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Third-Party Releases: Is There a Fair Price to Pay?

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2024

Third-Party Releases

Is there a fair price to pay?

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We hold that nonconsensual third-party releases of **such direct claims** are statutorily permitted under 11 U.S.C. 9 §§ 105(a) and 1123(b)(6) of the Bankruptcy Code. We further conclude that this Court's **case law also allows for nonconsensual third-party claim releases in specific circumstances**, such as those presented in this appeal.

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Purdue Factors

1. Identity of Interests Between Debtors and Released Parties
2. Factual and Legal Overlap Between Claims Against Debtors and Settled Third-Party Claims
3. The Releases are Essential to the Reorganization
4. The Releases are Proper in Scope
5. **Substantial Contribution to the Reorganization**
6. Overwhelming Approval by Creditors
7. **Fair Payment of Enjoined Claims**

[O]ur primary focus is on the impact of the financial contribution. …It is not for this Court to determine whether a greater contribution from the Sacklers would be desirable, but rather our role is simply to decide **whether the bankruptcy court erred in finding the Sacklers' contribution substantial**. It did not. Five and a half billion dollars—purportedly the largest contribution in history for such releases—is a significant sum.

[T]he valuation of the claims—estimated at $40 trillion—far exceeds the total funds available, as well as the Sacklers' personal wealth…although in a vacuum the ultimate judgments…might well be higher than the Sacklers' contribution to the plan… Thus, **as it is not possible to require the full payment of all claims, we do prioritize fair allocation over the full payment of any one claim.**

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Alternative Measures of Contribution

- Share of Claim Liability/Damages
  - *Value of claims liability*
  - *Share of fault*
  - *Availability of defenses*
- Disgorgement of Benefits
  - *Dividends paid to third party*
  - *Other transfers*
- Value of Release
  - *Avoided costs of litigation absent release*
- Ability to Pay

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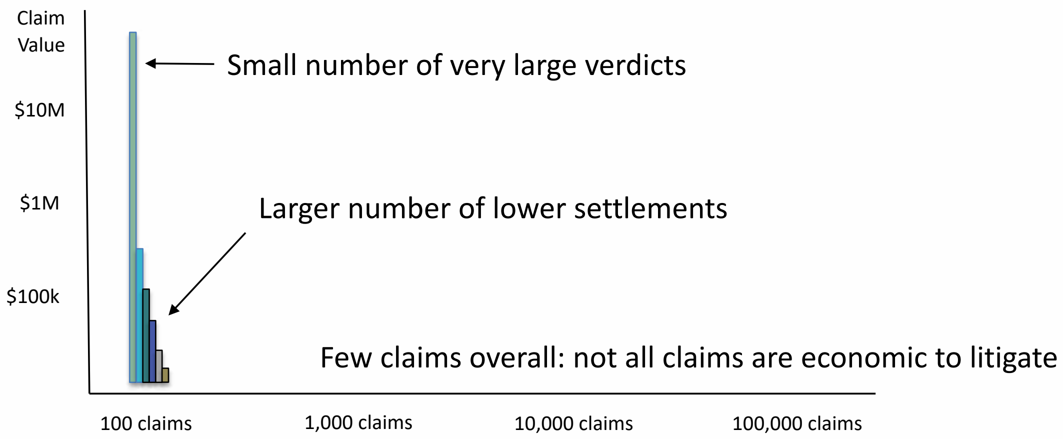
Historical Liability in the Tort System



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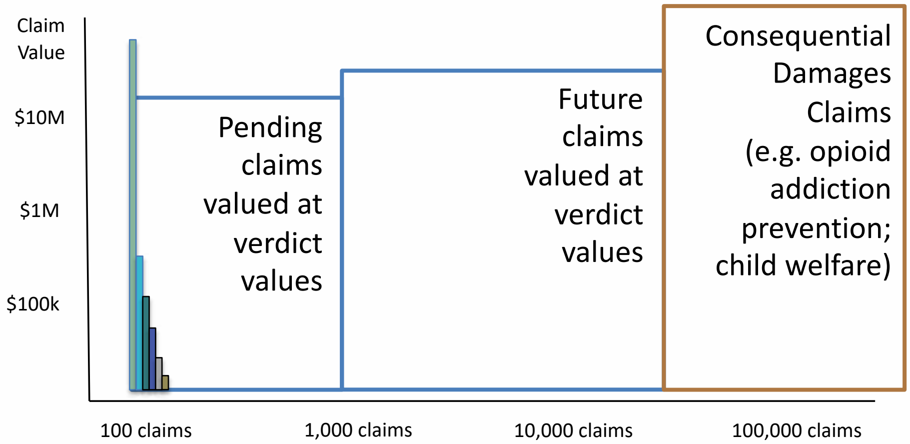
Aggregate Liability = Claim Value x # of Claims



Aggregate pending and future claims vastly exceed historical numbers

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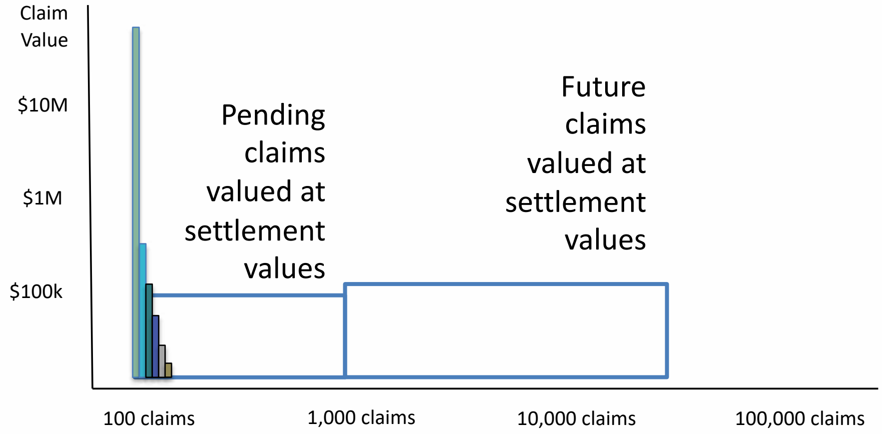
Valuations Based on Settlements Not Verdicts



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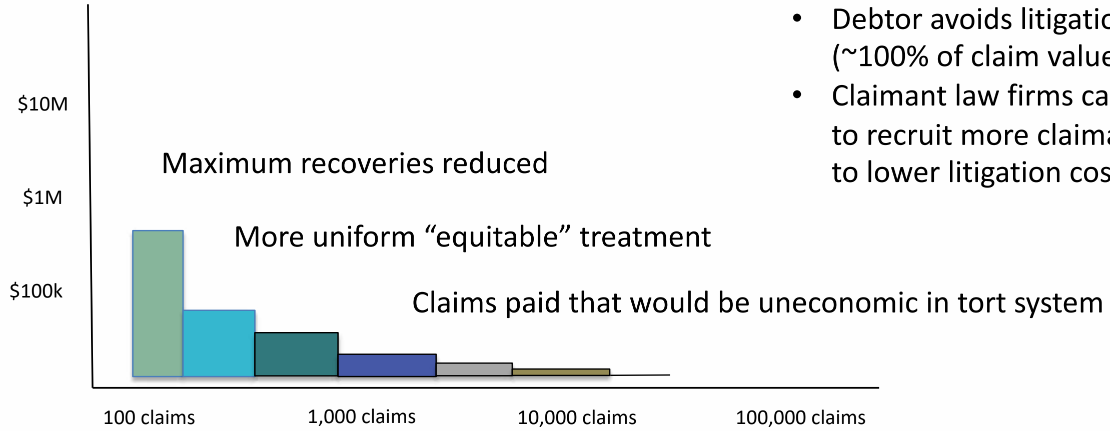
Claims Liability in Bankruptcy Settlement

