AMERICAN BANKRUPTCY INSTITUTE

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Confirmation Issues

Alec P. Ostrow, Moderator
Becker, Glynn, Muffly, Chassin & Hosinski LLP

Philip M. Abelson
White & Case LLP

Darren S. Klein
Davis Polk & Wardwell LLP

Edward E. Neiger
ASK LLP

Cullen Drescher Speckhart
Cooley LLP | Washington, D.C.

Hon. Michael E. Wiles
U.S. Bankruptcy Court (S.D.N.Y.)

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Draft Materials for CLE Applications

Serta and 1123(a)(4)

I. *In re Serta Simmons Bedding, L.L.C.*, 125 F.4th 555 (5th Cir. 2024) (Feb. 14, 2025 revision) ("Serta")

a. Among the many issues in Serta, the Fifth Circuit was faced with the question of whether an indemnity provided under the plan to certain creditors by the reorganized debtors violates section 1123(a)(4) because only a subset of those creditors will benefit from the indemnity

b. Background: In 2020, Serta agreed with certain lenders to implement an uptier transaction, whereby those lenders were able to improve their position relative to the non-participating lenders. Certain non-participating lenders challenged the uptier transaction, and that challenge remained pending as of the confirmation of the Serta plan. Although claims arising from an original indemnity provided to the participating lenders in the uptier transaction was disallowed under section 502(e)(1)(b) as contingent, Serta agreed to provide a new indemnity under the plan and made that indemnity applicable to all lenders in classes 3 (first-out uptier debt) and 4 (second-out uptier debt), regardless of whether the lenders participated in the uptier transaction.

c. Section 1123(a)(4) provides:

   i. "**(a)**Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall—**(4)** provide the same treatment for each claim or interest of a particular class, unless the holder of a particular claim or interest agrees to a less favorable treatment of such particular claim or interest"

d. Decision:

   i. The Bankruptcy Court confirmed the plan, holding, among other things, that the indemnity was a fair and equitable settlement;

   ii. On direct appeal, the Fifth Circuit reversed;

   iii. The Fifth Circuit found the indemnity to be:

      1. an impermissible end-run around section 502(e)(1)(b)'s disallowance of contingent claims;

      2. violative of section 1123(a)(4)'s equal class treatment requirement because only the participating lenders will receive a benefit from the indemnity – those that bought the debt after the transaction were not subject to potential liability and thus had no need for an indemnity.

II. Backstop and Other Financing Fees

a. To exit chapter 11, a debtor typically needs additional capital. A common method of providing that capital is through a rights offering offered to a group of creditors through the plan confirmation solicitation process.

b. The issue with rights offerings is that, unless there is committed capital backing the offering, the outcome of the offering may be insufficient for the needs of the debtor and will render the plan infeasible. To solve this problem, rights offerings are typically supported by a committed backstop facility. A backstop facility, as the name implies, provides committed financing to ensure that the debtor has the capital needed to effectuate its plan and exit chapter 11, regardless of the outcome of the rights offering itself.

c. When a party commits to providing capital (particularly if that commitment is outstanding for any period of time), the debtor will need to compensate such party for the risk associated with the financing and the time that its capital is committed and cannot be used elsewhere.

d. An additional issue with backstops facilities is that they are most commonly provided by existing stakeholders, which typically are a large group of noteholders or lenders to the debtor. Given that dynamic, backstop fees and other compensation will often create a "haves" and "have nots" scenario, which the Bankruptcy Code generally rejects. The justification, however, is that the backstop parties are providing a benefit to the estate for which they must be compensated. Regardless, backstop compensation remains a point of contention where certain stakeholders are selected to provide financing and other interested parties are excluded.

e. *In re Pacific Drilling S.A.*, Case No. 17-13193 (MEW), 2018 WL 11435661 (Oct. 1, 2018) ("*Pacific Drilling*")

   i. One of the first cases to address this tension was *Pacific Drilling*, where Judge Wiles in the Southern District of New York questioned the propriety of approving a backstop proposal with fees and other compensation that seemed excessive. While Judge Wiles ultimately approved the proposal, he did so after noting that none of the stakeholders objected to the arrangement and expressing deep skepticism of a dynamic where the larger creditors can decide among themselves how to divide the value of the estate. Notably, though Judge Wiles addressed the potential threat to the equality among similarly-situated creditors that goes to the heart of section 1123(a)(4), that section was not specifically addressed in *Pacific Drilling*.

f. After *Pacific Drilling*, several courts addressed whether backstop fees provided to certain creditors was impermissible, each noting that section 1123(a)(4) did not preclude the provision of backstop fees to creditors so long as such fees were based on their new money contributions (and not distributions under the plan), even where the opportunity to provide financing is not available to all similarly-situated holders:

   i. In re Peabody Energy Corp., 933 F.3d 918, 925 (8th Cir. 2019) ("[A] reorganization plan may treat one set of claimholders more favorably than another so long as the treatment is not for the claim but for distinct, legitimate rights or contributions from the favored group separate from the claim");

   ii. In re LATAM Airlines Grp S.A., 2022 WL 2541298 (Bankr. S.D.N.Y. July 7, 2022) (holding that backstop fees and consideration were distributed to certain creditors "in consideration for their commitments described in" approved backstop agreements and did not violate section 1123(a)(4));

   iii. In re ConvergeOne Holdings, Inc., Case No. 24-90194-11 (CML) (Bank. S.D. Tex. May 23, 2024) ("[c]reditors should not confuse similar treatment of claims with equal treatment of claimants. Parties can receive the same distribution in a class and then a subset of those creditors can receive other forms of compensation for matters unrelated to their claim assuming there's a justification for it").

III. Attempted Application of Serta to Backstop Fees

a. WOM S.A., 24-10628 (Bankr. D. Del 2024) (KBO)

i. Background: After an extensive court-approved marketing process, an ad hoc group of noteholders was selected as the winning bidder for a plan transaction whereby the ad hoc group would backstop a $500m rights offering that was offered to all noteholders in the class. For that commitment, the ad hoc group were proposed to receive certain backstop consideration, including fees and professional fees. Shortly after the agreement was reached by the debtors with the ad hoc group on the plan proposal and before the disclosure statement was approved, the debtors moved to approve the backstop agreement. That motion was approved over the objection of a splinter group of noteholders, which objected to the consideration as being excessive and unnecessary. The ad hoc group reserved the right to contest the issue at confirmation.

