit** - *In re Mortgages, Ltd*., 771 F.3d 623 (9th Cir. 2014) - Substantial consummation, which often occurs upon confirmation or shortly thereafter, does not always render a bankruptcy appeal moot. An appellate court must consider whether it can provide effective relief without upsetting confirmed plan or impacting innocent third parties

        - *In re Mortgages, Ltd.*, 771 F.3d 1211 (9th Cir. 2014) - Confirming that failure to diligently pursue rights in seeking a stay pending appeal will result in equitable mootness.

        - *JPMCC 2007-C1 Grasslawn Lodging, LLC v. Transwest Resort Properties, et al* (Case No. 12-17176) (argued January 13, 2015, decision pending) - whether third party investor and sponsor for Chapter 11 plan is an innocent third party that should be protected by doctrine of equitable mootness

    - **Supreme Court -** Petition for Certiorari in *Charter Communications* seeking uniformity in application of equitable mootness doctrine - Denied in April 2013

No.

IN THE

Supreme Court of the United States

LAW DEBENTURE TRUST COMPANY OF NEW YORK, AND R^2 INVESTMENTS, LDC,

Petitioners,

v.

CHARTER COMMUNICATIONS, INC., CCH I, LLC, CCH I CAPITAL CORPORATION, CCH II, LLC, CCH II CAPITAL CORPORATION, PAUL G. ALLEN, AND OFFICIAL COMMITTEE OF UNSECURED CREDITORS,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court of Appeals For The Second Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

This case concerns a judge-made doctrine called "equitable mootness." As part of the multi-billion-dollar Chapter 11 reorganization plan for the nation's fourth-largest cable provider, the bankruptcy court granted a select group of insiders payouts worth hundreds of millions of dollars, at the expense of other stakeholders, including petitioners. But the legality of that plan has not been reviewed by a single Article III court because the lower courts held that the appeals from the bankruptcy court were equitably moot. The equitable-mootness doctrine—which this Court has never endorsed—has no basis in the Bankruptcy Code and, as one Member of this Court has observed, has been "extended well beyond" any conceivable legitimate foundation. *In re Cont'l Airlines*, 91 F.3d 553, 570 (3d Cir. 1996) (en banc) (Alito, J., dissenting).

The question presented is:

Whether the court of appeals correctly dismissed these bankruptcy appeals as "equitably moot" despite acknowledging the availability of effective relief and, in conflict with other circuits, by applying a presumption of mootness and reviewing the district court's mootness determination only for abuse of discretion.

RULE 29.6 STATEMENT

Law Debenture Trust Company of New York is 100% owned by LDC Trust Management Limited, which in turn is 100% owned by Law Debenture Corporation plc, a publicly held corporation.

R^2 Investments, LDC, is an investment fund whose investment manager is Amalgamated Gadget, L.P. No publicly held corporation owns 10% or more of the stock of either entity.

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OPINIONS BELOW

The opinion of the Second Circuit (Pet. App. 1a–23a) is reported at 691 F.3d 476. The district court's decision (Pet. App. 24a–56a) is reported at 449 B.R. 14. The bankruptcy court's opinion (Pet. App. 57a–153a) is reported at 419 B.R. 221, and its findings and conclusions (Pet. App. 154a–431a) are unreported.

JURISDICTION

The Second Circuit issued its decision on August 31, 2012. Petitioners timely filed petitions for rehearing en banc, which were denied on November 13, 2012 (Pet. App. 432a–433a) and October 18, 2012 (*id.* at 434a–435a). This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

In pertinent part, 28 U.S.C. § 158 provides:

(a) The district courts of the United States shall have jurisdiction to hear appeals (1) from final judgments, orders, and decrees * * * of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title.

* * * * *

(d)(1) The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees entered under subsections (a) and (b) of this section.

STATEMENT

This case is about a doctrine that allows Article III courts to refuse to entertain the merits of indisputably live appeals from non-Article III bankruptcy courts. The doctrine is called "equitable mootness," but that moniker is highly misleading: There is nothing genuinely "moot" about live bankruptcy appeals, and there is nothing genuinely "equitable" about declaring a bankruptcy plan to be immune from Article III appellate review simply because its proponents raced to consummate the plan before that review could commence. What is more, the equitable-mootness doctrine is entirely judge-made, and in recent years it has morphed into a cudgel repeatedly wielded by the "winners" in bankruptcy court to deprive the "losers" of their statutory right to appeal.

This case presents two particularly troubling mutations of the equitable-mootness doctrine. The Second Circuit held that once a bankruptcy plan is substantially consummated, any appeal challenging the plan's confirmation is *presumed* to be equitably moot. That holding accords with decisions by the First, Sixth, and D.C. Circuits, but it directly conflicts with decisions by the Third, Fourth, Ninth, Tenth, and Eleventh Circuits. The Second Circuit further held that when a district court dismisses a bankruptcy appeal as equitably moot, a court of appeals reviews that dismissal only for abuse of discretion. That holding accords with decisions by the Third and Tenth Circuits but, as the decision below correctly acknowledged, is in direct conflict with decisions by the Fifth, Sixth, Eighth, Ninth, and Eleventh Circuits.

More fundamentally, this case concerns whether the equitable-mootness doctrine is cognizable at all and, if so, under what circumstances. The Second Circuit acknowledged that petitioners had diligently pursued their legal rights to challenge the plan; that the merits of petitioners' appeal could be decided; and that effective relief could be fashioned without disturbing the reasonable expectations of any innocent third parties. Only those parties who proposed and profited from the disputed plan—or others who later invested in the new enterprise with full awareness of petitioners' legal challenge—would be affected. And yet the Second Circuit believed itself powerless to decide the merits of petitioners' (substantial) legal challenges simply because respondents had successfully rushed to consummate the plan and were unwilling to abandon the benefits of their illicit bargain. In any other context, a defendant's completion of an unlawful transaction and a desire to retain its rewards would pose no obstacle to judicial review. But in the bizarre world of equitable mootness, that is exactly what happens.

The time has come for this Court to rein in the "curious doctrine" of equitable mootness (*In re Cont'l Airlines*, 91 F.3d 553, 567 (3d Cir. 1996) (en banc) (Alito, J., dissenting)), and this case presents the ideal opportunity to do it.

A. Charter's Prearranged Bankruptcy And The Bankruptcy Court Proceedings

Respondents Charter Communications, Inc. (CCI) and its affiliates (collectively, Charter) comprise the nation's fourth-largest cable company. Pet. App. 4a. In 2009, Charter filed for—and promptly emerged from—Chapter 11 bankruptcy, shedding billions of dollars in debt and wiping out shareholder equity. As the bankruptcy court acknowledged, the Charter reorganization plan was an "ambitious and contentious" "gamble" that presented "unusually complex legal issues" subject to "differing interpretations." *Id.* at 63a, 66a, 72a. The bankruptcy court ultimately confirmed the plan over objections by petitioners, the SEC, the U.S. Trustee, and others, in an order that has never been reviewed by an Article III court.