- Debtor avoids litigation costs (~100% of claim value)
- Claimant law firms can afford to recruit more claimants due to lower litigation costs



Mass Tort Valuation Considerations

<u>Use of Valuation</u>

- Solvency /Avoidance Action § 547
- Claims estimation § 502(c)
- Reasonableness of settlement § 9019
- Funding adequacy

<u>Basis of Estimate</u>

- Most-likely amount (GAAP)
- Highest and best use (§ 363)
- Range of reasonableness/ business judgement (rule 9019)
- **Fair value (discounted expected value)**
- Tort system value vs. value in bankruptcy
- Unreasonable small capital
- "Legal liability" (Garlock)

<u>Factors to Consider</u>

- Verdicts
- Settlements ("market value")
- Trends in tort system
- Distortions in tort
- Defense costs
- Cost of capital/ return on capital
- Funding sources/ ability to pay

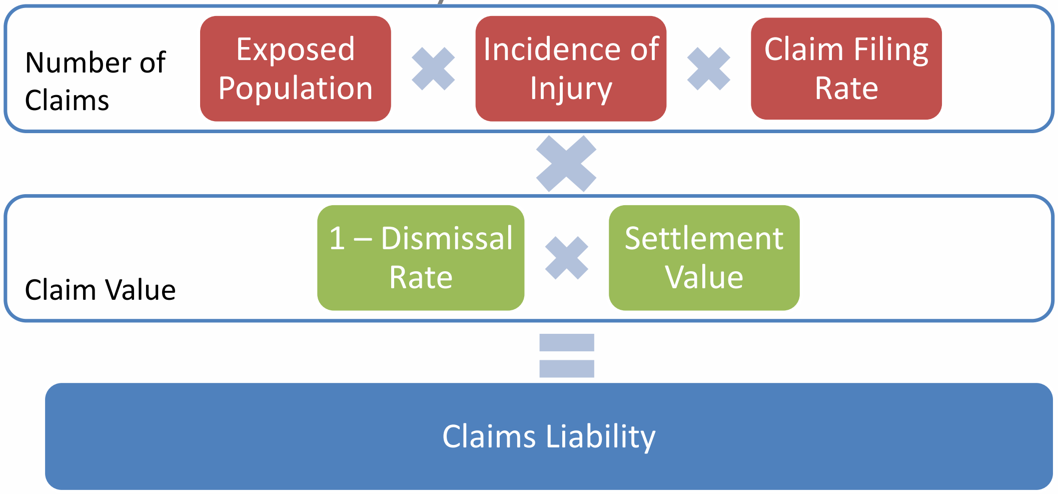
Fair Value: Discounted Expected Value

Expected Value = probability x average value

- Selected Estimation Precedents
  - *Eagle-Picher (1995)*
  - *Federal Mogul (2005); Owens Corning (2006)*
  - *Bondex (2013); Garlock (2014)*
- Avoidance Action Precedents
  - *Babcock & Wilcox (2002); Sealed Air (In re W.R. Grace) (2002)*
  - *Tronox (2013)*

See: Paul Hinton and Adrienna Huffman "The Mass Torts Gap in Contingent Liability Valuation Guidance," ABI Journal, forthcoming March 2024

Mass Tort Liability Valuation Framework



Direct vs. Derivative

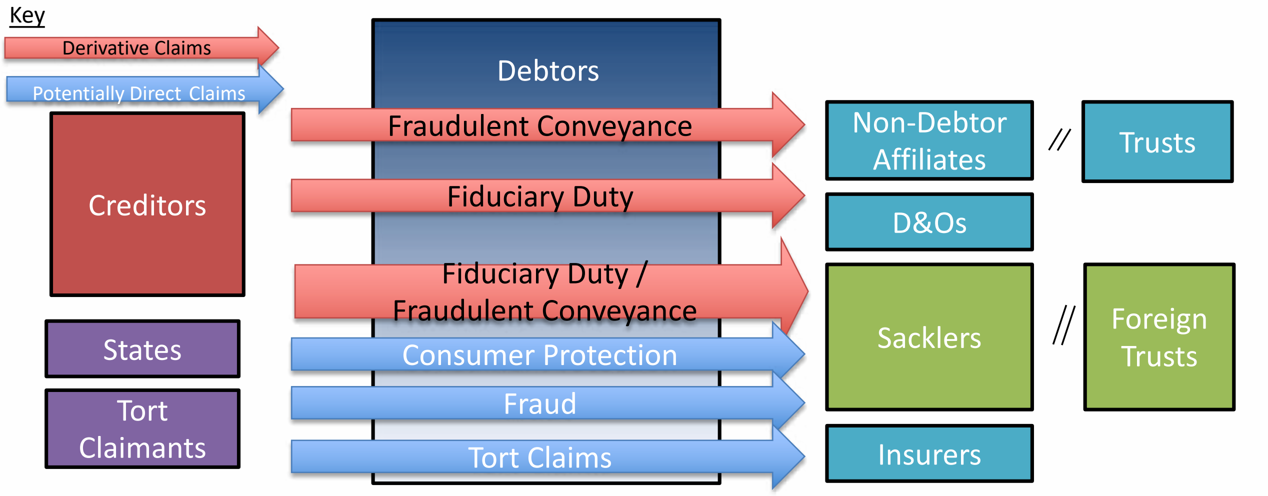
The released claims can be grouped into two categories: **direct claims and derivative claims**.

- **Direct claims** are causes of action brought to redress a **direct harm to a plaintiff caused by a non-debtor third party**.
- By contrast, **derivative claims** are ones that arise from **harm done to the estate and that seek relief against [the] third part[y]**.

The potential claims released against the Sacklers include, *inter alia*, fraudulent transfer, constructive fraudulent transfer, deceptive marketing, public nuisance, unfair competition, fraudulent misrepresentation, violation of state consumer protection acts, civil conspiracy, negligence, and unjust enrichment. Some of these claims are direct, and some are derivative. As conceded by the parties, **fraudulent transfer claims, for example, are typically derivative claims in that the real injury is to the Debtors' estate, and it is well-settled that a bankruptcy court may approve not only third-party releases which are consensual, but also third-party releases of derivative claims because those claims really belong to the estate**

[C]ertain consumer protection act claims at a minimum constitute direct claims in that the injury belongs directly to the claimant, and not to the Debtors. We need not define the exact claims which fall under the umbrella of direct claims but note that certain state law claims under consumer protection acts likely do.

Parties and Claims Potentially Affected by Third-Party Releases



Highland

We start with the scope of the non-debtor exculpation. In a Chapter 11 bankruptcy proceeding, "**discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt.**" 11 U.S.C. § 524(e)…. **[T]he exculpation here partly runs afoul of that statutory bar on non-debtor discharge by reaching beyond Highland Capital, the Committee, and the Independent Directors.** We must reverse and strike the few unlawful parts of the Plan's exculpation provision.