ii. Plan Objection: As previewed, the splinter ad hoc group objected to the plan on the basis, among others, that the backstop consideration provided the other ad hoc group an "outsized recovery" in violation of the equal treatment requirement in section 1123(a)(4). As support, the ad hoc group cited *Serta* and *Pacific Drilling*. In particular, the ad hoc group cited *Serta* for the concept that disparate treatment is a matter of "substance rather than form", and that the substance of the backstop consideration was to provide a greater recovery under the plan than that provided to similarly-situated creditors. The debtors responded that the propriety of the backstop consideration was approved several months earlier and should not be revisited at confirmation and, even if it had not been previously approved, section 1123(a)(4) was not violated because the consideration was unrelated to the plan distributions to the ad hoc group. As to *Serta*, the debtors noted that the indemnity provided in *Serta* was part of the plan distributions, and not for separate value provided by the creditors.

iii. Ruling: The Bankruptcy Court agreed with the debtors, finding that the question of the backstop fees and whether they were reasonable was answered at the backstop approval stage. Judge Owens did acknowledge that it was possible for backstop consideration to be excessive to the commitment provided by the creditors, but the testimony at the backstop approval stage was uncontested that the backstop consideration was reasonable and the plan proposal the best available. Judge Owens further found that the prior approval of backstop compensation demonstrates that it was on account of the backstop and unrelated to the plan distributions.

iv. Upshot: On its face, *Serta* does not fit easily with an objection to backstop compensation because the compensation provided to the backstop parties is not often characterized as plan distributions, as was the indemnity granted in *Serta*. As Judge Owens noted, however, there is a world in which the proposed backstop compensation is not in line with the benefit provided by the backstop and thus it can be characterized as something akin to plan

consideration. In that case, section 1123(a)(4) may be implicated. *WOM* was not that case, but it nonetheless has lessons for excluded parties.

Insurance Issues in the Confirmation Process

I. Insurance carriers have an increasing voice in the confirmation of a plan post *Truck Insurance Exchange v. Kaiser Gypsum Co., Inc.*, 603 U.S. 204 (2024)

a. Prior to *Truck Insurance Exchange v. Kaiser Gypsum Co., Inc*., insurers had limited standing in bankruptcy due to the insurance neutrality standard. An insurer did not have standing if the bankruptcy plan was considered "insurance neutral," that is, if the bankruptcy plan did not increase the insurer's pre-bankruptcy obligations or impair their pre-bankruptcy policy rights.

b. *Truck Insurance Exchange v. Kaiser Gypsum Co., Inc*. rejected the insurance neutrality standard in evaluating an insurer's standing.

i. Holding: U.S. Supreme Court unanimously held that insurers with financial responsibility for bankruptcy claims are "parties in interest" under Chapter 11, giving them standing to object to reorganization plans. The court held that while insurance neutrality is critical, it overlooks the ways bankruptcy proceedings and reorganization plans can alter and impair insurer interests.

ii. Brief case summary:

1. Issue: Kaiser Gypsum faced asbestos-related lawsuits and filed for Chapter 11 with its parent company and Truck Insurance Exchange, Kaiser's primary insurer, (the "Insurer") opposed the proposed reorganization plan on the basis that there were fraudulent claims due to unequal treatment of insured vs. uninsured claims. The Insurer argued the plan would alter its contractual insurance rights.
2. Analysis: The court ruled that Section 1109(b) should be interpreted broadly to promote fair bankruptcy proceedings. The court found that insurers can be directly harmed by reorganization plans (e.g., loss of control over claims, increased fraudulent claims, loss of contribution rights). Finally, the court recognized insurers may be the only party with an incentive to challenge flawed plans.

c. Takeaways

i. Now, insurers with financial responsibility for claims in bankruptcy have standing on any issue, including objecting to confirmation of a plan. Note that this gives insurers a seat at the table and the ability to extend the confirmation process if they find certain issues objectionable.

ii. Concerning 524(g) trusts, the court appeared to recognize the large financial impact these trusts can have on insurers, debtors, and other stakeholders and are thus more likely to consider the interests of those insurers in future asbestos-related bankruptcy cases.

II. Valuation and Recording of Claims

i. Claims are evaluated by the Debtors through streamlined processes that do not involve full discovery and defense by insurance counsel due to time constraints and are subject to challenge by insurers.

ii. Insurers may take issue with the use of master ballots for claims, arguing that a debtor can influence the vote count using an inflated master ballot and that the individuals voting are not certain to actually be real claimants against the Debtor in the case.

iii. In *In re Red River Talc*, the court denied the Debtors' plan confirmation because, in part, the plan had "numerous prepetition voting irregularities and solicitation hiccups that make it impossible to certify the vote," including a "controversial vote switch that did not follow the tabulation procedures in the Master Ballots and the disclosure statement." *See* In re Red River Talc LLC, 2025 WL 1029302, *3 (Bankr. S.D. Tex. 2025)**.** The insurance companies argued that the plan did not satisfy § 1129(a)(3) because it violates both state and bankruptcy law by abridging insurers' rights and was not "insurance neutral." *See also In re Imerys Talc America, Inc.*, 2021 WL 4786093, at *11 (Bankr. D. Del. Oct. 13, 2021) (excluded master ballots cast by law firm that "performed zero diligence to discern which of its clients, if any, had been exposed to talc, much less to Debtor's talc")

III. Insurance as an Estate Asset

a. Insurance is treated as an estate asset that any unsecured creditor could recover upon regardless of whether such creditor could recover on that claim outside of bankruptcy

i. In general, the debtor has an interest in its insurance *policy* while the named insureds have an interest in the *proceeds* of the policy.

1. In the context of a D&O policy, Delaware courts will consider proceeds property of the estate when:
    1. The debtor receives direct coverage;
    2. The debtor and its officers are both covered, and depletion of the proceeds would proportionally diminish assets available to other creditors; and
    3. The policy provides indemnification coverage that is beyond merely hypothetical, possible, or speculative. *In re Allied Digital Techns. Corp.*, 306 B.R. 505, 512 (Bankr. D. Del. 2004). Proceeds are generally not property of the estate when the policy provides only direct coverage to the directors and not the debtor. *Id.*; *see also In re Archdiocese of Saint Paul & Minneapolis*, 579 B.R. 188, 200-01 (Bankr. D. Minn. 2017) (discussing the *Allied Digital* analysis).

ii. Courts have applied a similar analysis to mass tort cases.