1. CCI is Charter's parent company, and respondent Paul Allen effectively controlled the enterprise through his 91% equity voting share of CCI (and 7% ownership stake), his chairmanship of CCI's board of directors, and his authority to appoint several other board members. *Id.* at 5a, 25a n.1, 26a, 68a–69a. Petitioner Law Debenture Trust Company ("LDT") represents investors that held CCI's $479 million in corporate bonds, and petitioner R^2 Investments, LDC held approximately 18,550,000 shares of CCI's common stock. *Id.* at 27a.

On March 27, 2009, Charter filed for Chapter 11 bankruptcy protection and simultaneously submitted a proposed reorganization plan to the bankruptcy court. *Id.* at 3a, 26a. That plan had been prearranged by Allen and an *ad hoc* group of

lenders—known as the "Crossover Committee"—who were creditors of certain mid-level entities in Charter's capital structure. *Id.* at 5a. CCI's bondholders and shareholders (other than Paul Allen) were not invited to participate in the bankruptcy planning. *Ibid.*

Not surprisingly, the insiders reaped enormous rewards under their prearranged plan. The "cornerstone" was a $200 million cash payment to respondent Allen to induce him to *continue* to wield substantial equity control over CCI. *Id.* at 6a–7a, 35a & n.13.[1] The plan also gave substantial benefits to members of the Crossover Committee, by swapping much of their debt for equity and allowing them to purchase additional shares in an exclusive rights offering, all at bargain-basement prices set by the plan.[2] *Id.* at 7a, 335a–337a. In addition, the plan included sweeping releases absolving respondent Allen and other nondebtor third parties

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[1] In particular, the "Allen Settlement" paid Allen *to retain* 35% voting control of CCI (permitting reinstatement of an affiliate's senior debt facility), and *to retain* an ownership interest in a subsidiary holding company (permitting CCI's valuable net operating losses, or "NOLs," to survive any cancellation-of-debt income generated by the reorganization). See Pet. App. 6a, 29a–30a.

[2] When the plan became effective, those shares *immediately* traded at nearly twice their acquisition price—a massive, overnight return. Compare CCI 2009 Form 10-K Annual Report F-13 (Feb. 26, 2010), and CCI S-1 Registration Statement, at item 15 (Dec. 31, 2009), with CCI 2010 Form 10-K Annual Report 31.

from practically any liability relating to Charter. *Id.* at 7a, 30a–31a, 124a–126a.

By contrast, the plan was unkind to the outsiders like petitioners. CCI's bondholders received only 32.7 cents on the dollar and an allocation from a pending legal settlement, despite the seniority of their claims to respondent Allen's equity stake. *Id.* at 7a, 31a. The bondholders voted overwhelmingly to reject the prearranged plan. CCI's shareholders—other than Allen, who received the $200 million payment described above—received no recovery at all and were deemed to reject the plan. *Ibid.*

Petitioners' objections to the plan should have been the end of it; the Bankruptcy Code forbids the approval of a plan unless there is an affirmative vote of at least one "impaired" class of a debtor's claimants. See 11 U.S.C. § 1129(a)(10). To engineer such approval at CCI, the plan carved out a separate class of unsecured creditors who together held a couple million dollars in claims against CCI—principally a former CEO's severance package—at the same priority level as petitioner LDT's $479 million. See *id.* at 138a–143a. Moreover, it artificially "impaired" that small class of unsecured creditors by paying their claims in full but without post-petition interest (their entitlement to which went undetermined). *Ibid.* Because these claimants received nearly a 100% payout, they understandably voted in favor of the plan. *Ibid.* The bankruptcy court then relied on that gerrymandered vote in

deciding to confirm the plan over petitioners' dissent. *Ibid.*[3]

2. Petitioners objected to Charter's reorganization plan, as did the SEC, the U.S. Trustee, and others. *Id.* 7a–8a, 124a n.27. In particular, petitioners objected under 11 U.S.C. § 1129 to the plan's method of securing the requisite approval of an "impaired" class of claim holders, its $200 million payment to Allen, its releases to Allen and other nondebtors, and its failure to value CCI's considerable assets and modest liabilities separately from its "enterprise" valuation of CCI's heavily encumbered affiliates. *Id.* at 8a.

Charter asked the bankruptcy court to "cram down" their prearranged plan by confirming it over petitioners' objections. The bankruptcy court did so on November 17, 2009. *Id.* at 7a. Petitioners promptly moved in the bankruptcy court for a stay of

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[3] The bankruptcy court held in the alternative that 11 U.S.C. § 1129(a)(10) can be satisfied on a "per plan" basis rather than a "per debtor" basis. Pet. App. 143a. According to the bankruptcy court, therefore, an affirmative vote by an impaired class at any of Charter's 131 affiliated debtors would permit a reorganization plan to be crammed down on claimants of the other 130 debtors. *Ibid.* Petitioner LDT challenged that conclusion as amounting to an improper "substantive consolidation" of these jointly administered bankruptcies. *Id.* at 54a n.39; see also *In re Owens Corning*, 419 F.3d 195, 205–12 (3d Cir. 2005) ("Consolidation restructures (and thus revalues) rights of creditors and for certain creditors this may result in significantly less recovery."); *In re Leslie Fay Cos.*, 207 B.R. 764, 779 (Bankr. S.D.N.Y. 1997).

the confirmed plan's implementation, and for certification of their appeals for expedited direct review by the Second Circuit under 28 U.S.C. § 158(d)(2). *Id.* at 7a, 14a & n.3. Debtors opposed the stay and certification requests, and the bankruptcy court denied both. *Ibid.* The next day, the district court likewise declined to stay plan implementation. *Ibid.* And on the following business day, debtors made their plan "effective" and engaged in a number of the transactions contemplated by the confirmed plan. *Id.* at 7a.

B. The District Court's Decision

Petitioners took separate appeals to the district court. Respondents opposed the appeals on the merits, but also moved to dismiss them as equitably moot. Although the district court acknowledged that petitioners were not seeking to "unravel[] the current Plan" (Pet. App. 41a), it granted respondents' motions to dismiss in a joint opinion (*id.* at 34a–66a).

The district court began with the premise that "bankruptcy appeals are strongly presumed to be equitably moot where the reorganization plan has been 'substantially consummated.'" *Id.* at 37a–38a. Here, the debtors had substantially consummated their reorganization plan soon after its confirmation. The district court therefore placed the "burden" on petitioners to demonstrate that the relief sought on appeal would not "jeopardize the bankruptcy's finality or otherwise be inequitable." *Id.* at 42a; see also *id.* at 55a n.41.

The district court concluded that petitioners failed to carry that burden with respect to *any* of their challenges to the plan. The district court

observed that the reorganization plan contained a non-severability clause, according to which every plan provision was deemed "integral to the Plan." *Id.* at 33a; see also *id.* at 42a–43a & n.22. In the district court's view, this provision meant that the court could not "modify the Confirmation Order or the Plan to provide for the requested relief, *not even to grant effective relief*, without nullifying the Plan's authorization." *Id.* at 43a (emphasis added).