The simple fact of the matter is that there is a circuit split concerning the effect and reach of § 524(e). **Our court along with the Tenth Circuit hold § 524(e) categorically bars third-party exculpations absent express authority in another provision of the Bankruptcy Code.**

Appellants, however, submit the bankruptcy court improperly stretched *Pacific Lumber* to shield other non-debtors from breach-of-contract and negligence claims, in violation of § 524(e). Highland Capital counters that the exculpation provision is a commonplace Chapter 11 term, is appropriate given Dondero's litigious nature, does not implicate § 524(e), and merely provides a heightened standard of care.

To support that argument, Highland Capital highlights the distinction between a concededly unlawful release of all non-debtor liability and the Plan's limited exculpation of non-debtor post-petition liability…
[T]he Third and Ninth Circuits have adopted that distinction when applying § 524(e). Under those cases, narrow exculpations of post-petition liability for certain critical third-party non-debtors are lawful….Highland Capital reads *Pacific Lumber* as "…allowing a limited exculpation of post-petition liability"

Moreover, the Ninth Circuit expressly disavowed *Pacific Lumber*'s rationale—that an exculpation provision provides a "fresh start" to a non-debtor in violation of § 524(e)—because, in the Ninth Circuit's view, the post-petition exculpation "affects only claims arising from the bankruptcy proceedings themselves." We are not persuaded….

But we rejected the parsing between limited exculpations and full releases that Highland Capital now requests.

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What's Next?

- Expansion of 524(g)?
- Refinement of MDL?
  - Timing vs preservation of due process
  - Use of bellwethers
- Tort Settlements
  - Aearo model?
  - Prior mixed results: Fen-Phen; Vioxx; Round-up
- New Plan Structures?
  - Pseudo-voluntary releases
    - Opt-out provisions
    - Payments for release
  - Channeling injunctions

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Value & Cents

By Paul Hinton and Dr. Adrienna Huffman

Mass Torts Gap in Contingent-Liability Valuation Guidance

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In mass torts, litigation-liability[1] valuation often plays a significant role in the assessment of proposed plan funding, third-party contributions, indemnification and settlements.[2] This has been seen in recent years in several large mass tort multi-district litigation and bankruptcy cases, including those involving LTL Management, Purdue Pharma, the Boy Scouts of America and Aearo Technologies.

Neither the Bankruptcy Code nor accounting standards provide specific guidance on how mass tort claims should be valued. However, courts have adopted a framework of estimating mass tort litigation claims at their expected present value,[3] both in connection with estimation proceedings under § 502(c) of the Bankruptcy Code, and (2) in avoidance actions involving tests of insolvency under § 547. These precedents provide guidance that fills in the gap left by the Bankruptcy Code and accounting standards.[4]

Valuation of Contingent Liabilities

The Bankruptcy Code defines "insolvent" as a condition in which liabilities exceed an entity's assets,[5] but it is not prescriptive as to how an entity's nonfinancial liabilities are to be valued. Contingent liabilities, which for accounting purposes include mass tort claims, are included in the Code's definition of an entity's liabilities,[6] but again, the Code — including §§ 502(c) and 547 — is silent on how contingent liabilities are to be valued.

The U.S. Generally Accepted Accounting Principles (GAAP) codifies contingent liabilities, referred to as loss contingencies, Accounting Standards Codification (ASC) Topic 450-20, but these rules do not employ the fair-value standard as a measurement basis.[7] Contingent liabilities are measured using the "most likely amount"[8] if it is likely that the associated contingent event is probable[9] and the amount of the loss can be reasonably estimated.[10] "Probable" is defined as "likely to occur," but no threshold or measurement basis is specified.[11]

The most specific GAAP guidance in relation to valuing mass tort claims is found in the contingent-liability rules related to litigation, claims and assessments, and is limited to the assessment of the

1 The Third Circuit has defined a contingent claim as one that "the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event." *Frenville*, 744 F.2d at 336, n.7. A debt subject to default risk would not be a contingent liability, since a credit event is intrinsic to the lending relationship, not extrinsic.

2 *See, e.g.*, the bankruptcy of Johnson & Johnson's subsidiary LTL Management related to talc claims, Case No. 3:21-bk-30589 (Bankr. D.N.J.); Purdue Pharma LP bankruptcy related to opioid claims, Case No. 7:19-bk-23649 (Bankr. S.D.N.Y.); Boy Scouts of America bankruptcy related to sexual-abuse claims, Case No. 20-10343 (LSS) (Bankr. D. Del.); and Aearo Technologies bankruptcy related to claims of hearing loss claims, Case No. 1:22-bk-02890 (Bankr. S.D. Ind.).

3 This valuation method is typically implemented using discounted-cash-flow (DCF) models. A widely referenced exposition of the economic and finance theory of expected present value method is described in *Principles of Corporate Finance* by Richard Brealey, Stewart Myers, Franklin Allen and Alex Edmans (McGraw Hill).

4 The relevant literature spans disparate disciplines involved in claims estimation and valuation in mass torts. The bulk of the relevant literature is distributed across a number of areas of research: the estimation and demography of exposed populations; the estimation of hazard risks and injury rates, including epidemiology and studies in public health and occupational safety; the economics of claiming activity, including claimant recruitment and the propensity to sue; and the study of the tort system, including cost of compensation, which is encompassed within the field of law and economics.

5 11 U.S.C. § 101(32)(A) ("[A] financial condition such that the sum of such entity's debts is greater than all of such entity's property, at a fair valuation.").

6 The Bankruptcy Code's definition of "claim" is a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." *See* 11 U.S.C. § 101(5)(A).

7 "Fair value" is defined in ASC Topic 820 as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." This standard does not provide any guidance specific to mass torts.

8 According to ASC-450-20-30-1, "If some amount within a range of loss appears at the time to be a better estimate than any other amount within the range, that amount shall be accrued. When no amount within the range is a better estimate than any other amount, however, the minimum amount in the range shall be accrued."

9 Under GAAP, "the single most likely outcome within the range is used without consideration of the other possible outcomes." *See* "Accounting for Legal Claims: IFRS Compared to U.S. GAAP," KPMG (Feb. 28, 2019), *available at* kpmg.com/us/en/articles/2023/measuring-provisions.html (last visited on Jan. 2, 2024).

10 ASC 450-20-25-2.

11 "While there is diversity in practice ... the threshold for 'probable' would need to be at least 70 percent." *See* "Roadmap: Contingencies, Loss Recoveries and Guarantees," Deloitte (March 2023), p. 21.

reporting threshold.[12] It does not address the particular valuation issues related to mass tort claim liabilities.[13] Indeed, the bankruptcy courts have long recognized that GAAP rules do not provide applicable metrics for solvency determinations.[14]

Learning from Major Asbestos Bankruptcy Decisions

The use of bankruptcy to achieve the resolution of asbestos mass torts has resulted in significant cases in which expert issues relating to liability valuation were adjudicated. The expert testimony, cited authorities and courts' assessments of this testimony define a framework for estimating claims and show how the expected value approach can be used to value mass tort claims. The framework accepted by courts in these cases involves developing an exposed population,[15] as well as estimating expected claiming rates and related per-claim expected values.