1. *In re Boy Scouts of Am.*, 642 B.R. 504, 572-73 (Bankr. D. Del. 2022) aff'd by *In re Boy Scouts of Am., 2025 WL 1377408* (3d. Cir. May

13, 2025) (holding that insurance policies are property of the estate and the bankruptcy did not alter rights under those contracts).
2. *In re W.R. Grace & Co.*, 475 B.R. 34, 82-84 (D. Del. 2012) (party claiming interest in insurance proceeds must demonstrate entitlement).
3. In mass tort bankruptcies, courts "[tend] to include insurance proceeds as property of the estate to avoid a 'free-for-all against the insurer.'" *W.R. Grace & Co.*, 475 B.R. at 82 (citing *Houston v. Edgeworth*, 993 F.2d 51, 56 n.21 (5th Cir. 1993)).

b. Insurance policies and/or proceeds become accessible to general unsecured creditors when either:
   i. The debtor and the insurer(s) execute a buy-back agreement by which the insurer purchases the policies that it issued to the debtor; or
   ii. The debtor assigns the policies and/or the proceeds to the litigating trust.
c. Certain courts have allowed claimants who otherwise wouldn't recover under the policies to recover from a settlement consisting of the proceeds. *See, e.g.*, *In re Caribbean Petroleum Corp.*, 2013 WL 950361 (Bankr. D. Del. March 11, 2013), *aff'd*, 580 Fed. App'x 82 (3d Cir. 2014). However, other plans have accounted for this issue and have created separate classes of trusts. *See In re Boy Scouts of Am.*, 642 B.R. 504 (Bankr. D. Del. 2022); *In re Congoleum Corp.*, 362 B.R. 167 (Bankr. D.N.J. 2007); *In re Nutraquest, Inc.*, 434 F.3d 639 (3d Cir. 2006)

IV. Insurance Rights and Litigation Post-Confirmation

a. While a bankruptcy discharge releases the debtor from personal liability for certain debts, it generally does not affect the liability of insurers under their policies.
   i. Non-bankruptcy laws generally define parties' property rights. See *Butner v. United States*, 440 U.S. 48, 55 (1979).
b. If the case is delayed creating larger than accounted for administrative expenses, post-confirmation trusts may not have sufficient resources to litigate with insurers. This creates an incentive for insurers to delay the confirmation process as long as possible.

Exculpation and Gatekeeping Injunctions

I. What Is Exculpation?

a. Exculpation is an exoneration from any liability arising from a bankruptcy case for those participating in conducting a successful chapter 11 case, enforced by an injunction in a chapter 11 plan. It generally has exceptions for willful misconduct and gross negligence.
b. It differs from what is usually referred to as a nonconsensual third-party release, because it concerns only actions that occur during the bankruptcy case, and does not affect a third-party's liability on a debt incurred by the debtor. *Blixseth v. Credit Suisse*, 961 F.3d 1074, 1082 (9th Cir. 2020).
c. Examples:
   i. *Bed Bath & Beyond:* "No Exculpated Party shall have or incur liability for, and each Exculpated Party is exculpated from, any Cause of Action or claim

related to any act or omission in connection with, relating to, or arising out of, the Chapter 11 Cases, the formulation, preparation, dissemination, negotiation, or filing of the DIP Facility, the Disclosure Statement, the Plan, the Plan Supplement and the Asset Sale Transactions, the pursuit of Confirmation, the pursuit of Consummation, the administration and implementation of the Plan, including the issuance or distribution of debt, and/or securities pursuant to the Plan, or the distribution of property under the Plan or any other related agreement, except for Claims related to any act or omission that is determined in a final order by a court of competent jurisdiction to have constituted actual fraud, willful misconduct, or gross negligence, but in all respects such Entities shall be entitled to rely upon the advice of counsel with respect to their duties and responsibilities pursuant to the Plan." Plan, Article X.E (para. 1).

ii. *Celsius Network:* "Effective as of the Effective Date, to the fullest extent permissible under applicable law [qualification and exception omitted], no Exculpated Party shall have or incur liability for, and each Exculpated Party hereby is exculpated from any claim or Cause of Action related to, any act or omission in connection with, relating to, or arising out of the negotiation, solicitation, confirmation, execution, or implementation (to the extent on or prior to the Effective Date) of, as applicable, the Chapter 11 Cases, the Plan Sponsor Agreement, the Backup Plan Sponsor Agreement, the Definitive Documents (as defined in the Backup Plan Sponsor Agreement), the Plan (including, for the avoidance of doubt, the Plan Supplement), the Disclosure Statement, the New Organizational Documents, [other specific Plan transactions], or any restructuring transaction, contract, instrument, release, or other agreement or document created or entered into during the Chapter 11 Cases in connection with the Chapter 11 Cases [other named documents], the pursuit of Confirmation, the pursuit of Consummation, the administration and implementation of the Plan [including specific implementation transactions], or any other related agreement or upon any other related act or omission, transaction, agreement event, or other occurrence taking place on or before the Effective Date (including, for the avoidance of doubt, providing any legal opinion required by any Entity regarding any transaction, contract, instrument, document, or other agreement contemplated by the Plan or the reliance by any Exculpated Party on the Plan or the Confirmation Order in lieu of such legal opinion), except for claims related to any act or omission that is determined by a Final Order by a court of competent jurisdiction to have constituted bad faith, fraud, willful misconduct, or gross negligence, but in all respects such Entities shall be entitled to reasonably rely upon the advice of counsel with respect to their duties and responsibilities pursuant to the Plan." Plan Article VIII.E (para. 1).

iii. *Roman Catholic Diocese of Rockville Centre:* "Effective as of the Effective Date, to the fullest extent permissible under applicable law [qualification and exception omitted], no Exculpated Party shall have or incur liability for, and each Exculpated Party hereby is exculpated from any claim or Cause of

> Action related to, any act or omission occurring on or after the applicable Petition Date through and including the Effective Date in connection with, relating to, or arising out of the negotiation, solicitation, confirmation, execution, or implementation of, as applicable, the Chapter 11 Cases, the Plan Documents, the pursuit of entry of the Confirmation Order, the administration and implementation of the Plan, including the distribution of property under the Plan, or any other related agreement, or any other related agreement, or any restructuring transaction, contract, instrument, release, or other agreement or document created or entered into during the Chapter 11 Cases in connection with the Chapter 11 Cases, or upon any other act or omission, transaction, agreement, event, or other occurrence related or relating to the foregoing; provided, however, that this Article XI.J shall not apply to release (a) [obligations imposed or assumed by the Plan], (b) any Claims or Causes of Action arising from or related to an act or omission that is judicially determined by a Final Order to have constituted actual fraud or willful misconduct on the part of the Exculpated Party, or (c) [claims reinstated under the Plan]." Plan, Article XI.J.