C. The Court of Appeals' Decision

The Second Circuit considered the cases in tandem and affirmed. Like the district court, the court of appeals began with the premise that "[i]n this circuit, an appeal is presumed to be equitably moot where the debtor's plan of reorganization has been substantially consummated." Pet. App. 9a. An appellant can rebut that presumption, the court explained, only by demonstrating "all" of "five factors":

> (1) 'the court can still order some effective relief';
>
> (2) 'such relief will not affect the re-emergence of the debtor as a revitalized corporate entity';
>
> (3) 'such relief will not unravel intricate transactions so as to knock the props out from under the authorization for every transaction that has taken place and create an unmanageable, uncontrollable situation for the Bankruptcy Court';
>
> (4) 'the parties who would be adversely affected by the modification have notice of the appeal and an opportunity to participate in the proceedings'; and

> (5) 'the appellant pursued with diligence all available remedies to obtain a stay of execution of the objectionable order if the failure to do so creates a situation rendering it inequitable to reverse the orders appealed from.'

Id. at 10a (quoting *Frito-Lay, Inc.* v. *LTV Steel Co. (In re Chateaugay Corp.)*, 10 F.3d 944, 952–53 (2d Cir. 1993) (*"Chateaugay II"*)).

The court concluded that petitioners had satisfied *three* of those five factors on every claim raised by their appeals. See *id.* at 14a–16a, 20a, 22a. In particular, the court agreed that petitioners had been "diligent in seeking a stay of the confirmation order (factor 5)." *Id.* at 14a; see also *supra* pp. 7–8. The court further held that it *could* grant effective relief to petitioners on each claim (factor 1)—specifically, monetary payments from respondents CCI or Allen, a standalone valuation of CCI and recovery of any misappropriated value, and the removal of the nondebtor releases. See Pet. App. 14a, 20a, 22a.

The court also held that none of that effective relief would "adversely affect parties without an opportunity to participate in the appeal (factor 4)." *Id.* at 14a–15a; see also *id.* at 20a, 22a. "[T]he parties most affected [by the relief requested] would be Charter itself, Allen, and Charter's creditors, all of whom are either parties to this appeal or participated actively in the bankruptcy proceedings." *Id.* at 15a. With respect to any "[l]ess direct effects" that "may be felt by reorganized Charter's shareholders," the court concluded that it was sufficient that "Charter has regularly and fully disclosed the existence of this appeal and the

possibility of an adverse ruling as a risk factor" in public financial reports. *Id.* at 15a–16a.

Applying abuse-of-discretion review, however, the court concluded that the district court had correctly dismissed petitioners' appeals. The court acknowledged that "the courts of appeals are split over whether a de novo or abuse of discretion standard of review applied." *Id.* at 12a. Casting its lot with the Third and Tenth Circuits (*id.* at 12a–13a), the court held that the district court had not abused its discretion in concluding that petitioners failed to satisfy factors 2 and 3 (*id.* at 16a, 20a, 22a). The court stated that it would "cut the heart out of the reorganization" to deprive respondent Allen of his payment and nondebtor releases even if they "are legally unsupportable." *Id.* at 18a–19a.[4] Similarly, R²'s request for a standalone valuation of CCI, though "simple relief," would require "a significant revision of Charter's reorganization." *Id.* at 20a. And it was likewise a permissible "exercise of discretion" to dismiss petitioner LDT's claim that the plan improperly gerrymandered CCI's stakeholders to achieve a "cram down" against dissenting bondholders. *Id.* at 22a–23a. The court of appeals acknowledged that those bondholders' claims would

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[4] At the same time, the court recognized that a $200 million remedy "would not impact reorganized Charter's financial health" because "reorganized Charter has been quite successful with substantial assets and cash flow." Pet. App. 16a. Likewise, the court recognized that the plan's nondebtor releases were *expressly severable* from the rest of the plan under a "term sheet" incorporated into the Allen Settlement. *Id.* at 17a n.4.

be satisfied in full by "the simple payment of $330 million." *Id.* at 22a. But it refused to review the bondholders' entitlement to that remedy on the ground that any "legal conclusions" supporting such a "simple payment" would also "require unwinding the plan and reclassifying creditors." *Ibid.*

REASONS FOR GRANTING THE PETITION

The Second Circuit committed three errors of law, each of which merits this Court's review. First, it held—consistent with three Circuits but in conflict with five others—that reviewing courts must *presume* equitable mootness once debtors have substantially consummated a bankruptcy reorganization plan. Second, it held—consistent with two Circuits but in conflict with five others—that courts of appeals should review only for abuse of discretion a district court's dismissal of an appeal on equitable-mootness grounds. This case illustrates just how outcome-determinative both of those choices can be.

But there is an even more basic infirmity in the decision below: The court of appeals held that a fully contested appeal may be dismissed even when (i) effective relief can be fashioned, (ii) appellants have diligently pursued their rights, and (iii) granting relief would not upset the reasonable expectations of innocent third parties. It is far from clear that equitable mootness is *ever* legitimate. See, *e.g.*, *In re Cont'l Airlines*, 91 F.3d at 567–73 (Alito, J., dissenting). The United States, for example, has rightly called equitable mootness a "judicial construct of questionable foundation" that "is open to substantial abuse, and invites manipulation of the bankruptcy process," and has explained that "to the

extent the Bankruptcy Code addresses the issue, it appears to preclude the doctrine." Pet. 22–23, *United States* v. *GWI PCS 1, Inc.*, No. 00-1621 (Apr. 2001). But if the doctrine exists at all, it cannot possibly justify "the refusal of the Article III courts to entertain a live appeal over which they indisputably possess statutory jurisdiction and in which meaningful relief can be awarded." *In re Cont'l Airlines*, 91 F.3d at 571 (Alito, J., dissenting).[5]

This Court's review is necessary to resolve those deep, acknowledged, and intractable divisions among the circuits on important questions that arise in countless bankruptcy appeals. Review is also warranted so this Court may evaluate—for the first time—the fundamental legitimacy of an "equitable mootness" doctrine that looms large in virtually every major Chapter 11 reorganization.

I. The Circuits Are Divided Over Whether There Is A Presumption Of Equitable Mootness Whenever A Reorganization Plan Has Been Substantially Consummated

A. The Second Circuit held that "[i]n this circuit, an appeal is presumed equitably moot where the debtor's plan of reorganization has been substantially consummated." Pet. App. 9a; see also 11 U.S.C. § 1101(2) (defining "substantial consummation"). Applying that presumption, the court of

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[5] This case does not, by contrast, present questions about statutory mootness under 11 U.S.C. § 363(m) or similar provisions of the Bankruptcy Code. Cf. *Ind. State Police Pension Trust* v. *Chrysler LLC*, 130 S. Ct. 1015 (2009) (mem.).

appeals concluded that petitioners had "failed to establish" two of the mootness "factors." *Id.* at 16a. Accordingly, held the court, the merits of the appeal could not be decided.

