AMERICAN BANKRUPTCY INSTITUTE

2019 Annual Spring Meeting

CONCURRENT SESSION

Plan and Confirmation Issues: RSAs, Third-Party Releases, Valuation, Classification and Gifting

Sheryl L. Toby, Moderator
Dykema Gossett PLLC; Bloomfield Hills, Mich.

Hon. Michelle M. Harner
U.S. Bankruptcy Court (D. Md.); Baltimore

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2019

Bankruptcy Rapid Fire:
9 Confirmation Issues in 75 Minutes
Audience Decides the Correct Answer

Michelle M. Harner, United States Bankruptcy Court, District of Maryland
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Melissa M. Root, Jenner & Block LLP
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1. In re Millennium Lab Holdings II, LLC, et al.

242 F. Supp. 3d 322 (D. Del. 2017)

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Issue:

May a bankruptcy court constitutionally allow non-consensual third-party releases?

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Facts:

- Debtors filed voluntary Chapter 11 bankruptcy petitions with a prepackaged plan of reorganization
- As part of the lender group, Voya funded a large portion of the loan and subsequently objected to confirmation of the plan
- Voya did not object to the overall compromise of the plan, but rather to the inclusion of releases of claims that creditors, including Voya, might assert against non-debtor equity holders
- Voya argued that the Bankruptcy Court did not have subject matter jurisdiction to grant nonconsensual third-party releases and that third-party releases were impermissible

Holding:

Judge Stark held that the appeal from the Bankruptcy Court order confirming the plan had to be dismissed as equitably moot and even assuming that appeal from the Bankruptcy Court order did not have to be dismissed as equitably moot, Bankruptcy Court properly approved releases as not only fair, but necessary to Debtors' reorganization.

2a. In re Jevic Holding Corp., et al.
and
Czyzewski v. Jevic Holding Corp.

787 F.3d 173 (3d Cir. 2015)

137 S. Ct. 973 (2017)

Issue:

May a case arising under Chapter 11 ever be resolved in a "structural dismissal" that deviates from the Bankruptcy Code's priority scheme?

Facts:

- Jevic Transportation filed for Chapter 11 protection in Delaware
- A group of terminated drivers, previously employed by the Debtors, filed a class action adversary proceeding for federal and state WARN Act violations
- Representatives of the Debtors, the lenders and the WARN plaintiffs convened settlement negotiations, but the WARN plaintiffs objected to the settlement on the grounds that it distributed estate assets to junior creditors in violation of the Code's priority scheme
- The Bankruptcy Court overruled the objection, finding that the "dire circumstances" of the case warranted approval of the settlement notwithstanding its deviation from the priority scheme
- The Delaware District Court affirmed and the appeal then went to the Third Circuit

Holding:

- The Third Circuit affirmed the Bankruptcy and District Court rulings holding that the Bankruptcy Court had discretion to order the priority-skipping decision and, as a matter of first impression, "absolute priority" rule is not necessarily implicated outside the plan confirmation context when settlement is presented for court approval apart from a reorganization plan.
- Supreme Court Ruling: The Supreme Court reversed and remanded the lower courts' decision in *Jevic* by a 6-2 decision. The Supreme Court ultimately held that a bankruptcy court may not approve a structured dismissal of a Chapter 11 case that provides for distributions that do not follow the Bankruptcy Code's ordinary priority rules without the affected creditors' consent

2b. In re Nuverra Environmental Solutions, Inc., et al.

590 B.R. 75 (D. Del. 2018)

Issue:

May a "gift" of cash and stock from a secured creditor to holders of unsecured claims violate confirmation standards for approving a plan under Chapter 11?

Facts:

- The appeal arises from Debtors' plan of reorganization, pursuant to which secured creditors, who would not receive 100% recovery on their secured claims, made a gift to general unsecured creditors, who would otherwise receive no distribution under the Bankruptcy Code's priority scheme, in order to enable the Debtors to reorganize
- Even though unsecured creditors would receive no distribution absent the gift, a general unsecured creditor appealed the Confirmation Order based on the fact that the plan placed general unsecured claims of the same priority into separate classes and provided disparate treatment

Holding:

The District Court affirmed the Bankruptcy Court decision by first ruling that the appeal was equitably moot. The Court then went onto rule that the Debtors' proposed plan did not "unfairly discriminate" in favor of unsecured creditors holding claims and against creditors holding other claims, and the Debtors had a rational basis for placing unsecured creditors holding certain claims in a separate class from other general unsecureds.