The first step in the framework involves methods of modeling exposed populations that were developed by epidemiologists working in the field of industrial hygiene. Perhaps the most widely cited is one from a seminal 1982 paper by epidemiologist Dr. William Nicholson and his colleagues.[16] He forecasted future injuries from an existing exposed population using an epidemiological dose-response function. This work was relied on by liability valuation experts in the 1995 *Eagle-Picher Industries* bankruptcy estimation, and Dr. Nicholson was hired in that case to update his original study through the bar date.

In its decision on estimation, the court accepted the four experts' estimates that were each based on Dr. Nicholson's forecast approach.[17] In addition to using the Nicholson method to forecast future injuries, the court endorsed a discounted-expected-value approach and identified factors that it considered important to estimate the value of future claims, including using the history of claim filings against the debtor and past settlement values.

In the *Babcock & Wilcox* bankruptcy in 2002, other related methods were also evaluated and relied on. The debtor's expert, Dr. Frederick Dunbar, testified on various methodologies — described in his 1996 book, *Estimating Future Claims* — for determining future asbestos liabilities.[18] Another expert in the case, Dr. Thomas Florence, used an alternative approach for estimating the size of an exposed population from known claims data. This approach, known as the Walker method (after Harvard epidemiologist Alexander Walker, who developed it in a 1983 article), involves estimating "the effective number of asbestos-exposed workers required to produce the current national incidence of mesothelioma."[19] The court ruled that the contemporaneous forecasts developed by the company were reasonable based on Dr. Dunbar's expert assessment, even though these forecasts — unlike the Nicholson and Walker approaches — did not rely on epidemiology.

The question of how to estimate expected claiming rates and the corresponding expected value of claims was also adjudicated in both the 2006 *Owens Corning* and the 2014 *Garlock* bankruptcies. These courts deviated from the *Eagle-Picher* court's view that the volume of claim filings and the value of settlements close to the bankruptcy date determine the value of the liability. In these later decisions, the courts found that claim liabilities could, in certain circumstances, be artificially inflated if recent settlement values and filing rates were used to compute claims-liability estimates.

In *Owens Corning*, the court found that tort reforms indicated that expected values would be lower than historical claim values.[20] The court reasoned that historical trends in filings and settlement costs were not indicative of future claim liability as of the petition date, but rather that "adjustments should be made to historical values."[21]

Later, in *Garlock*, the court found that improper plaintiff-litigation strategies, including selective disclosure of other sources of claimant exposures to asbestos, had inflated historical tort settlement values. The court ruled that the company's past settlement history was so distorted as to "make [Garlock's] settlement history an unreliable predictor of its true liability." Instead, the court endorsed an estimate of "true liability" based on Garlock's share of liability relative to other defendants overall. The debtor's expert referred to this as the "legal liability" approach.

Guidance from Fraudulent-Transfer Cases

Court decisions in fraudulent-transfer cases also provide guidance on the valuation of mass tort liability in the context of solvency. The most recent cases described herein treat mass tort liabilities as certain rather than contingent liabilities for solvency purposes. These cases also have endorsed the same estimation framework and discounted expected value approach.

Mass Tort Liabilities Are Not Contingent

In 2002, the court in the *Sealed Air* case was asked to rule on the "legal standards applicable to determining the debtor's solvency" as a result of a transfer of asbestos-claim liabilities.[22] In contrast to treatment under the GAAP, the

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12 ASC 450-20-55-10.

13 *Id.*

14 *See, e.g., Babcock & Wilcox Co. v. Babcock & Wilcox Co.*, 274 B.R. 230, 259 (Bankr. E.D. La. 2002) ("Virtually all of the cases that discuss GAAP in the context of a solvency analysis recognize that the court is not bound by GAAP in making a solvency determination.").

15 Sources of data from which exposed populations can be developed include employment data, sales data, claims data or population census data. *See, e.g.*, Lucy P. Allen, Denise N. Martin, Simona Heumann, Paul Hinton & Faten Sabry, "Forecasting Product Liability by Understanding the Driving Forces," Global Legal Group, *The International Comparative Legal Guide to Product Liability 2006: A Practical Insight to Cross-Border Product Liability Work* (June 2006).

16 William J. Nicholson, George Perkel & Irving J. Selikoff, "Occupational Exposure to Asbestos: Population at Risk and Projected Mortality — 1980-2030," *Am. J. of Industrial Medicine* 3:2S9-311 (1982).

17 *In re Eagle-Picher Indus.*, 189 B.R. 681, 690 (Bankr. S.D. Ohio 1995).

18 Frederick C. Dunbar, Denise Neumann Martin & Phoebus J. Dhrymes, *Estimating Future Claims: Case Studies from Mass Tort and Product Liability* (Andrews Professional Books 1996).

19 Alexander M. Walker, *et al.*, "Projections of Asbestos-Related Disease 1980-2009," *J. of Occupational Medicine* 25(5) (May 1983). In *Babcock & Wilcox*, Dr. Florence used a version of this method developed by Prof. Julian Peto.

20 The *Owens Corning* bankruptcy estimation hearing involved four expert estimates of asbestos-claim liabilities, which differed from lowest to highest by more than a factor of five. *Owens Corning v. Credit Suisse First Boston*, 322 B.R. 719 (D. Del. 2005).

21 The features of historical tort system settlements that one judge identified as requiring adjustments included the following: (1) forum-shopping; (2) overpayment to unimpaired claims; (3) group lawsuits; and (4) punitive damages. These adjustments are discussed further in Frederick C. Dunbar, Paul J. Hinton & Faten Sabry, "Forecasting Asbestos Liability After Recent Bankruptcy Decisions: How Forecasts Must Adjust for Changes in the Tort System," NERA Working Paper (June 8, 2006).

22 "The [plaintiff] committees maintained that the debtor's potential mass tort liability for future asbestos claims was known at the time of the transfer [to have been transferred] for less than fair value, and the debtor was thus insolvent at the time of the transfer, rendering the transfer fraudulent.... [T]he parties applied for a ruling *in limine* to determine the legal standards applicable to determining the debtor's solvency at the time of the transfer." *Official Comm. of Asbestos Pers. Injury Claimants v. Sealed Air Corp. (In re W.R. Grace & Co.)*, Case Nos. 01-1139 through 01-1200, Adv. No. 02-2210, Adv. No. 02-2211 (Bankr. D. Del. 2002).

court ruled that the future mass tort claim liabilities are not contingent liabilities[23] for the purposes of solvency analysis because mass tort liabilities arising from past exposures do not depend on a future extrinsic event.[24] Instead, the court found that unasserted future claims arising from pre-existing asbestos exposures impose liabilities that are certain; only their magnitude is uncertain.[25]

From an economic valuation perspective, the injury incidence and propensity to claim together generate the average probability of occurrence of individual future claims from the exposed population. The certainty equivalent value of the claims liabilities in the aggregate equals the expected value of individual claims across the entire population. In this way, the expected value calculations implicit in the standard-estimation framework incorporate the appropriate likelihood that individual claims will be filed, whether the unasserted claims are legally considered contingent or not.

Estimates Using the Expected-Value Approach

In the more recent *Tronox* fraudulent-transfer decision from 2013, the court endorsed the *Sealed Air* view that unasserted future mass tort claims are not contingent.[26] However, it also endorsed the plaintiff's expert's expected-value analysis based on the likelihood that future lawsuits would arise. Thus, the *Tronox* court agreed with the *Sealed Air* assessment that the liability associated with the future as-yet-unasserted claims is not contingent, and also endorsed the discounted expected-value approach.