II. Roots of Exculpation

a. Official Committee Immunity: Courts have held that the functions of an official committee set forth in 11 U.S.C. § 1103(c) imply both a fiduciary duty and a qualified immunity. *Pan Am Corp. v. Delta Air Lines, Inc.*, 175 B.R. 438, 514 (S.D.N.Y. 1994); *In re L.F. Rothschild Holdings, Inc.*, 163 B.R. 45, 49 (S.D.N.Y. 1994). The exculpation of committee members and their professionals restates the principle of qualified immunity. *In re PWS Holding Corp.*, 228 F.3d 224, 246 (3d Cir. 2000).

b. Standard of Conduct for Trustee Tort Liability: A plan that exculpates a trustee for anything other than gross negligence is consistent with the standard of personal liability for bankruptcy trustees. *In re Hilal*, 534 F.3d 498, 501 (5th Cir. 2008) (citing *In re Smyth*, 207 F.3d 758, 761-62 (5th Cir. 2000) (adopting gross negligence standard from Nat'l Bankr. Review Comm'n Final Report § 3.3.2, at 859 (1997)). The gross negligence standard has not been adopted in all circuits. The Supreme Court has held that trustees are liable for breach of fiduciary duty. *Mosser v. Darrow*, 341 U.S. 267, 272 (1951). Other courts of appeal have held trustee liable for intentional and negligent violations of duties imposed by law, *In re Gorski*, 766 F.2d 723, 727 (2d Cir. 1985); but not for mistakes in judgment where discretion is allowed. *In re Cochise College Park, Inc.*, 703 F.2d 1339, 1357 (9th Cir. 1983).

c. Extension to All Estate Professionals: The permissible set of persons entitled to exculpation has been extended to include all estate professionals. *In re Mallinckrodt PLC*, 639 B.R. 837, 882 (Bankr. D. Del. 2022); *In re Washington Mutual, Inc.*, 442 B.R. 314, 348 (Bankr. D. Del. 2011).

d. Extension to All Court-Supervised Transactions: "In the absence of gross negligence or intentional wrongdoing, parties should not be liable for doing things that the Court authorized them do and that the Court decided were reasonable things to do." *In re Aegean Marine Petroleum Network, Inc.*, 599 B.R. 717, 721 (Bankr. S.D.N.Y. 2019). The exculpation provision "requires, in effect, that any claims in

connection with the bankruptcy case be raised in the case and not saved for future litigation." *In re Granite Broadcasting Corp.*, 369 B.R. 120, 139 (Bankr. S.D.N.Y. 2007).

e. Securities Law Safe Harbor Provisions in Bankruptcy Code: The exemption from liability under the securities laws for good faith solicitations of acceptances or rejections of a plan in connection with a court-approved disclosure statement under 11 U.S.C. § 1125(e), additionally protects against common law liability and provides the foundation for a plan exculpation provision concerning such liability. *In re Davis Offshore, LP*, 644 F.3d 259, 266-69 (5th Cir. 2011).

III. What Is Gatekeeping?

a. Gatekeeping is a requirement imposed by a chapter 11 plan and enforced by an injunction against non-debtors who wish to sue third parties who are protected by the plan on the basis of claims that supposedly have not been otherwise enjoined by the plan – because such claims have been released by debtors, released by the non-debtors themselves, or are subject to exculpation – to obtain from the bankruptcy court a prior (i) determination that the proposed lawsuit is not one belonging to a prohibited category, and (ii) authorization to file the lawsuit.

b. Examples:

i. *Bed Bath & Beyond*: "From and after the Effective Date, any Entity [exceptions omitted] that opted out of (or otherwise did not participate in) the [third-party releases] may not assert any claim or other Cause of Action against any Released Party for which it is asserted or implied that such claim or other Cause of Action against any Released Party is not subject to [the releases by the Debtors] without first obtaining a Final Order from the Bankruptcy Court (a) determining, after notice and hearing, that such claim or other Cause of Action is not subject to [the releases by the Debtors] and (b) specifically authorizing such Person or Entity to bring such claim or other Cause of Action against any such Released Party." Plan, Article X.D (para. 2).

ii. *Celsius Network:* "No Releasing Party may commence or pursue a Claim or Cause of Action of any kind against the Debtors, the Post-Effective Date Debtors, the Exculpated Parties, or the Released Parties the (i) is a core claim that arises from or relates to the Chapter 11 Cases and (ii) relates to or is reasonably likely to relate to any act or omission in connection with, relating to, or arising out of a Claim or Cause of Action subject to [releases by the Debtors, releases by the Releasing Parties, or subject to exculpation], without the Bankruptcy Court (x) first determining, after notice and a hearing, that such Claim or Cause of Action represents a colorable Claim of any kind, and (y) specifically, authorizing such Person or Entity to bring such Claim or Cause of Action against any such Debtor, Post-Effective Date Debtor, Exculpated Party, or Released Party. The Bankruptcy Court will have sole and exclusive jurisdiction to adjudicate whether such a colorable Claim or Causes [sic] of Action exists." Plan, Article VIII.F (para. 3).

iii. *Roman Catholic Diocese of Rockville Centre:* "To the extent permitted by law, and subject in all respects to this Article XI, no Enjoined Party may

commence or pursue against any Protected Party (a) an Abuse Claim or (b) any other Claim or Cause of Action that arose or arises from or is related to an Abuse Claim, the Chapter 11 Cases, the negotiation of the Plan, the administration of the Plan or property distributed under the Plan, the wind-down or reorganization of the business of the Debtor, the Additional Debtors, the Reorganized Debtor, the Reorganized Additional Debtors, the administration of the Trust, or the transactions in furtherance of the foregoing with the Bankruptcy Court (i) first determining, after notice and a hearing, the such Claim or Cause of Action represents a colorable Claim against a Protected Party and (ii) subject in all respects to the Channeling Injunction and the Settling Insurer and Supplemental Injunction, specifically authorizing such Enjoined Party to bring such Claim or Cause of Action against any Protected Party. The Bankruptcy Court will have sole and exclusive jurisdiction to determine whether a Claim or Cause of Action is colorable and, only to the extent legally permissible and is provided for in Article XII shall have jurisdiction to adjudicate the underlying Claim or Cause of Action." Plan, Article XI.H (para. 1).