3. In re Tribune Company, et al.

464 B.R. 126 (Bankr. D. Del. 2011)

Issue:

Does 1129(a)(10) require acceptance on a “per plan” or “per debtor” basis?

Facts:

Confirmation hearing was held on competing Chapter 11 plans proposed. One plan was proposed jointly by the debtors, unsecured creditors' committee, and certain senior lenders, while the other was proposed by noteholders.

Holding:

Judge Carey held that 1129(a)(10) is evaluated on a “per debtor” basis. Since the Tribune Company debtors had not been substantively consolidated and the plan did not provide for substantive consolidation, each “joint plan” was found to comprise a separate plan for each debtor and the confirmation requirements had to be satisfied for each debtor. Judge Carey noted that joint administration exist merely for the convenience of the court and parties but is not a substantive remedy. The convenience of joint administration and a joint plan do not override the rights of creditors in impaired classes of claims that reject a plan.

4. In re Arsenal Energy Holdings, LLC

C.A. No. 19-10226 (BLS), United States Bankruptcy Court for the District of Delaware, Shannon, J.

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Issue:

Can/should the Bankruptcy Court approve confirmation of a prepackaged chapter 11 plan of reorganization where (i) solicitation and notices of objection deadlines occurred pre-petition, (ii) all affected classes voted overwhelmingly to accept the plan, and (iii) the parties seek confirmation in a week (give or take a couple of days)?

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Facts:

Debtors contented that they complied with all provisions of the Bankruptcy Code, except that the trigger of the time periods occurred and was virtually completed pre-petition.

Holding:

- Such proceedings are procedurally proper, it just so happened that the filing occurred during that process - so compliant with Bankruptcy Rules.
- Solicitation complied with Bankruptcy Rules 2002, 3017 and 3018.
- Questions from Court regarding timing?

5. In re Indianapolis Downs, LLC, et al.

486 B.R. 286 (Bankr. D. Del. 2013)

Issue:

Are postpetition Restructuring Support Agreements permissible?

Facts:

Certain of the Debtor's equity holders attempted to thwart confirmation of a prenegotiated chapter 11 plan by arguing that a postpetition lockup agreement among the Debtors and a large group of secured creditors violated the plan solicitation requirements of the Bankruptcy Code and that the votes of the signatory creditors should therefore be disallowed, or "designated."

Holding:

- The Bankruptcy Court rejected the Equity Objectors' argument, adopting a narrow interpretation of "solicitation" in section 1125(b). The Bankruptcy Court held that the term "solicitation" in section 1125(b) must be interpreted narrowly to avoid interference with negotiations during a bankruptcy case
- The Court concluded that the votes of creditors who had signed a term sheet embodying key economic terms of a chapter 11 plan should not be designated because "the term 'solicitation' should be construed very narrowly, in deference to a clear legislative policy encouraging negotiations among creditors and stakeholders in Chapter 11 cases"
- Bankruptcy Court ruled that "solicitation" occurs only when a plan, disclosure statement and ballot are actually presented. Relying on this narrow interpretation of "solicitation," the Bankruptcy Court in *Indianapolis Downs* concluded that the RSA was not an improper solicitation because it required creditors to vote in favor of a plan only if and when a plan conforming to the terms of the RSA was proposed in accordance with section 1125(b)

6. In re Zenith Elecs. Corp.

241 B.R. 92 (Bankr. D. Del. 1999)

Issue:

Are “death traps” impermissible under the Bankruptcy Code as unfair or discriminatory treatment of creditors who may be similarly situated?

Facts:

- The plan provided that certain creditors (holders of bonds) would receive no recovery if they did not vote in favor of the plan, but would receive a pro-rata share of a certain notes if they did vote in favor of the plan

- Equity objected on the basis that under the valuation proposed by the debtors, such creditors would receive nothing under the plan and, as such, the proposed treatment was unfair as both a matter of value and because equity (also out of the money) would not receive similar treatment (although similarly situated)

Holding:

- The Bankruptcy Court overruled the objection, finding that that "[t]here is no prohibition in the Code against a Plan proponent offering different treatment to a class depending on whether it votes to accept or reject the Plan"

- The Court bolstered its ruling by noting that such treatment serves the addition benefit of potentially saving the plan proponent the "expense and uncertainty of a cramdown fight" furthering the Bankruptcy Code's overall policy of "fostering consensual plans of reorganization . . . ."