That holding accords with the conclusions of three other Circuits. The First Circuit held, in *Rochman* v. *Northeast Utilities Service Group (In re Pub. Serv. Co. of N.H.)*, 963 F.2d 469, 473 n.13 (1992), that the substantial consummation of a reorganization plan "raises a 'strong presumption' that an appellate court will not be able to fashion an equitable and effective remedy." See also *Deloitte & Touche LLP* v. *Aquila Biopharmaceuticals, Inc. (In re Cambridge Biotech Corp.)*, 214 B.R. 429, 431 (D. Mass. 1997) (applying *In re Pub. Serv. Co. of N.H.*). Likewise, the Sixth Circuit has held in an unpublished opinion that "[s]ubstantial consummation raises a presumption that the appeal is moot and should be dismissed." *Unofficial Comm. of Co-Defendants* v. *Eagle-Picher Indus., Inc. (In re Eagle Picher Indus., Inc.)*, Nos. 96-4309, 97-4260, 1998 WL 939869, at *4 (6th Cir. Dec. 21, 1998); see also *First Century Bank, NA* v. *Sovereign Pocahontas Co. (In re HNRC Dissolution Co.)*, No. 0:05-CV-79-HRW, 2006 WL 782837, at *5 (E.D. Ky. Mar. 28, 2006) (applying *In re Eagle Picher Indus., Inc.*); *United Steelworkers of Am.* v. *Ormet Corp. (In re Ormet Corp.)*, No. 2:04-CV-1151, 2005 WL 2000704, at *4 (S.D. Ohio Aug. 19, 2005) (same). And the D.C. Circuit held in *In re AOV Industries, Inc.*, 792 F.2d 1140, 1149 (1986), that many of the appellate challenges before it were "control[led]" by "a strong presumption of mootness" generated by the substantial consummation of a plan.

B. By contrast, the Tenth Circuit explicitly rejected the Second Circuit's presumption in *Search Market Direct, Inc.* v. *Jubber (In re Paige)*, 584 F.3d 1327, 1331, 1339–40 (10th Cir. 2009). The court there concluded "that the party seeking to prevent this court from reaching the merits of the appeal bears the burden of proving that * * * the court should abstain from reaching the merits of the case." *Id.* at 1339–40. The court proceeded to "reject the conclusion that some circuits have reached"—citing a Second Circuit decision—"that a finding of substantial consummation will shift the burden to the party seeking to have the court reach the merits of its challenge to the plan." *Id.* at 1340 (citing *Aetna Cas. & Sur. Co.* v. *LTV Steel Co. (In re Chateaugay Corp.)*, 94 F.3d 772, 776 (2d Cir. 1996) ("*Chateaugay III*")).

As the Tenth Circuit explained, "the party inviting the court not to reach the merits of an appeal *always* carries the burden of showing that the answers to the [relevant factors] demonstrate that it would be unfair or impracticable to reverse the confirmed plan." *Ibid.* (emphasis added). The court held that no factor—substantial consummation or any other—"create[s] a presumption against the court reaching the merits of the challenge." *Ibid.* Indeed, the court stated, it is even "less inclined" to determine mootness where—as here—the plan proponents "accelerated the consummation of the plan despite their knowledge of a pending appeal." *Id.* at 1343. The court went on to hold that "[t]he district court [had] wrongly placed the burden of proof on this issue" on the appellant, and reversed that court's dismissal order because "[a]ppellees have

the burden of proof on this issue" and had failed to meet it. *Id.* at 1343, 1348.

Likewise, the Eleventh Circuit held in *Alabama Department of Economic and Community Affairs* v. *Ball Healthcare-Dallas, LLC (In re Lett)*, 632 F.3d 1216, 1225 (2011), that "[t]he party asserting mootness bears the burden of persuasion." "'[E]ven if substantial consummation has occurred, a court must still consider all the circumstances of the case to decide whether it can grant effective relief.'" *Ibid.* The Ninth Circuit has also held that "[t]he 'party moving for dismissal on mootness grounds bears a heavy burden,'" and that court has never shifted that burden to an appellant after substantial consummation. See *Motor Vehicle Cas. Co.* v. *Thorpe Insulation Co. (In re Thorpe Insulation Co.)*, 677 F.3d 869, 880 (9th Cir. 2012); *Focus Media, Inc.* v. *Nat'l Broad. Co. (In re Focus Media, Inc.)*, 378 F.3d 916, 923 (9th Cir. 2004). Moreover, the Third and Fourth Circuits have grappled with bankruptcy appeals that—like this one—challenged nondebtor releases after a plan's substantial consummation, without presuming equitable mootness. *Gillman* v. *Cont'l Airlines (In re Cont'l Airlines)*, 203 F.3d 203, 210 (3d Cir. 2000); *Behrmann* v. *Nat'l Heritage Found.*, 663 F.3d 704, 713–14 (4th Cir. 2011).[6]

C. The latter Circuits have the better of the argument. For starters, a presumption of mootness

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[6] See also *So. Pac. Transp. Co.* v. *Voluntary Purchasing Grps., Inc.*, 246 B.R. 532, 534 (E.D. Tex. 2000) ("Obviously, the burden is upon the party asserting the equitable mootness doctrine to prove that it applies.").

conflicts with the "virtually unflagging obligation of the federal courts to exercise the jurisdiction given them." *Colo. River Water Conservation Dist.* v. *United States*, 424 U.S. 800, 817 (1976). Bankruptcy appellants have a statutory right to seek Article III review of bankruptcy court orders. 28 U.S.C. § 158(a), (d)(1). A presumption of mootness abridges the express command of Congress.

Presuming mootness after substantial consummation of a reorganization plan also insulates from Article III review the most consequential orders that a non-Article III bankruptcy court issues. The present case is a telling example: The bankruptcy court distributed billions of dollars in assets, richly rewarding some stakeholders while wiping others out entirely. And it did so by approving a plan gerrymandered to ensure cramdown over vociferous objections. The presumption of mootness shields all of that from Article III review, effectively giving bankruptcy courts the final word on the lawfulness of their own orders. And it does all this based upon a factor—the timing of substantial consummation—that is largely in the control of the bankruptcy court and the plan's proponents.

Finally, a presumption of equitable mootness is difficult to square with the fact that, in every other mootness context, the presumption works just the opposite way. Proponents of *constitutional* mootness must bear a heavy burden before such appeals will be dismissed. See, *e.g.*, *County of L.A.* v. *Davis*, 440 U.S. 625, 631 (1979). Proponents of *prudential* mootness—to which the Second Circuit analogized equitable mootness (Pet. App. 21a. But cf. *infra* p. 20–21)—bear "the formidable burden" of demon-

strating mootness. *Already, LLC* v. *Nike, Inc.*, ___ S. Ct. ___, No. 11-982, slip op. at 4 (Jan. 9, 2013) (quoting *Friends of the Earth, Inc.* v. *Laidlaw Envtl. Servs. (TOC), Inc.*, 528 U.S. 167, 190 (2000)); see also *id.*, slip op. 1 (Kennedy, J., concurring) (same); *United States* v. *W.T. Grant Co.*, 345 U.S. 629, 633 (1953). There is no reason to invert the presumption when it comes to the doctrine of equitable mootness.

II. The Circuits Are Divided On The Standard For Reviewing A District Court's Decision To Dismiss An Appeal As Equitably Moot

As the decision below explicitly acknowledged, "the courts of appeals are split over whether a de novo or abuse of discretion standard of review should be applied by a court of appeals" when reviewing a district court's equitable-mootness dismissal of a bankruptcy appeal. Pet. App. 12a.