IV. Roots of Gatekeeping

a. The *Barton* Doctrine: A receiver appointed by a court to administer assets may not be sued without leave of the appointing court. *Barton v. Barbour*, 104 U.S. 126, 136-37 (1881). This doctrine applies to trustees in bankruptcy. *In re VistaCare Grp., LLC*, 678 F.3d 218, 224 (3d Cir. 2012) (collecting cases); *Vass v. Conron Bros. Co.*, 59 F.2d 969, 970 (2d Cir. 1932) (L. Hand, J.). It also applies to counsel for trustees. *In re DeLorean Motor Co.*, 991 F.2d 1236, 1241 (6th Cir. 1993). It also applies to persons performing the duties of a trustee whose appointments were approved by the court, and who are thus the "functional equivalent" of a trustee. *Carter v. Rodgers*, 220 F.3d 1249, 1252-53 & n.4 (11th Cir. 2000).

b. There is a statutory exception, 28 U.S.C. § 959(a), which provides that trustees, receivers, and debtors in possession are suable without leave of the court appointing them for "acts or transactions in carrying on business," but any such lawsuit is "subject to the general equity power of [the appointing] court so far the same may be necessary to the ends of justice, but this shall not deprive a litigant of his right to trial by jury." This exception does not apply when the actions involving liquidating a business as opposed to operating it. *In re Lehal Realty Assocs.*, 101 F.3d 272, 276 (2d Cir. 1996).

c. 11 U.S.C. § 105(a) empowers a bankruptcy court to enjoin a lawsuit filed in violation of the *Barton* doctrine. *In re Crown Vantage, Inc.*, 421 F.3d 963, 977 (9th Cir. 2005); *DeLorean*, 991 F.2d at 1242-43.

d. Extension to Debtors in Possession: The *Barton* doctrine has been extended to debtors in possession and their officers. *In re Silver Oak Homes, Ltd.,* 167 B.R. 389, 394-95 (Bankr. D. Md. 1994) (citing 11 U.S.C. § 1107(a), giving a debtor in possession the rights, powers, and duties of a trustee).

e. Extension to Committee Members: The *Barton* doctrine has been extended to official committee members. "We conclude that *Barton* applies to UCC members

. . . who are sued for acts performed in their official capacities." *In re Yellowstone Mountain Club, LLC*, 841 F.3d 1090, 1095 (9th Cir. 2016).

V. Who Should Be Protected by Exculpation and Gatekeeping Injunctions?

a. Extension to Non-Estate Fiduciaries Participating in RSA Agreements: Christopher A. Jones & Alexandra G. DeSimone, *Courts Should Approve Exculpation for the Pre-Petition Conduct of RSA Parties*, Am. Bankr. Inst. L.J. (Jul. 2022) (citing *In re Murray Metallurgical Coal Holdings LLC*, 623 B.R. 444, 504 (Bankr. S.D. Ohio 2021); *Aegean Marine Petroleum*, 599 B.R. at 721) (as to exculpation).

b. Restriction to Estate Fiduciaries: *Highland Capital Management* cases.

i. *In re Highland Capital Management, LP (Highland I)*, 48 F.4th 419, 437-39 (5th Cir. 2022) (as to exculpation): The court equated non-debtor party exculpation with impermissible non-consensual third-party releases as violative of 11 U.S.C. § 524(e) under existing Fifth Circuit precedents (pre-*Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024)), and restricted reversed confirmation of a plan that exculpated non-debtor parties other than members of the creditors' committee, but otherwise affirmed the injunction and gatekeeping provisions in the plan.

ii. *In re Highland Capital Management, LP (Highland II),* 132 F.4th 353, 358-62 (5th Cir. 2025) (as to gatekeeping): On remand, the bankruptcy court confirmed a plan that did not change the gatekeeping provision. On second trip to the Fifth Circuit, confirmation was again reversed. The court held that the bankruptcy court had failed to follow the court's instructions in *Highland I*, when it failed to restrict the persons protected by the gatekeeping provision to those permissibly protected by the exculpation provisions, namely, the debtor and creditors' committee parties, and that gatekeeping protecting other non-debtors was impermissible. *See also* Michael Lathwell, *The Permissibility of Exculpation Clauses Post-Purdue*, Am. Bankr. Inst. L.J. (Mar. 2005).

Equitable Mootness

I. The Doctrine

a. Pursuant to the doctrine of equitable mootness, which applies to bankruptcy appeals, a court may decline to hear an appeal where a plan of reorganization has been substantially implemented and where granting relief would affect third parties not before the court

- Equitable mootness is premised on the notion that practical considerations and fairness to third parties may justify a court's decision not to hear an otherwise valid appeal of an order approving confirmation of a plan

b. The doctrine seeks to balance the competing interests of plan proponents versus opponents

- Parties may have competing interests in the speed of implementation of the plan

1. On one hand, if the plan is implemented quickly, the debtor and other parties in interest who support the plan will benefit from swiftly executing the plan terms
2. By contrast, opponents of the plan may seek to exercise their right to appeal the confirmation order. A lengthy appeals process could stall and possibly permanently block effective resolution for the remaining parties

c. Finality is also a key consideration. Achieving plan support is often the product of hard-fought, complex, multi-party negotiations that would require much time, effort, and resources to renegotiate
d. For the debtor, timeliness is also paramount. Prolonging time in bankruptcy can hinder a debtor's business operations and fresh start
e. For all parties involved, the expenses of further administrative fees can have a substantial impact as the case is prolonged

II. Second Circuit Test

a. The Second Circuit applies the following test for when to apply equitable mootness:
b. When a plan is substantially consummated, an objection is presumed moot. *Beeman v. BGI Creditors' Liquidating Tr. (In re BGI, Inc.)*, 773 F.3d 102, 108 (2d Cir. 2014); *R2 Invs. LDC v. Charter Commc'ns, Inc. (In re Charter Commc'ns, Inc.)*, 691 F.3d 476, 482 (2d Cir. 2012).
    1. A plan is substantially moot when, pursuant to the plan:
        (a) All or substantially all property proposed has been transferred
        (b) Debtor or debtor's successor has assumed, under the plan of business or of the management, all or substantially all property
        (c) Distributions have begun.

    See 11 U.S.C. § 1101(2)
    2. To overcome the presumption, the following factors must be met:
        (a) The court can grant some effective relief
        (b) Such relief will not harm the debtor as a revitalized corporate entity
        (c) Such relief will not unravel the plan
        (d) Parties adversely affected by such relief have notice and an opportunity to participate
        (e) The objector's were diligent in seeking a stay

    See Frito-Lay, Inc. v. LTV Steel Co. (In re Chateaugay Corp.), 10 F.3d 944, 952-53 (2d Cir. 1993)