Conclusion

The Bankruptcy Code and GAAP do not provide specific guidelines in relation to the contingent liability valuation of mass torts. Fortunately, the specialized literature on estimating future claims — along with the expert analyses in prior cases that rely on these authorities and associated court decisions — provide valuation guidance. Such guidance is critical to determining the most appropriate methodology in each case, how to use past empirical evidence to calibrate forecasts, and how to account for changing conditions or distortions in the tort system that affect the value of mass tort liabilities. abi

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23 This view was not shared in the earlier *Babcock & Wilcox* case, since the court in *Babcock & Wilcox* treated the asbestos claims as contingent liabilities. The *Sealed Air* court concluded that "it is difficult to satisfactorily explain why the *Babcock* court found that the post-transfer claims were contingent in the first place."

24 A contingent claim as defined as one in "which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event." *Frenville*, 744 F.2d.

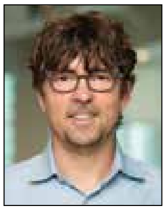
25 *In re Sealed Air.*

26 *In re Tronox Inc. v. Kerr McGee Corp., et al.*, Case No. 09-10156 (ALG) (2013).

Value & Cents

By Paul Hinton, David McKnight and Pietro Grandi

The Verdict Valuation Paradox: Implications for Mass Torts



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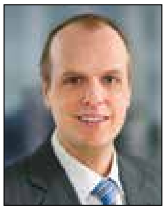

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Litigators routinely value individual cases in settlement negotiations based on the probability of succeeding at trial, the likely size of a verdict and the amount of avoided legal costs. Paradoxically, using past verdicts to value populations of mass tort claims can lead to erroneous valuations. Naively using verdicts in prior cases as benchmarks in mass tort cases fails to account for selection bias, which can grossly distort claim values. Research in law and economics into the selection of cases for trial provides a framework for understanding how choices that litigants make to settle or litigate affect observed verdict outcomes. This article identifies some important implications for the estimation of aggregate claim liabilities in mass tort cases.

Selection Effects in Tort Claims Valuation

The discounted-cash-flow valuation method can be used to value tort claims. The relevant cash flows result from expected future verdict awards or, alternatively, from settlements negotiated before a verdict is rendered, accounting for any costs incurred to litigate the claims. Economically rational plaintiffs will only accept settlement offers that exceed the expected value of a litigated outcome (discounted to account for expected timing and risk), less any costs to prosecute the case. Similarly, defendants will only accept settlements that are less than their expected value of a verdict, plus any associated defense costs. When these thresholds overlap, the parties may be able to negotiate a settlement within the overlapping range of values that are agreeable to both plaintiffs and defendants. By this logic, settlement values are a function of the risk-adjusted, discounted present value of awards expected through litigation. This explains why verdict values tend to be larger than settlements for similar cases. Relative to settlement, litigating to a verdict is risky, includes the possibility of no award and delays any recovery.

The problem with using observed verdicts as benchmarks for tort claim values is that they are not expected values and might not be representative. Expected verdict values must be adjusted for the likelihood of prevailing through trial, but even adjusted verdict values might not be representative because they are not observed for all claimants — only for those that choose not to settle.

The higher typical value of verdicts over settlements leads some to falsely believe that these different levels of compensation derive from weaker and stronger claims, respectively. This belief is unfounded. Whereas settlements provide a measure of expected values, verdict awards do not measure the compensation that claimants can expect in the tort system. Expected verdict values are a fraction of average realized verdict awards because they reflect the probability of prevailing through trial.

Economic analyses of decisions to settle reveal that claims that are actually litigated to verdict are not representative of all claims. Contrary to the naive view, they are not higher on average because they are necessarily the strongest, most highly valued claims. The claims that are litigated and result in verdicts are those in which the parties cannot agree on the strength of the claims in terms of the likelihood of prevailing and the expected amount of potential award. As litigation progresses, the parties learn more about the strength of the claims, increasing the likelihood of settlement, through which they may resolve uncertainty and avoid litigation costs. Research in law and economics into litigation outcomes predicts that plaintiffs' likelihood of winning a verdict at trial will trend 50/50, although only a smaller percentage of all cases reach trial at all.[1] Empirical evidence generally bears out this prediction.[2]

This theory helps explain litigation outcomes and has profound implications for the valuation of filed claims. First, observed-verdict values in similar cases must be adjusted for the likelihood of reaching trial and prevailing. Second, such expected verdict amounts might not be presumed to be representative benchmarks for valuation for all claims. The choices that parties make to settle rather than to litigate results in a selection effect that could make verdicts unrepresentative benchmarks.

Careful analysis of claims history can reveal other potentially important selection effects in addition to those associated with past settlement decisions. For example, claims that are filed and litigated but have yet to reach trial (*i.e.*, pending cases)

1 From 1990-2014, the percentage of cases reaching trial in U.S. district courts ranged between 1.1 and 4.3 percent. Donald Wittman, "Dispute Resolution, Bargaining, and the Selection of Cases for Trial: A Study of the Generation of Biased and Unbiased Data," *J. of Legal Studies* (1988), 17(2), pp. 313-52.

2 George Priest & Benjamin Klein, "The Selection of Disputes for Litigation," *J. of Legal Studies* (1984), 13(1), pp.1-55.

may differ from cases that choose settlement, and from cases litigated to verdict. In mass tort cases in particular, the expectation that claims will be resolved in a global settlement or in a bankruptcy changes the incentives to file, as well as the commercial incentives for attorneys to recruit claims. As a consequence, claims filed in anticipation of mass resolution outside of the tort system may differ materially from claims that were filed and resolved previously. Each of these selection effects have potentially important implications for claims valuation in mass torts.

Empirical Support for Selection Effects in Litigation

In their seminal 1984 article, George Priest and Benjamin Klein showed that the small number of cases that reach verdict are neither random nor representative, but rather are a selected sample of all disputes.[3] They showed that this source of selection bias lies in the pre-trial negotiations between plaintiffs and defendants.[4] Under rational expectations, setting aside the peculiarities of mass torts, the parties will agree on a settlement unless the difference between their estimated probability of prevailing at trial or expected verdict amount is sufficiently large, and the avoided litigation costs are sufficiently small.[5] For example, if parties have a large disagreement about the probable outcome of a trial, the case is more likely to be litigated.

Conversely, disputes where the parties' disagreement about the outcome is small — whether in favor of the plaintiff or defendant — are more likely to settle in order to avoid litigation costs.[6] This selection effect is exacerbated by the high cost of litigation. Rational actors will only litigate cases to verdict if the expected verdict award, less the associated litigation costs, is sufficiently higher than any settlement, which weeds out the lowest-value cases. The economics are reinforced by plaintiff attorneys who act as gatekeepers and help decide the cases that go to trial. Because plaintiff attorneys are paid on a contingency-fee basis (a percentage of the settlement or verdict amounts), attorneys will only try cases with potential awards that exceed their litigation costs.[7] Similarly, defendants may settle weaker cases for nuisance values to avoid litigation costs.