A. The Second Circuit held that the district court's decision to dismiss petitioners' appeals as equitably moot was reviewable only for "abuse of discretion." *Ibid.* It reasoned that such dismissals are "somewhat analogous" to mootness dismissals arising from a "defendant's voluntary cessation of allegedly illegal conduct," in which abuse-of-discretion review is also applied. *Ibid.* See, *e.g.*, *W. T. Grant Co.*, 345 U.S. at 633–34. The Second Circuit's position accords with decisions by the Third and Tenth Circuits. *In re Cont'l Airlines*, 91 F.3d at 560; *In re Paige*, 584 F.3d at 1334–35.

B. By contrast, the Fifth, Sixth, Eighth, Ninth, and Eleventh Circuits review a district court's equitable-mootness dismissal *de novo*. Those courts have generally relied on the fact that courts of

appeals and district courts play the same role as appellate tribunals in bankruptcy cases under 28 U.S.C. § 158. In *United States* v. *GWI PCS 1 Inc. (In re GWI PCS 1 Inc.)*, 230 F.3d 788, 799–800 (5th Cir. 2000), for example, the Fifth Circuit explained that courts of appeals and district courts "'perform the same function'" in "'the bankruptcy appellate process'" when they review bankruptcy court decisions. It therefore applied *de novo* review in addressing the appropriateness of an equitable-mootness dismissal.

Likewise, the Sixth Circuit in *Curreys of Nebraska, Inc.* v. *United Producers, Inc. (In re United Producers, Inc.)*, 526 F.3d 942, 946 (2007), applied the "well established" principle that it "independently reviews a decision of the bankruptcy court that has been appealed to the Bankruptcy Appellate Panel." (Bankruptcy Appellate Panels—or BAPs—hear bankruptcy appeals in some circuits in the same capacity as district courts do in other circuits. See *id.* at 946 n.1; see also 28 U.S.C. § 158(b), (c)).[7] De novo review of a BAP's equitable-mootness conclusion, the court explained, is "consistent" with the court of appeals' "plenary review of the decisions of a lower court exercising its appellate jurisdiction." 526 F.3d at 947.

In reaching that conclusion, the Sixth Circuit explicitly recognized (*id.* at 946) that the en banc Third Circuit had reached the opposite conclusion

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[7] For the sake of clarity, our references in this Part to equitable-mootness dismissals by a "district court" include such orders issued by a bankruptcy appellate panel.

(by a 7–6 vote) in *Continental Airlines*. But the Sixth Circuit adopted the position of then-Judge Alito's dissent, agreeing that "the court of appeals is 'in just as good a position to make this determination as was the district court.'" *Ibid.* (quoting 91 F.3d at 568 n.4 (Alito, J., dissenting)).

The Ninth and Eleventh Circuits have long hewn to the same principles. See *Baker & Drake, Inc.* v. *Pub. Serv. Comm'n of Nev.*, 35 F.3d 1348, 1351 (9th Cir. 1994); *Olympic Coast Inv., Inc.* v. *Crum (In re Wright)*, 329 F. App'x 137, 137 (9th Cir. 2009); *First Union Real Estate Equity & Mortg. Invs.* v. *Club Assocs. (In re Club Assocs.)*, 956 F.2d 1065, 1069 (11th Cir. 1992); *Liquidity Solutions, Inc.* v. *Winn-Dixie Store, Inc. (In re Winn-Dixie Store, Inc.)*, 286 F. App'x 619, 622 & n.2 (11th Cir. 2008) (per curiam). Moreover, the Eighth Circuit applied "careful de novo review" to a district court's equitable-mootness dismissal in an unpublished opinion. *Zegeer* v. *President Casinos, Inc. (In re President Casinos, Inc.)*, 409 F. App'x 31, 31 (2010) (per curiam).[8]

C. The de-novo Circuits have the better view—there is simply no good reason for one appellate court to defer to another appellate court's dismissal on equitable-mootness grounds. As explained above, the Second Circuit reasoned by analogy to prudential-mootness dismissals following a

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[8] The Fourth Circuit has acknowledged but not resolved the issue. *Retired Pilots Ass'n of U.S. Airways, Inc.* v. *US Airways Grp., Inc. (In re US Airways Grp., Inc.)*, 369 F.3d 806, 809 n.* (4th Cir. 2004).

defendant's voluntary cessation of the conduct that was causing the plaintiff's injury. Pet. App. 12a–13a. But those cases rest on the very different premise that it often makes sense to *withhold* (not necessarily *preclude*) judicial relief until the defendant resumes his allegedly illegal conduct—at which time the plaintiff can return to court to vindicate his rights. See *In re Cont'l Airlines*, 91 F.3d at 569 (Alito, J., dissenting) (citing 13A Charles Alan Wright *et al.*, FEDERAL PRACTICE AND PROCEDURE § 3533.1 at 226 (1984)). Under the equitable-mootness doctrine, by contrast, the appellant forever loses his right to Article III review, even though he is alleging a *permanent and existing* injury from the bankruptcy plan (not merely a *potential and future* injury from resumed misconduct).

Moreover, as the Second Circuit acknowledged, the courts of appeals apply plenary review to virtually all other legal rulings by a district court in bankruptcy appeals. Pet. App. 12a. There is no reason to depart from that tried-and-true approach in response to a district court's conclusion that an appeal is equitably moot. See *In re Cont'l Airlines*, 91 F.3d at 568 n.4 (Alito, J., dissenting) (criticizing the majority's departure from the Third Circuit's "unbroken and well-established line of authority * * * holding that '[b]ecause the district court sits as an appellate court in bankruptcy cases, our review of the district court's decision is plenary'").

Finally, to whatever extent an equitable-mootness doctrine is appropriate, it is a "judicial anomaly" that should be applied "with a scalpel rather than an axe." *Bank of N.Y. Trust Co.* v.

Official Unsecured Creditors' Comm. (In re Pac. Lumber Co.), 584 F.3d 229, 240 (5th Cir. 2009). De novo review of district court dismissals is better suited to ensuring that the equitable-mootness doctrine adheres—and returns (see Part III, *infra*)—to its proper limits. See *In re Cont'l Airlines*, 91 F.3d at 568 n.4 (Alito, J., dissenting); cf. *Pierce* v. *Underwood*, 487 U.S. 552, 562 (1988) (abuse-of-discretion review provides "flexibility" to the lower court).

III. This Court's Review Is Necessary To Determine Whether Article III Courts Can Decline To Review Live Bankruptcy Appeals Where Effective Relief Is Available

Presumptions and standards of review aside, this Court's review is necessary for a more fundamental reason: The equitable-mootness doctrine is now regularly invoked to deny Article III review of a bankruptcy court's confirmation order even where, as here, effective relief is fully available. It is doubtful that equitable mootness is ever cognizable. But here—where the court of appeals acknowledged that some effective relief is available; that petitioners fully pursued their appellate rights; and that no innocent third parties would be affected by granting petitioners relief—the doctrine is simply invalid.