III. Recent Developments

a. There is a trend among numerous circuit courts toward restricting the doctrine of equitable mootness:
b. In *In re VeroBlue Farms U.S.A. Inc.*, 6 F. 4th 880, 883-84, 891 (8th Cir. Aug. 5, 2024), the Eighth Circuit held that the use of the doctrine should be exception and

should not result in the refusal "to entertain a live appeal over which the court has statutory jurisdiction and when meaningful relief can be awarded"

c. In *In re Nuverra Environmental Solutions, Inc.*, 834 Fed App'x 729 (3d Cir. Jan. 6, 2021), cert. denied, 142 S. Ct. 337 (Oct. 12, 2021), the Third Circuit stated that equitable mootness is a "narrow doctrine" and there should be a "strong presumption that appeals from confirmation orders of reorganization plans need to be decided"
d. This trend has a continued with the Fifth Circuit's decision in *Serta*:
e. In *In re Serta Simmons Bedding*, LLC, 125 F. 4th 555, 585-588 (5th Cir. Dec. 31, 2024), the Fifth Circuit rejected equitable mootness as a bar to reviewing the confirmation order, affirming that this doctrine cannot be "a shield for sharp or unauthorized practices"
    1. The Fifth Circuit analyzed three factors:
        (a) whether a stay was obtained;
        (b) whether the plan was substantially consummated; and (c) whether the relief requested would affect the plan's success or rights of parties not before the court
    2. Despite finding the first two factors weighed in favor of Serta, the third factor weighed against equitable mootness
    3. The Fifth Circuit rejected the argument that it would be unfair to excise the settlement indemnity from the Plan and accepting such an argument would "effectively abolish appellate review of even clearly unlawful provisions in bankruptcy plans"
f. Most recently, the Third Circuit addressed the question of equitable mootness in *In re Boy Scouts of America and Delaware BSA LLC* (Case No. 23-1664) (3rd Cir. May 13, 2025):
g. The plan of reorganization for *Boy Scouts of America* was confirmed in 2022 and was subsequently appealed. The issue of equitable mootness was raised by various parties in submissions to the Third Circuit following the Supreme Court's rejection of nonconsensual third-party releases in *Harrington v. Purdue Pharma* and the Fifth Circuit's *Serta* decision
h. Certain parties appealed requesting the confirmation order be vacated as violating the *Harrington's* prohibition on third-party releases; other parties requested more narrow relief to preserve certain rights to collect defensive costs and excess liability claims from the Settlement Trust established by the plan
i. With respect to vacating the confirmation order, the Third Circuit ruled on statutory mootness grounds
    1. The statutory mootness argument under section 363(m) itself raises important issues
    2. A concurring opinion rejected the statutory mootness argument but would have affirmed on equitable mootness grounds
j. The Third Circuit applied an equitable mootness analysis to the more narrow relief requested by other parties using two factors:
    1. whether the confirmed plan was substantially consummated; and

2. whether the relief requested would (a) fatally scramble the plan and/or (b) significantly harm third parties who justifiably relied on confirmation of the plan

k. While the Third Circuit found that the plan had been substantially consummated, it rejected the equitable mootness argument because "narrow, cabined relief" was requested which the parties carrying the burden did not demonstrate would put the Plan's success at risk

l. As part of its analysis, the Third Circuit emphasized that this doctrine is "limited in scope" and "must be cautiously applied" noting that "bare assertions of inequity and '"Chicken Little" statements' do not suffice"

Mass Tort Cases

I. Purdue Pharma – Non-Consensual Releases

a. Purdue Pharma was an opioid maker founded by the Sackler family and was responsible for hundreds of thousands of opioid overdoses and deaths.

b. Purdue filed bankruptcy in 2019, with the Sacklers planning to convert the company into a public benefit company and pay billions in exchange for releases from any personal liability. Importantly the Sacklers themselves did not file for bankruptcy.

c. In September 2021 Purdue filed a $4.5B bankruptcy plan that would be financed by the Sacklers, but would eliminate the family's exposure to civil litigation. Bankruptcy Judge Robert Drain confirmed this plan, finding that the Sackler's contributions would be more beneficial to opioid victims that years of litigation trying to wrest assets from the Sackler's offshore trusts.

d. The United States Trustee appealed. The plan was overturned by the District Court, holding that the non-consensual releases were not permitted under the Bankruptcy Code.

e. The parties appealed to the Second Circuit, which reversed and held that the Code permitted such releases, analogizing to past cases involving asbestos liability and relying on the inherent equitable powers of bankruptcy courts.

f. The United States Supreme Court overturned the Second Circuit in the case of *Harrington v. Purdue Pharma L.P.* on June 27, 2024. *Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024). The Supreme Court held that non-consensual non-debtor releases are not authorized by the Bankruptcy Code, setting the plan process in the bankruptcy to square one. However, *Harrington* left questions open including what kind of consent is required for a non-debtor to receive a release in a Chapter 11 plan.

g. Subsequently Purdue and its creditors have negotiated a new bankruptcy plan as of March 2025 that is currently in the confirmation process.

II. J&J – The "Texas Two-Step"

a. The "Texas two-step" involves creating a new subsidiary company under a Texas corporate law provision that allows a company to split itself into two entities with the parent company exercising control over the newly spun-off subsidiary.

b. The parent can then put all of the liabilities for a particular class of claim into the spin off, then have that new company file for Chapter 11 bankruptcy to try to channel tort claims while keeping the main company's assets entirely separate and out of bankruptcy.

c. Johnson & Johnson tried this maneuver with its tort liability related to talcum powder products, which have been linked to various cancers.

d. J&J created a new entity, LTL Management LLC, then filed bankruptcy for LTL in North Carolina. The Bankruptcy Court allowed the case to continue after parties filed a motion to dismiss. But the Third Circuit overturned, finding that LTL's filing was in bad faith as LTL had no financial distress – J&J had agreed as part of the filing to backstop all liabilities that LTL may have incurred. *In re LTL Management, LLC*, 64 F.4th 84 (3d Cir. 2023) (dismissing first case).

e. Amazingly, after the Third Circuit dismissed the first case, J&J tried the same thing twice again. In April 2023, LTL filed bankruptcy in New Jersey, with that case being dismissed on the same basis—that LTL's filing was not based on any financial distress. *In re LTL Management, LLC*, Nos. 23-2971, 23-2971, 2024 WL 3540467 (3d Cir. Jul. 25, 2024) (affirming dismissal of second case). J&J then formed a new entity, Red River Talc, LLC and filed another Chapter 11 in the Southern District of Texas with the support of a larger creditor group. J&J solicited a proposed Chapter 11 plan, which it believed would be confirmable. That case was also dismissed on the basis of procedural irregularities in soliciting the plan pre-bankruptcy and the fact that the plan would not be confirmable as presented. *In re Red River Talc LLC*, Case No. 24-90505, 2025 WL 1029302 (Bankr. S.D. Tex. Mar. 31, 2025)

f. Likewise, 3M used the same technique to try to offload liabilities related to combat ear protection, creating a spin-off entity called Aearo and filing bankruptcy in the Southern District of Indiana. As with J&J, 3M said that it would backstop any settlement under the Aearo case, but did not itself file for bankruptcy. *In re Aearo Technologies LLC*, Case No. 22-02890-JJG-11, *et al.*, 2023 WL 3938436 (Bankr. S.D. Ind. Jun. 9, 2023), *appeal dismissed per stipulation*, Nos. 22-2606, *et al.,* 2024 WL 5277357 (7th Cir. Jul. 11, 2024).

g. Some entities have successfully used a Texas two-step procedure, but all three (Georgia Pacific, Saint-Gobain, and Trane Technologies) used it for asbestos liabilities. After J&J it is unlikely that that the "Texas two-step" remains viable.