Therefore, litigated disputes will not constitute a random sampling of the underlying population of claims, but will skew toward those where there is a larger disagreement over the merit of the claims[8] and those that have larger potential awards relative to litigation costs.[9] Because of these sources of selection bias, it is difficult to infer claim values based on verdicts alone.[10]

3 Priest & Klein, pp. 1-55. J.P. Gould, "The Economics of Legal Conflicts," *J. of Legal Studies* (1973), 2(2), pp. 279-300. Robert D. Cooter & Daniel L. Rubinfeld, "Economic Analysis of Legal Disputes and Their Resolution," *J. of Econ. Literature* (1989), 27(3), pp. 1067-97.

4 Priest & Klein, *supra* n.3, pp. 1-55.

5 Specifically, larger than the difference between litigation and settlement costs, scaled by the size of the expected judgment should a plaintiff verdict be rendered. Priest & Klein, *supra* n.3, p. 13.

6 As a corollary of this result, if the vast majority of litigated disputes are close cases, the probability of a plaintiff victory at trial will approach 50 percent. Priest & Klein, *supra* n.3.

7 Henry S. Farber & Michelle J. White, "Medical Malpractice: An Empirical Examination of the Litigation Process," 22 *RAND J. of Econ.* 2 (1991).

8 Priest & Klein, *supra* n.3.

9 Wittman, *supra* n.1, pp. 313-52; Donald Wittman, "Is the Selection of Cases for Trial Biased?," *J. of Legal Studies* (1985), 14(1), pp. 185-214.

10 Joel Waldfogel, "The Selection Hypothesis and the Relationship Between Trial and Plaintiff Victory," *J. of Political Econ.* (1995), 103(2), pp. 229-60.

Empirical research provides evidence of the presence of selection bias in verdicts. For example, using data on plaintiff verdicts in contested civil actions litigated to trial between 1959-79 in the Chicago metropolitan area, Priest and Klein showed that the trial outcomes are suggestive of selectivity; Priest provides similar evidence in successive studies.[11] Subsequent research provides support for the selection hypothesis more generally. For example, Peter Siegelman and John J. Donohue III documented in 1995 that plaintiff win rates in employment-discrimination disputes vary with the business cycle and are lower in recessions, when parties with weaker cases would be more likely to sue.[12] In 1995, Joel Waldfogel used a natural experiment provided by a random assignment of cases to judges to compare trial probabilities and plaintiff win rates across judges, and found evidence supporting selection bias.[13] In 1998, he provided evidence that the relationship between tried cases and win rates generated by the litigation process is consistent with Priest's and Klein's 1984 theoretical framework, and is not consistent with that of alternative models of litigation.[14]

From the time of its original publication until the present day, Priest's and Klein's theory about the selection of cases for litigation remains an important benchmark for both theoretical and applied work in law and economics. The key implication that litigated cases differ systematically from settled cases has proved enduring and withstood the scrutiny of empirical tests. Priest's and Klein's piece from nearly four decades ago "has proven to be one of the most influential articles in legal scholarship" and one of the most influential law articles of all time.[15]

Implications for Mass Torts

The presence of selection bias in verdicts has direct implications for the way that parties estimate the value of claims in mass tort bankruptcies. In this setting, it is often necessary to estimate the value of all pending and future claims for the purposes of confirming a bankruptcy plan or reaching a global resolution. The question of which resolutions to use as benchmarks to value claims in a mass tort case can be a contentious issue for the parties' experts.

In cases without an established settlement history, some experts may look to verdicts to establish the value of claims. In these cases, it is essential to adjust average verdicts for the probability of prevailing at trial. It is also important to consider the inherent selection bias in verdicts. Even an unbiased procedure to estimate average verdict val-

11 George L. Priest, "Reexamining the Selection Hypothesis: Learning from Wittman's Mistakes," *J. of Legal Studies* (1985), 14(1), pp. 215-243; George L. Priest, "Measuring Legal Change," *J. of Law, Econs. & Org.* (1987), 3(2), pp. 193-225.

12 Peter Siegelman & John J. Donohue III, "The Selection of Employment Discrimination Disputes for Litigation: Using Business Cycle Effects to Rest the Priest-Klein Hypothesis," *J. of Legal Studies* (1995), 24(2), pp. 427-62.

13 Waldfogel, *supra* n.10, pp. 229-60.

14 Joel Waldfogel, "Reconciling Asymmetric Information and Divergent Expectations Theories of Litigation," *J. of Law and Econs.* (1998), 41(2), pp. 451-76.

15 Daniel Klerman, "The Selection of 13th-Century Disputes for Litigation," *J. of Empirical Legal Studies* (2012), 9(2), pp. 320-46. Fred R. Shapiro ranks Priest and Klein the 99th of all law articles (*see* "The Most-Cited Law Review Articles Revisited," 71 *Chi.-Kent L. Rev.* 751, 771 (1996)). Similarly, James E. Krier and Stewart J. Schwab rank Priest and Klein the 81st of all law articles (*see* "The Cathedral at Twenty-Five: Citations and Impressions," 106 *Yale L. J.* 2121, 2145 (1997)). William M. Landes and Richard A. Posner rank Priest and Klein the 28th of all articles in "predicted 'lifetime' citations" (*see* "Heavily Cited Articles in Law," 71 *Chi-Kent L. Rev.* 825, 838 (1996)).

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ues cannot be presumed to be representative of the claims population as a whole. If verdict outcomes are affected by selection bias, a reliable estimate of expected verdict values will also be biased.

There are also issues that arise in mass torts that can lead to additional modes of selection bias. For example, mass tort plaintiffs' attorneys have an incentive to focus early litigation efforts on cases with the highest expected damages. As a result, initial trial outcomes might not provide a reliable guide to estimate the value of the population of outstanding claims. Conversely, defendants may seek to settle weak claims at nuisance values to avoid litigation costs and set a low benchmark for anticipated future settlements. Similar competing problems of bias can arise through the selection of bellwether cases. In considering initial trial outcomes as benchmarks, it is important to consider these selection effects and ensure that the historically resolved claims are similar in severity and strength to the claims in the population being valued.

Another important source of selection bias in mass tort bankruptcies is the difference in the cost of litigating claims in the tort system as opposed to a bankruptcy proceeding. As previously discussed, plaintiffs will only bring cases in the tort system if the expected recovery is sufficiently higher than the cost of litigation. However, the cost of litigating an individual claim in the tort system can be very different from the cost of litigating that claim in a bankruptcy proceeding, which can result in claims being filed in a bankruptcy that would not be economically viable in the tort system.

For example, in the *Boy Scouts of America* bankruptcy, there were 2,000 sexual abuse cases filed in the tort system, but once a bankruptcy proceeding was established, more than 80,000 claims had been filed. In these cases, there is strong reason to suspect that the claims filed prior to the bankruptcy may materially differ from the bankruptcy claims. Historical claim resolutions would then provide an unreliable basis for estimating the value of the full population of claims.

Conclusion

Mass tort cases are ones in which claims valuation is commonly needed, and where experts may look to historical resolutions as a benchmark for claim values. Unfortunately, historically resolved claims, and verdicts in particular, might not be representative of the universe of pending and future mass tort claims. Careful claims analysis is needed to ensure that appropriate benchmarks are chosen, and that verdict values are properly adjusted to avoid mis-valuing claims. abi

22-110-bk (L)
In re: Purdue Pharma L.P.