In the court of appeals' view, it would not be "equitable" to hear petitioners' appeals because granting relief would disturb the benefits of the bargain that respondents claimed for themselves under the plan. But the entire point of these appeals was that those very benefits *were illegal*. This Court

should take the opportunity to make clear that—if equitable mootness exists at all—it cannot defeat Article III review where the appellate courts "indisputably possess statutory jurisdiction and * * * meaningful relief can be granted." *In re Cont'l Airlines*, 91 F.3d at 571 (Alito, J., dissenting).

A. There are considerable constitutional problems with refusing to hear appeals from non-Article III bankruptcy courts in the name of "equitable mootness." This Court's approval of non-Article III adjudication has turned on, among other things, whether Article III courts still retain "'essential attributes of judicial power'" like the "de novo" review of "legal rulings." *Commodity Futures Trading Comm'n* v. *Schor*, 478 U.S. 833, 852–53 (1986); cf. *Thomas* v. *Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 592–93 (1985) (availability of some Article III review supports administrative adjudication); see also Richard H. Fallon, Jr., *Of Legislative Courts, Administrative Agencies, and Article III*, 101 HARV. L. REV. 915, 939 (1988) ("Even if a case is tried in the first instance by a non-article III tribunal, a separation-of-powers interest remains in ensuring appellate review by an article III court."). As this Court recently explained in *Stern* v. *Marshall*, 131 S. Ct. 2594 (2011), the bankruptcy court's authority to enter binding, final judgments in "core" bankruptcy proceedings—like plan confirmation—is supposed to be subject to district court review on appeal "under traditional appellate standards," *id.* at 2604.

The concern that the lower federal courts—and particularly those in the Second Circuit—are routinely turning away bankruptcy appeals is

magnified by what the government has correctly identified as the potential for "substantial abuse" of the equitable-mootness doctrine by bankruptcy plan proponents. Pet. 23, *United States* v. *GWI PCS 1, Inc.*, No. 00-1621 (Apr. 2001). In this case, for example, respondents secured confirmation over vociferous objections that their plan was illegal. They then successfully opposed a stay pending appeal by threatening to exercise a self-destruct deadline they had built into their plan (but had postponed *six times* to facilitate confirmation). See Bankr. S.D.N.Y. Dkt. Nos. 946, 972. And one business day later, they rushed to consummate their plan—only to contend later that depriving them of the "important" but allegedly illegal plan terms they implemented would be unjust. In that manner, respondents used the Second Circuit's equitable-mootness doctrine "as a weapon to prevent any appellate review." *Nordhoff Invs., Inc.* v. *Zenith Elecs. Corp.*, 258 F.3d 180, 192 (3d Cir. 2001) (Alito, J., dissenting).

The equitable-mootness doctrine encourages precisely such gamesmanship by any debtor or related insider who wants to protect an "ambitious and contentious," prearranged reorganization plan from Article III appellate review. Stay requests halting bankruptcy reorganizations are rarely granted and, when granted, often require appellants to post substantial bonds. See, *e.g.*, *ACC Bondholder Grp.* v. *Adelphia Commc'ns Corp. (In re Adelphia Commc'ns Corp.)*, 361 B.R. 337 (S.D.N.Y. 2007) (setting a $1.3 billion bond as a condition to a stay pending appeal). And without a stay, plan proponents often can quickly implement a sophisticated corporate reorganization by completing

a series of paper transactions. Bankruptcy appellants should not so easily be denied their only shot at Article III review—certainly not in the absence of any statement by this Court that such a drastic departure from basic principles of judicial review is warranted.

B. Indeed, the decision below illustrates just how far equitable mootness has strayed from any legitimate origin. The Second Circuit correctly concluded that effective relief is available to petitioners on each of their claims. See Pet. App. 14a, 20a, 22a. Petitioners seek limited remedies—money judgments and the striking of nondebtor liability releases—and not an unwind of Charter's reorganization plan. Moreover, that relief is available from active participants in Charter's bankruptcy proceedings, who are litigants before the Court. *Id.* at 14a–16a, 20a, 22a. And petitioners diligently pursued their claims by applying to stay plan implementation pending appeal. *Id.* at 14a, 20a, 22a.

Despite all that, the Second Circuit concluded that appellate review was unavailable. With respect to two of petitioners' challenges, the court of appeals held that the pertinent plan provisions were simply too "important" to the plan insiders to permit the appeal to be heard on the merits. *Id.* at 19a. Petitioners contended, for example, that the blanket liability releases granted to respondent Allen and other nondebtors were unlawful. The court of appeals refused to reach that claim, even though respondent Allen and the other plan proponents had expressly agreed in a "term sheet" for their settlement that any judicial decision to strike the plan's nondebtor releases *would not affect the*

validity of any other plan provision. See *id.* at 17a n.4.[9]

Likewise, petitioners challenged respondent Allen's extraction of $200 million from Charter while CCI's bondholders were shorted $330 million and the

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[9] In this additional respect, the Second Circuit's decision conflicts with numerous other circuits that "have agreed that equitable mootness need not foreclose an appeal from aspects of Chapter 11 plan confirmation that solely concern * * * releases." See *Hilal* v. *Williams (In re Hilal)*, 534 F.3d 498, 501 (5th Cir. 2008) (collecting cases); see also *Behrmann*, 663 F.3d at 714 (releases claim not moot where, as here, the releases were severable from the plan); *United Artists Theatre Co.* v. *Walton (In re United Artists Theatre Co.)*, 315 F.3d 217, 228 (3d Cir. 2003) (court could "modify" the plan's "indemnity provision" and "the Plan otherwise would survive intact"); *W.R. Huff Asset Mgmt. Co.* v. *HSBC Bank USA (In re PWS Holding Corp.)*, 228 F.3d 224, 236 (3d Cir. 2000) ("The releases (or some of the releases) could be stricken from the plan without undoing other portions of it."). In fact, the question whether a bankruptcy court has the power to grant nondebtor releases at all is itself the subject of a deep split among the circuits. Compare Pet. App. 124a–126a with *Vitro S.A.B. de CV* v. *Ad Hoc Group of Vitro Noteholders (In re Vitro S.A.B. de CV)*, No. 12-10542, 2012 WL 5935630, at *23 (5th Cir. Nov. 28, 2012); *Resorts Int'l, Inc.* v. *Lowenschuss (In re Lowenschuss)*, 67 F.3d 1394, 1401–02 (9th Cir. 1995); *Landsing Diversified Props.-II* v. *First Nat'l Bank & Trust Co. of Tulsa (In re W. Real Estate Fund, Inc.)*, 922 F.2d 592, 600–02 (10th Cir. 1990), amended by *Abel* v. *West*, 932 F.2d 898 (10th Cir. 1991). The Bankruptcy Code does not authorize nondebtor releases, except in asbestos cases. See 11 U.S.C. § 524(e), (g).