III. Boy Scouts of America

a. The Boy Scouts confirmed a plan in 2022 that provided approximately $2.4 billion in settlement funds to victims of sex abuse related to Scouting. The settlement was funded through insurance buy backs that released the primary insurance companies (principally Hartford and Chubb) from any further liability under their polices. These polices were in some cases shared with the 250 Local Councils that actually provided the scouting activities nationwide and Chartered Organizations—often schools, religious institutions, and civic associations—that provide facilities and support for scouting activities. The confirmed plan (as in Purdue) contained non-consensual non-debtor releases for settling insurers, the Local Councils and Charter

Organizations, none of whom filed bankruptcy. A small number (144) of the 82,000 victims appealed, claiming that the non-debtor releases violated the Bankruptcy Code. The District Court affirmed the Bankruptcy Court's confirmation decision in April 2023 (all occurring before the Supreme Court's *Harrington* decision that rejected the use of non-consensual non-debtor releases). Some of the non-settling insurance companies (mostly excess insurance carriers) also appealed, seeking a modification to the Plan that would specifically preserve their indemnification rights to collect defense and excess liability costs that they would have been entitled to assert against the primary carriers. Now that the policies were sold to the Debtor and transferred to the Settlement Trust these non-settling insurance companies wanted the plan to be modified to make sure their interest were protected and considered in the Settlement Trust.

b. The appeal went to the Third Circuit, which upheld the bankruptcy plan in May 2025, even after *Purdue*. The Third Circuit reviewed four issues: whether the Bankruptcy Court had subject matter jurisdiction, whether the appeal was moot under Section 363(m) of the Bankruptcy Code; whether the appeal was equitably moot; and finally, the validity of the separate insurer claims.

c. The Third Circuit quickly found that both claims were related to the bankruptcy proceeding and the confirmation process and found that subject matter jurisdiction was proper. *In re Boy Scouts of America*, Nos. 23-1664, *et al.*, 2025 WL 1377408 (3d Cir. May 13, 2025). The Third Circuit also found that a related sale of insurance policies was a sale under Section 363 of the Bankruptcy Code, and inasmuch as the relief requested would unwind that sale, Section 363(m) would bar such relief, mooting the dissenting victims' appeal. Because the Third Circuit found that the appeal by the victim groups was statutorily moot, it did not discuss whether the appeal would be equitably moot as to that group.

d. (In a separate concurrence, Judge Rendell argued that equitable, rather than statutory, mootness should have barred those claims.)

e. However, the separate appeal by the insurers remained, and the Third Circuit concluded that appeal was not equitably moot. Because those insurers were only asking for collateral changes to the Plan rather than unwinding it in its entirety, the Third Circuit considered the merits of the insurer's claim. However, the Third Circuit concluded that except for a technical change for certain insurers (the Allianz Insurers), the Plan was valid and proposed in good faith and need not be modified.

f. The Third Circuit made it clear that its decision was based on timing—unlike the plan in Purdue the BSA plan had been "substantially consummated" and substantial payments were going out to victims prior to the motion to dismiss. The Third Circuit noted that though the BSA plan with nonconsensual third-party releases would not be confirmable after Supreme Court's *Harrington* decision, Supreme Court clearly stated that its decision did not apply retroactively to plans that had been substantially consummated and appeals of asset sales under Section 363 may be limited by Section 363(m) of the Code.

Faculty

Philip Abelson is a partner in the Financial Restructuring and Insolvency Practice at White & Case LLP in New York, where his practice focuses on debtors' and creditors' rights and corporate restructurings. He represents debtors, creditors, official and unofficial committees, bondholders and third parties in both in-court and out-of-court restructurings. Mr. Abelson has been recognized as a "Rising Star" by *Law360*, and as a "Leading Lawyer" by *Chambers USA*. He has spoken on bankruptcy and governance issues, including on Debtwire's panel on Puerto Rico in 2015; ABI's New York City Bankruptcy Conference on municipal bankruptcies, insolvencies and restructurings in 2014; and the American Bar Association's Business Law Section Spring Meeting on chapter 11 current developments in 2013, among others. He also attended the working group session (model insolvency law) of the United Nations Commission on International Trade Law at the United Nations on behalf of the New York State Bar Association. Mr. Abelson received his B.A. from Indiana University and his J.D. from the University of Michigan Law School.

Darren S. Klein, CFA is a partner in Davis Polk & Wardwell LLP's Restructuring Department in New York. He advises on a wide range of corporate restructurings, both in and out of court, and represents debtors, creditors and other strategic parties in bankruptcies, out-of-court workouts, financings, litigation and § 363 sales. Mr. Klein has had a leading role in several of the largest restructurings on both the debtor and creditor side. He has been recognized in the *IFLR1000* as "Highly Regarded" in U.S.: Restructuring and Insolvency for 2018, in the *Legal 500 U.S.* as a "Next Generation Lawyer" in Finance: Restructuring (including Bankruptcy), Corporate, and in the Turnaround Atlas Awards for both "Chapter 11 Restructuring Turnaround of the Year" (Verso Corp. reorganization) and "Energy Deal of the Year (over $100 million to $500 million)" (chapter 11 reorganization of Venoco), both in 2017. Mr. Klein is a member of ABI and the New York Society of Security Analysts. He previously was with NERA, Inc. before heading to law school. Mr. Klein received his A.B. in economics and philosophy from the University of Michigan in 1999, his M.A. from the University of Michigan School of Business in 2000 and his J.D. from Harvard Law School in 2007, where he served as a business editor of the *Harvard Negotiation Law Review*.