In the
United States Court of Appeals
For the Second Circuit

AUGUST TERM 2021

ARGUED: APRIL 29, 2022
DECIDED: MAY 30, 2023

NOS. 22-110-bk (L), 22-113-bk, 22-115-bk, 22-116-bk, 22-117-bk, 22-119-bk, 22-121-bk, 22-299-bk, 22-203-bk

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In Re: Purdue Pharma L.P., Purdue Pharma Inc, Purdue Transdermal Technologies L.P., Purdue Pharma Manufacturing L.P., Purdue Pharmaceuticals L.P., Imbrium Therapeutics L.P., Adlon Therapeutics L.P., Greenfield BioVentures L.P., Seven Seas Hill Corp., Ophir Green Corp., Purdue Pharma of Puerto Rico, Avrio Health L.P., Purdue Pharmaceutical Products L.P., Purdue Neuroscience Company, Nayatt Cove Lifescience Inc., Button Land L.P., Rhodes Associates L.P., Paul Land Inc., Quidnick Land L.P., Rhodes Pharmaceuticals L.P., Rhodes Technologies, UDF LP, SVC Pharma LP, SVC Pharma Inc.,

Debtors.

****

PURDUE PHARMA, L. P., PURDUE PHARMA INC, PURDUE TRANSDERMAL TECHNOLOGIES L.P., PURDUE PHARMA MANUFACTURING L.P., PURDUE PHARMACEUTICALS L.P., IMBRIUM THERAPEUTICS L.P., ADLON THERAPEUTICS L.P., GREENFIELD BIOVENTURES L.P., SEVEN SEAS HILL CORP., OPHIR GREEN CORP., PURDUE PHARMA OF PUERTO RICO, AVRIO HEALTH L.P., PURDUE PHARMACEUTICAL PRODUCTS L.P., PURDUE NEUROSCIENCE COMPANY, NAYATT COVE LIFESCIENCE

INC., BUTTON LAND L.P., RHODES ASSOCIATES L.P., PAUL LAND INC., QUIDNICK LAND L.P., RHODES PHARMACEUTICALS L.P., RHODES TECHNOLOGIES, UDF LP, SVC PHARMA LP, SVC PHARMA INC.,

Debtors-Appellants-Cross-Appellees,

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF PURDUE PHARMA L.P., ET AL., AD HOC COMMITTEE OF GOVERNMENTAL AND OTHER CONTINGENT LITIGATION CLAIMANTS, THE RAYMOND SACKLER FAMILY, AD HOC GROUP OF INDIVIDUAL VICTIMS OF PURDUE PHARMA, L.P., MULTI-STATE GOVERNMENTAL ENTITIES GROUP, MORTIMER-SIDE INITIAL COVERED SACKLER PERSONS,

Appellants-Cross-Appellees,

— v. —

THE CITY OF GRANDE PRAIRIE, AS REPRESENTATIVE PLAINTIFF FOR A CLASS CONSISTING OF ALL CANADIAN MUNICIPALITIES, THE CITIES OF BRANTFORD, GRAND PRAIRIE, LETHBRIDGE, AND WETASKIWIN, THE PETER BALLANTYNE CREE NATION, ON BEHALF OF ALL CANADIAN FIRST NATIONS AND METIS PEOPLE, THE PETER BALLANTYNE CREE NATION ON BEHALF ITSELF, AND THE LAC LA RONGE INDIAN BAND,

Appellees-Cross Appellants,

THE STATE OF WASHINGTON, STATE OF MARYLAND, DISTRICT OF COLUMBIA, U.S. TRUSTEE WILLIAM K. HARRINGTON, STATE OF CONNECTICUT, RONALD BASS, STATE OF CALIFORNIA, PEOPLE OF THE STATE OF CALIFORNIA, BY AND THROUGH ATTORNEY GENERAL ROB BONTA, STATE OF OREGON, STATE OF DELAWARE, BY AND THROUGH ATTORNEY GENERAL JENNINGS, STATE OF RHODE ISLAND, STATE OF VERMONT, ELLEN ISAACS, ON BEHALF OF PATRICK RYAN WROBLEWSKI, MARIA ECKE, ANDREW ECKE, RICHARD ECKE,

Appellees.

Before: NEWMAN, WESLEY, and LEE, *Circuit Judges*.

Appellants appeal from an order of the United States District Court for the Southern District of New York (Colleen McMahon, *J.*) reversing an order of the United States Bankruptcy Court for the Southern District of New York (Robert D. Drain, *Bankr. J.*) confirming a Chapter 11 plan that included nonconsensual third-party releases of direct claims against non-debtors. We hold that nonconsensual third-party releases of such direct claims are statutorily permitted under 11 U.S.C. §§ 105(a) and 1123(b)(6) of the Bankruptcy Code. We further conclude that this Court's case law also allows for nonconsensual third-party claim releases in specific circumstances, such as those presented in this appeal. Accordingly, we **REVERSE** the district court's order holding that the Bankruptcy Code does not permit nonconsensual third-party releases against non-debtors, **AFFIRM** the bankruptcy court's approval of the Plan, and **REMAND** the case to the district court for such further proceedings as may be required, consistent with this opinion. We also **AFFIRM** the district court's denial of the Canadian Creditors' cross-appeal.

Judge Wesley concurs in the judgment in a separate opinion.

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EUNICE C. LEE, *Circuit Judge*:

Bankruptcy is inherently a creature of competing interests, compromises, and less-than-perfect outcomes. Because of these defining characteristics, total satisfaction of all that is owed—whether in money or in justice—rarely occurs. When a bankruptcy is the result of mass tort litigation against the debtor, the complexities are magnified because the debts owed are wide-ranging and the harm caused goes beyond the financial. That is the circumstance here.

The Debtor, Purdue Pharma L.P. ("Purdue"), was owned and operated by the Sackler family[1] for decades. In the 1990s, Purdue introduced to market—and

[1] The district court explained that the "Sackler Family," as used in the court's opinion, "means the Mortimer D. Sackler Family (also known as 'Side A' of the Sackler family) and the Raymond R. Sackler Family (also known as 'Side B' of the Sackler family.)." *In re Purdue Pharma, L.P.*, 635 B.R. 26, 35 n.2 (S.D.N.Y. 2021). The Mortimer D. Sackler family

promoted as non-addictive—OxyContin, a controlled-release semisynthethic opioid analgesic. In the years following, OxyContin has been blamed for significantly contributing to one of the largest public health crises in this nation's history: the opioid epidemic.

The fallout from this crisis led to a veritable deluge of litigation against both Purdue and individual members of the Sackler family. Claimants, spread across the United States and Canada, included many sufferers of opioid addiction and the families of those lost to opioid overdoses. To settle the mass of civil claims, the parties, including Purdue and the Sacklers, agreed that in exchange for Purdue filing for bankruptcy, the Sacklers would personally contribute billions of dollars to the bankruptcy if all civil claims against them were released.[2]

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explains that the "Mortimer-side Initial Covered Sackler Persons include Theresa Sackler, Ilene Sackler Lefcourt, Kathe Sackler, and Mortimer D.A. Sackler, as well as trusts of which they are beneficiaries and the trustees of those trusts, and Beacon Company." Br. for Appellant-Cross-Appellee Mortimer-Side Initial Covered Sackler Persons at 1 n.1. The Raymond R. Sackler family explains that the "Raymond Sackler family is comprised of natural persons who are descendants of Raymond R. Sackler and current and former spouses of their descendants." Br. for Appellant-Cross-Appellee the Raymond Sackler Family at 1 n.1.