rest of CCI's equity holders received nothing. See *Bank of Am. Nat'l Trust & Sav. Ass'n* v. *203 N. LaSalle St. P'ship*, 526 U.S. 434, 437 (1999) (rejecting shareholders' retention of equity in a reorganized enterprise, over the objection of senior creditors, upon granting themselves the exclusive right to contribute "new value" to the enterprise). The court of appeals acknowledged that a monetary judgment completely remedies petitioners' injury and would not imperil the reorganization in the slightest. Pet. App. 16a. Charter, it explained, "has been quite successful" since emerging from bankruptcy, and has substantial assets and cash flow, access to an $800 million revolving line of credit, and long-term debt structured on favorable terms." *Ibid.* Indeed, Charter generated $7.1 billion in 2010 revenue and $7.2 billion in 2011 revenue. CCI 2011 Form 10-K Annual Report 33. But the court declined to reach the merits.[10]

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[10] By contrast, other circuits have concluded that active combatants in the bankruptcy proceedings have an exceedingly tenuous claim to "equitable mootness" when they are defending their own spoils on appeal. In *Spirtos* v. *Moreno (In re Spirtos)*, 992 F.2d 1004, 1007 (9th Cir. 1993), for example, the court held that it could award effective relief "by ordering * * * a party to this appeal[] to return the money to the estate" where that party "knew at the time he received and spent his plan distribution that [the appellant] had appealed the bankruptcy court's decision." Accord *TNB Fin., Inc.* v. *James F. Parker Interests (In re Grimland, Inc.)*, 243 F.3d 228, 232 n.6 (5th Cir. 2001) ("Of course, the administrative claimants are not strangers to the bankruptcy case, and as parties

With respect to the two other appellate issues, the court of appeals affirmed dismissal not because the relief sought on appeal would *itself* unravel Charter's plan, but based on hypothetical concerns. For example, petitioner R^2 sought a separate valuation of CCI's assets and liabilities, and requested a pro rata share of any surplus value as an equity holder. See Pet. App. 20a. The court of appeals did not contend that such a hearing or any resulting surplus distribution to petitioners would upend Charter's reorganization. See *id.* at 20a–21a. Instead, it affirmed dismissal on the unsupported ground that providing petitioner R^2 a standalone valuation of CCI would necessarily entitle hypothetical *other* parties to standalone valuations of every *other* Charter entity. *Ibid.* But there are no such hypothetical other parties who objected to Charter's reorganization and appealed from the bankruptcy court's confirmation order.

Similarly, petitioner LDT challenged the gerrymandered and artificially impaired class of CCI stakeholders for purposes of allowing the "cram down" of the plan. See 11 U.S.C. § 1129(a)(10). Once again, the court of appeals recognized that the bondholders can be made whole though a $330 million payment, and that such a payment will not threaten Charter's re-emergence from bankruptcy. Pet. App. 22a. But "[a]s with [petitioner] R^2's claims regarding valuation," the court of appeals affirmed the district court's "exercise of its discretion in

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intimately connected to the case administration, their expectations may not be settled.").

dismissing the claim" on the ground that granting monetary relief to petitioner LDT would require a wholesale reclassification of Charter's claimants. *Id.* at 22a–23a. But no party has asked for that, and the requested $330 million payment would not knock the props out from under the plan—it would simply remedy the damages caused by illegal confirmation.

* * *

The decision below confirms that the equitable-mootness doctrine has truly run amok. If equitable mootness has any validity at all, it cannot preclude Article III courts from hearing appeals where effective relief can be fashioned without unwinding the plan or disturbing reasonable expectations of innocent third parties, and where the appellants diligently sought appellate review. At the very least, this Court should consider whether such extreme applications of the doctrine are legitimate.

IV. These Issues Are Recurring And Nationally Important

For more than three decades—and with steadily increasing frequency—the lower courts have been confronted with claims that bankruptcy appeals are equitably moot. See*, e.g.*, *In re Thorpe Insulation Co.*, 677 F.3d at 879–83; *In re Lett*, 632 F.3d at 1225–26; *Bank of N.Y. Trust Co.* v. *Pac. Lumber Co. (In re Scopac)*, 624 F.3d 274, 281–82 (5th Cir. 2010); *Alberta Energy Partners* v. *Blast Energy Servs., Inc. (In re Blast Energy Servs., Inc.)*, 593 F.3d 418, 424–26 (5th Cir. 2010); *Schaefer* v. *Superior Offshore Int'l, Inc. (In re Superior Offshore Int'l, Inc.)*, 591 F.3d 350, 353–54 (5th Cir. 2009); *In re Paige*, 584 F.3d at 1337–48; *In re Pac. Lumber*, 584 F.3d at 240–44,

249–52; *In re Hilal*, 534 F.3d 498, 500–01 (5th Cir. 2008); *In re United Producers*, 526 F.3d at 946–52; *Bank of Montreal* v. *Official Comm. of Unsecured Creditors (In re Am. Homepatient, Inc.)*, 420 F.3d 559, 563–65 (6th Cir. 2005); *Deutsche Bank AG* v. *Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136, 143–45 (2d Cir. 2005); *In re Focus Media*, 378 F.3d at 922–24; *In re US Airways Grp., Inc.*, 369 F.3d at 809–11; *U.S. Trustee* v. *Unofficial Comm. of Equity Sec. Holders (In re Zenith Elecs. Corp.)*, 329 F.3d 338, 345–48 (3d Cir. 2003); *In re United Artists Theatre Co.*, 315 F.3d at 228; *MAC Panel Co.* v. *Va. Panel Corp.*, 283 F.3d 622, 625–27 (4th Cir. 2002); *Nordhoff Invs.*, 258 F.3d at 184–91; *In re Grimland*, 243 F.3d at 231–32; *In re GWI PSC 1*, 230 F.3d at 799–805; *In re PWS Holding Corp.*, 228 F.3d at 235–37; *S.S. Retail Stores Corp.* v. *Ekstrom (In re S.S. Retail Stores Corp.)*, 216 F.3d 882, 884–85 (9th Cir. 2000); *In re Cont'l Airlines*, 203 F.3d at 209–11; *Nationwide Mut. Ins. Prods.* v. *Berryman Prods. Inc. (In re Berryman Prods., Inc.)*, 159 F.3d 941, 943–46 (5th Cir. 1998); *Chateaugay III*, 94 F.3d at 775–76; *South St. Seaport L.P.* v. *Burger Boys, Inc. (In re Burger Boys, Inc.)*, 94 F.3d 755, 759–60 (2d Cir. 1996); *In re Cont'l Airlines*, 91 F.3d at 557–67; *Resolution Trust Corp.* v. *Best Prods. Co. (In re Best Prods. Co.)*, 68 F.3d 26, 29–30 (2d Cir. 1995); *Manges* v. *Seattle-First Nat'l Bank (In re Manges)*, 29 F.3d 1034, 1038–43 (5th Cir. 1994); *In re UNR Indus.*, Inc., 20 F.3d 766, 768–71 (7th Cir. 1994); *Chateaugay II*, 10 F.3d at 952–54; *In re Specialty Equip. Cos.*, 3 F.3d 1043, 1047–49 (7th Cir. 1993); *In re Spiritos*, 992 F.2d at 1006–07; *Official Comm. of Unsecured Creditors of LTV Aerospace & Defense Co.* v. *Official Comm. of Unsecured Creditors*

of LTV Steel Co. (In re Chateaugay Corp.), 988 F.2d 322, 325–27 (2d Cir. 1993) ("*Chateaugay I*"); *In re Pub. Serv. Co. of N.H.*, 963 F.2d at 471–76; *In re Club Assocs.*, 956 F.3d at 1069–71; *Haliburton Serv.* v. *Crystal Oil Co. (In re Crystal Oil Co.)*, 854 F.2d 79, 81–82 (5th Cir. 1988); *Miami Ctr. Ltd. P'ship* v. *Bank of N.Y.*, 820 F.2d 376, 378–80 (11th Cir. 1987); *In re AOV Indus., Inc.*, 792 F.2d at 1146–50; *Trone* v. *Roberts Farms, Inc. (In re Roberts Farms, Inc.)*, 652 F.2d 793, 796–98 (9th Cir. 1981).