Edward E. Neiger is a co-managing partner at ASK LLP in New York, where his practice focuses on representing unsecured trade creditors in complex bankruptcy cases and prosecuting and defending large preferences and fraudulent conveyance actions. He is a nationally recognized leader in both bankruptcy and mass tort law. Prior to joining ASK, Mr. Neiger founded Neiger LLP, where he represented clients in the bankruptcy cases of Lehman Brothers, American Airlines and General Motors, among others. Previously, he was in the bankruptcy group of Weil, Gotshal & Manges LLP, where he worked on behalf of such debtors as Enron, Lehman Brothers, GM and PG&E, and he currently represents thousands of victims of Boy Scout sexual abuse, more than 50,000 victims of Purdue Pharma, and hundreds of victims of the Maui wildfires, among other victims in high-profile mass tort cases. Mr. Neiger is on the board of 2EndTheSitgma and works to help those suffering from addiction, including those incarcerated, get the help they need. At the same time, he fights to hold those responsible for the opioid crisis, especially governments and elected officials, accountable. In the past, Mr. Neiger helped Holocaust survivors recover monetary damages from the German government, including his own grandfather (all of his grandparents are Holocaust survivors and came to the

U.S. as refugees after the Second World War). He is a member of the New York City Bar Association's Imperfect History Committee, which explores and uncovers the racist roots of the NYC Bar Association, and in 2020, he was honored as one ABI's "40 Under 40." Mr. Neiger is the author of the *New York Law Journal*'s "Mass Torts Roundup" and "Bankruptcy Update" columns. He received his undergraduate degree *summa cum laude* from Touro College, where he served as the president of the Pre-Law Society and as editor-in-chief of the *Pre-Law Journal*, and his J.D. in 2004 from Fordham University, where he served on its law review.

Alec P. Ostrow is a partner in the New York law firm of Becker, Glynn, Muffly, Chassin & Hosinski LLP and has been specializing in bankruptcy, creditors' rights, corporate reorganizations, workouts, cross-border insolvency and commercial litigation for more than 40 years. He is a Fellow of the American College of Bankruptcy and since 2000 has been an adjunct professor at St. John's University School of Law in its LL.M. in bankruptcy program. Mr. Ostrow has been selected to *Super Lawyers* since 2006, and in 2020 he was honored with the Marquis Who's Who Albert Nelson Marquis Lifetime Achievement Award. He has lectured on numerous bankruptcy issues, including at conferences sponsored by ABI, the American Bar Association, the American Law Institute - American Bar Association, the American Institute of Certified Public Accountants, the Judicial Conference of the Second Circuit, the National Association of Bankruptcy Trustees, the Association of Insolvency and Restructuring Advisors and the New York State Society of Certified Public Accountants. He also has published many articles on diverse topics in bankruptcy law, including the *American Bankruptcy Law Journal*, the *ABI Law Review* and the *Norton Annual Survey of Bankruptcy Law*. Mr. Ostrow received his undergraduate degree *magna cum laude* from Dartmouth College in 1977 and his J.D. from New York University School of Law in 1980.

Cullen A. Drescher Speckhart is chair of Cooley LLP's business restructuring & reorganization practice and partner in charge of its Washington, D.C., office. She is a top advocate in corporate restructuring and financial litigation, with a diverse practice spanning a range of industries, including health care, life sciences, technology, energy and retail. Ms. Speckhart regularly represents debtors, creditors' committees, trustees and foreign representatives in significant bankruptcy matters throughout the U.S. Having led some of the largest and most significant restructuring engagements in a multitude of jurisdictions, she has deep experience in complex insolvency litigation. Her recent practice experience includes serving as lead restructuring counsel to official creditor constituencies in Mallinckrodt, LTL Management (Johnson & Johnson), Endo International, Le Tote, 24 Hour Fitness and White Stallion Energy. Ms. Speckhart also acts as lead restructuring counsel to companies seeking to reorganize in and out of court and provides business risk management and strategic advice to entities across such industries as technology, life sciences, cyber services and cryptocurrency. Her company-side practice involves representation of public and private debtors in chapter 11 cases, and she often confronts complex emerging legal issues and matters of public importance. Her current work on behalf of companies in bankruptcy includes representing Ascena Retail Group (Ann Taylor, Loft, Lane Bryant), as well as serving as lead restructuring counsel to Enjoy Technology, NS8, PhaseBio Pharmaceuticals, Quanergy Systems and Lucira Health in chapter 11 proceedings. Ms. Speckhart is a frequent speaker on corporate insolvencies, restructuring in life sciences and technology, career and professional development, advocacy and leadership. In 2015, she co-authored the ABI's manual on Chapter 15, and in 2017, she was selected as a member of ABI's inaugural "40 Under 40" class. In 2021, on account of exemplary practice performance and leadership, she was named Restructuring Lawyer of the Year at the Global M&A Network's 13th Annual Turnaround Atlas Awards. Ms.

Speckhart serves on the advisory board of the Institute for Restructuring Studies at the University of Pennsylvania, and her career, practice and leadership experiences have been covered by numerous national media outlets. As part of her work on issues related to diversity, equity and inclusion and women's initiatives, she led a team in designing and delivering a bespoke leadership training program for Cooley professionals seeking development in confidence, public speaking and personal branding. Before entering private practice, Ms. Speckhart clerked for then-Chief Judge Stephen C. St. John of the U.S. Bankruptcy Court for the Eastern District of Virginia. During law school, she was the first prize winner of the ABI's inaugural Bankruptcy Law Student Writing Competition and the first law student ever to receive the Thatcher Prize for Excellence, an award presented annually to a William & Mary graduate student of outstanding scholarship, leadership, service and character. Ms. Speckhart received her B.A. in politics and economics from Georgetown University and her J.D. from the College of William & Mary, Marshall-Wythe School of Law.

Hon. Michael E. Wiles is a U.S. Bankruptcy Judge for the Southern District of New York in New York, sworn in on March 3, 2015. Previously, he was a partner with Debevoise & Plimpton LLP, where he focused on general commercial litigation and bankruptcy. Judge Wiles has presided over many large bankruptcy cases, including *Westinghouse*, *Pacific Drilling*, *Garrett Motion*, *McClatchy*, *Aegean Marine Petroleum*, *Relativity Media*, *SAS AB* and *Voyager Digital*. He also co-authored the *Collier Business Workout Guide* (Mathew Bender 2007). Judge Wiles has appeared on panels organized by ABI, the Association of the Bar of the City of New York, the American College of Investment Council, the Federal Judicial Center and many other organizations to discuss current bankruptcy issues, and he is a judicial delegate to the Committee on Bankruptcy and Reorganization of the Association of the Bar of the City of New York. His publications and written CLE materials include "May Parties Consent to Bankruptcy Court Adjudication of '*Stern* Claims'" (September 2014) (presented at a continuing legal education session at the Association of the Bar of the City of New York); "Ponzi Schemes and Avoidance Actions: 3 Issues," *Law360* (March 7, 2011); "The Good Faith Defense to Fraudulent Transfer Claims" (December 2010) (presented at a continuing legal education session at the Association of the Bar of the City of New York); and "At the Crossroads: The Intersection of the Federal Securities Laws and the Bankruptcy Code," *The Business Lawyer* (November 2007). Judge Wiles received his A.B. from Georgetown University in 1975 and his J.D. from Yale Law School in 1978.