7. In re Claire's Stores, Inc., et al.

C.A. No. 18-10584 (MFW)

United States Bankruptcy Court for the District of Delaware, Walrath, J.

Issue:

May debtors close all but one jointly administered case where the cases have not been consolidated and have remaining claims processing administered through the open case, where a final decree is otherwise appropriate pursuant to Bankruptcy Rule 3022?

Facts:

- Debtors presented an uncontroverted record that they had, in fact, complied with B.R. 3022 for all of the cases proposed for final decree
- The UST objected on the basis that some general unsecured claims for such cases were still being reviewed, objected to and resolved, and , as such, a final decree could not be entered
- The UST also argued that this approach would be 'deemed consolidation'

Holding:

The Court applied the six non-exclusive factors set forth in the comments to B.R. 3022, found that all creditors except general unsecured creditors had received distributions and that the plan had been fully administered, and concluded that the it was "not disturbed by closing the operating entities and leaving only the parent debtor open for that purpose." In so ruling, the Court also noted that "the substantive rights of creditors and other parties are not being adversely affected by the closing..."

8. In re Concepts America, Inc.

2018 WL 2085615 (Bankr. N.D. Ill. May 3, 2018)

Issue:

May a bankruptcy court allow substantive consolidation of a debtor with entities that are not under the protection of the Bankruptcy Code?

Facts:

- Chapter 7 Trustee sought to substantively consolidate debtor with other non-debtor entities owned and operated by defendants
- The defendants owned 50% of stock in the debtor and operated various restaurants, engaging in a fraudulent scheme commingling money of each of the businesses with the debtor
- Chapter 7 Trustee sought to consolidate the debtor with non-debtor entities run by defendants because the affairs were so entangled that consolidation would benefit all creditors, the funds were commingled and inadequate financial records existed to sort out the alleged scheme between debtor and non-debtor entities

Holding:

- The 7th Circuit held that it would not allow substantive consolidation of a debtor with non-debtor entities
- There is a split of authority as to substantive consolidation with non-debtors and the 7th Circuit ruled that it would not apply substantive consolidation because it lacked support in the 7th Circuit and it could find no power to do so under the Bankruptcy Code
- The 7th Circuit provided that the Bankruptcy Code allows for a non-debtor to be forced into bankruptcy involuntarily, thus there was no need to extend substantive consolidation, a theory based in equity, to non-debtor parties
- The 7th Circuit noted that the Trustee had similar state law remedies available on this matter

Additional Considerations re: Substantive Consolidation

In re Woodbridge Group of Companies, LLC

592 B.R. 761 (Bankr. D. Del. 2018)

- May a secured creditor's lien be eliminated through substantive consolidation?

9. In re Samson Resources Corporate, et al.

590 B.R. 643 (Bankr. D. Del. 2018)

Issue:

Can confirmation orders include language that provides a broader discharge or release than what is contained in the Plan? Or can a confirmation order (and related findings at the confirmation hearing by the Judge) limit the release language contained in the Plan?

Facts:

- Plan Settlement Trust filed a complaint against Defendants. Confirmed plan contained broad releases, including (a) all affiliates and former affiliates of the Debtors, (b) all affiliates and former affiliates of the "non-debtor subsidiaries;" and (c) all current and former equity holders of affiliates and former affiliates of the Debtors. Defendants argue that they are indisputably described by this language and thus file a motion for summary judgement based on the plan release.
- Plan Settlement Trust argued that the confirmation order explicitly controls over the Plan and thus, the proper question for the Court is not necessarily what the Debtors and their creditors agreed to in their Plan, but rather what persons and entities Judge Sontchi intended to treat as "Released Parties" in his Confirmation Order and what "Causes of Action" he was permitting the Debtors to compromise and release.

Holding:

The Court boiled the trustee's position as follows "the Plan just can't mean what it says." The Court held that "a plan is effectively a contract between and debtor and its stakeholders … [and] its provisions control."