Moreover, the deep divisions among the Circuits are, at this point, well entrenched. The Second Circuit cited two of its prior decisions as supporting a presumption of mootness after substantial consummation. See Pet. App. 9a (citing *Chateaugay III* and *Chateaugay II*). And district courts in the Second Circuit routinely apply the presumption to appeals following substantial consummation of a plan. See *Cyrus Select Opportunities Master Fund, Ltd.* v. *Ion Media Networks, Inc.* (*In re Ion Media Networks, Inc.*, 480 B.R. 494, 501 (S.D.N.Y. 2012) (relying on the decision below and holding that appellant "failed to overcome the presumption of equitable mootness"); *In re Motors Liquidation Co.*, No. 10 Civ. 9094 (RMB), 2011 WL 1842224, at *5 (S.D.N.Y. May 10, 2012) (appellant had not "overcome the strong presumption that its appeal is moot"); *Freeman* v. *Journal Register Co.*, 452 B.R. 367, 372 (S.D.N.Y. 2010) (applying "a 'strong presumption'" of mootness); *Bernardez* v. *Pawlowski (In re Pawlowski)*, 428 B.R. 545, 550 (E.D.N.Y. 2009) (appellant "fail[ed] to rebut the resulting presumption of mootness" after substantial plan consummation); *Windels Marx Lane & Mittendorf LLP* v. *Source Enters., Inc. (In re Source Enters.,*

Inc.), 392 B.R. 541, 548 (S.D.N.Y. 2008) (applying "'a strong presumption'" of mootness); *Compania Internacional Financiera S.A.* v. *Calpine Corp. (In re Calpine Corp.)*, 390 B.R. 508, 518 (S.D.N.Y. 2008) (appellants failed "to rebut the presumption that the [a]ppeals are moot"); *Kenton County Bondholders Comm.* v. *Delta Air Lines, Inc. (In re Delta Air Lines, Inc.)*, 374 B.R. 516, 522 (S.D.N.Y. 2007) (applying "'a strong presumption'" of mootness); *ACC Commc'ns Grp.* v. *Adelphia Commc'ns Corp. (In re Adelphia Commc'ns Corp.)*, 367 B.R. 84, 94 (S.D.N.Y. 2007) (appellants "fail[ed] to meet their burden" to overcome the "presumption of mootness"); *Loral Stockholders Protective Comm.* v. *Loral Space & Commc'ns Ltd. (In re Loral Space & Commc'ns Ltd.)*, 342 B.R. 132, 138 (S.D.N.Y. 2006) (appellant failed "to rebut the presumption that its appeal is moot").

In the Circuits that have rejected any mootness presumption, by contrast, courts repeatedly put the burden squarely on the proponent of an appeal's dismissal. See, *e.g.*, *Maxwell Techs., Inc.* v. *ISE Corp. (In re ISE Corp.)*, No. 11 Civ. 2704 L(NLS), 2012 WL 4793068, at *2 (S.D. Cal. Oct. 9, 2012) ("[T]he 'party moving for dismissal on mootness grounds bears a heavy burden.'"); *Meritage Homes of Nev., Inc.* v. *JPMorgan Chase Bank, N.A. (In re South Edge LLC)*, 478 B.R. 403, 412 (D. Nev. 2012) (same); *Friesen* v. *Seacoast Capital Partners II, L.P. (In re QuVIS, Inc.)*, 469 B.R. 353, 363 (D. Kan. 2012) ("The party asserting lack of jurisdiction based on mootness bears the burden of proof under both the constitutional and equitable mootness doctrines."); *In re VOIP, Inc.*, 461 B.R. 899, 903 n.4 (S.D. Fla. 2011) ("The burden of establishing mootness is on the party seeking dismissal."); *In re Anderson*, 349 B.R.

448, 454 (E.D. Va. 2006) ("[A]ppellees, as the moving parties, bear the burden of showing that Anderson's appeal is equitably moot and should be dismissed.").

Likewise, the Circuits that review a district court's equitable-mootness dismissal only for abuse of discretion have not wavered from that standard of review. See, *e.g.*, *In re Phila. Newspapers, LLC*, 690 F.3d 161, 167 (3d Cir. 2012), pet. for cert. filed, No. 12-642 (Nov. 16, 2012); *In re SemCrude, L.P.*, 456 F. App'x 167, 170 (3d Cir. 2012); *Sutton* v. *Weinman, (In re Centrix Fin. LLC*), 394 F. App'x 485, 486 (10th Cir. 2010); *In re Zenith Elecs. Corp.*, 329 F.3d at 343; *Official Comm. of Unsecured Creditors* v. *SPGA, Inc. (In re SPGA, Inc.)*, 34 F. App'x 49, 50 (3d Cir. 2002). And the Circuits that review the district courts' equitable-mootness decisions de novo are also standing pat. See, *e.g.*, *Stokes* v. *Gardner*, No. 11-35233, 2012 WL 1944552, at *1 (9th Cir. May 30, 2012) (unpublished); *Tech. Lending Partners LLC* v. *San Patricio County Cmty. Action Agency (In re San Patricio County Cmty. Action Agency)*, 575 F.3d 553, 557 (5th Cir. 2009); *Premier Entm't Biloxi LLC* v. *Pacific Inv. Mgmt. Co. LLC (In re Premier Entm't Biloxi LLC)*, No. 08-60349, 2009 WL 1616681, at *2 (5th Cir. 2009) (per curiam).

One need not agree with a leading commentator that equitable mootness is a "disgraceful doctrine" (David Gray Carlson, *The Res Judicata Worth of Illegal Bankruptcy Reorganization Plans*, 82 TEMP. L. REV. 351, 413 n.549 (2009)) to recognize that the doctrine constitutes a "substantial barrier to appeals brought by dissenters from the resolution of a bankruptcy case" that "can be dispositive in even the most important bankruptcy matters" (Troy A.

McKenzie, *Judicial Independence, Autonomy, and the Bankruptcy Courts*, 62 STAN. L. REV. 747, 790–91 (2010)). Bankruptcy courts determine legal rights to billions of dollars' worth of assets every year. See THE 2012 BANKRUPTCY YEARBOOK & ALMANAC 28 Kerry A. Mastroianni ed., 22d ed. 2012) (public companies that filed for bankruptcy in 2011 had $104 billion in assets). Those decisions ought not to be so readily insulated from Article III review.

This Court has yet to opine on even the basic contours of equitable mootness. With respect, the time for it to do so has arrived.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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