[2] The district court explained that the Sacklers' contribution would go "to a fund that would be used to resolve both public and private civil claims as well as both civil and criminal settlements with the federal government." *In re Purdue Pharma, L.P.*, 635 B.R. at 70.

In accordance with that plan, Purdue and its related entities (together, the "Debtors" or "Purdue") filed for bankruptcy; the Sacklers did not. Following an intensive months-long and multi-phase mediation involving various interested parties and potential creditors of Purdue, the bankruptcy court approved the proposed bankruptcy plan. In doing so, the court limited the release of claims against the Sacklers to *only* claims that directly affected the Debtors' estate and for which Purdue's conduct was a legal cause, or a legally relevant factor, of any released cause of action against the Sacklers. In exchange, the Sacklers agreed to contribute a total $5.5-6.0 billion to the bankruptcy. On subsequent appeal, however, the district court for the Southern District of New York reversed the bankruptcy court and vacated the court's confirmation order, ruling that the Bankruptcy Code did not permit such releases.

This appeal followed. During the pendency of the appeal, the various parties to the mediation engaged in further negotiations, resulting in additional changes to the proposed bankruptcy plan. These changes resulted in several more parties dropping their opposition and supporting the further-revised bankruptcy plan. The Appellants, who are challenging the district court's rejection of the proposed plan, include the Debtors, various creditor and claimant groups, and certain Sackler family members. The Appellees are those parties opposed to the proposed plan, although, as noted, their number has dropped since the initial filing of this appeal. These remaining Appellees consist of the U.S. Trustee, several Canadian municipalities and indigenous nations, and several individual *pro se* plaintiffs.

Aside from their legal arguments, the parties contend that various policy considerations should inform whether a bankruptcy plan containing nonconsensual third-party releases of direct claims may be approved. They also raise questions about fairness and accountability, particularly as it relates to the Sacklers, in releasing parties from liability for actions that cause great societal harm. They debate the very nature of bankruptcy, including the role it is intended to serve and the parties it is intended to benefit.

But, our role in this appeal does not require us to answer all of these serious and difficult questions. Instead, we are tasked only with resolving two key questions: *First*, does the Bankruptcy Code permit nonconsensual third-party releases of direct claims against non-debtors, and, *Second*, if so, were such releases proper here in light of all equitable considerations and the facts of this case. We answer both in the affirmative.

We conclude that two sections of the Bankruptcy Code, 11 U.S.C. §§ 105(a), 1123(b)(6), jointly provide the statutory basis for the bankruptcy court's authority to approve a plan that includes nonconsensual releases of third-party claims against non-debtors. In addition, this Court has recognized that in specific circumstances—such as those presented by this appeal—bankruptcy courts are permitted to approve of restructuring plans that include such releases. We accordingly hold that the bankruptcy court's approval of the releases here is permissible both statutorily and under this Court's case law. We further hold that the bankruptcy court's inclusion of the releases is equitable and appropriate under the specific factual circumstances of this case, and we articulate several factors to guide the analysis as to when to allow similar releases in reorganization plans.

Accordingly, we **REVERSE** the district court's order holding that the Bankruptcy Code does not permit nonconsensual releases of third-party direct claims against non-debtors, **AFFIRM** the bankruptcy court's approval of the reorganization plan, and **REMAND** the case to the district court for such further proceedings as may be required, consistent with this opinion. We also **AFFIRM** the district court's denial of the Canadian Creditors' cross-appeal.

BACKGROUND

I. Factual Background

The following discussion is limited to those underlying facts that are necessary for a determination of the issues on appeal.[3]

A. Purdue and OxyContin

The Sackler brothers, including Mortimer and Raymond Sackler,[4] purchased Purdue, a privately held pharmaceutical company, in the 1950s. Members of the Sackler family held various director and officer positions throughout the company and, from approximately 1993 to 2018, Purdue's Board of Directors contained at least six members of the Sackler family. Beyond the board, Sackler family members held other positions of influence in the company. For example, Mortimer and Raymond Sackler served as co-chief executive officers

[3] The decisions of the bankruptcy and district courts provide a more detailed recitation of the background facts. *See In re Purdue Pharma L.P.*, 633 B.R. 53 (Bankr. S.D.N.Y. 2021) ("*Purdue I*"); *In re Purdue Pharma, L.P.*, 635 B.R. 26 (S.D.N.Y. 2021) ("*Purdue II*").

[4] Arthur Sackler sold any interest in Purdue before the development of OxyContin. He and his heirs are therefore not involved in this action.

until their deaths, Richard Sackler served as a president, and Mortimer D.A., Ilene, and Kathe Sackler all served as officers.

In 1995, Purdue developed, and the Food and Drug Administration ("FDA") approved, OxyContin, a controlled-release semisynthetic opioid analgesic. At that time, and for years following, Purdue advertised that the time-release formulation prevented OxyContin from posing a threat of abuse or addiction. OxyContin's FDA label reflected a purportedly low risk of addiction. From 1996 to 2001, Purdue aggressively marketed OxyContin to patients and doctors while downplaying growing addiction concerns. Over this time-period, both prescribed and illegal use of OxyContin increased across the country.

Starting in 2000, state governments began to alert Purdue to the widespread abuse of OxyContin, and, in 2001, the FDA required Purdue to remove from its label that OxyContin had a low risk of addiction. In the years that followed, lawsuits against Purdue—brought by, among others, individuals, state governments, and federal agencies—proliferated across the United States.

B. The 2004 Indemnity Agreement

At the end of 2004, Purdue's Board of Directors voted to indemnify, among others, Purdue's directors and officers against claims made in connection with their service to the company. *Bryant C. Dunaway v. Purdue Pharma L.P.* (*In re Purdue*

Pharma L.P.), No. 19-cv-10941-CM (S.D.N.Y. June 22, 2020), ECF No. 24-2 (Appellees' Suppl. App'x at SA 627–36) (the "Sackler-Purdue Indemnity Agreement" or the "Indemnity Agreement"). As part of its obligations under the agreement, Purdue agreed to:

> indemnify and hold harmless each Indemnitee from and against any and all expenses (including attorneys' fees), amounts paid or incurred in satisfaction of or as part of settlements, judgments, fines, penalties, liabilities and similar or related items incurred or suffered or threatened to be incurred or suffered as a result of or in connection with such Indemnitee being made or threatened to be made a party to or participant in any pending, threatened or completed actions, suits or proceedings, whether civil, criminal, administrative, arbitrative or investigative . . . .

Id. at 628–29. Purdue further agreed to "advance all costs and expenses (including attorneys' fees and expenses) incurred by the Indemnitee in defending any one or more Proceedings." *Id*. at 630.

The protections conferred by the Indemnity Agreement were expansive and had no immediate time limit. The agreement ensured that "[t]he Indemnitee's rights under these provisions shall continue after the Indemnitee has ceased to serve" in his or her official capacity at Purdue, and "shall be binding on and inure to the benefit of successors, assigns, legatees, distributees, heirs, executors, guardians, administrators, estates and other legal representatives." *Id*. at 635.

At the same time, the Indemnity Agreement contained a bad faith carveout. Purdue's indemnification obligations did not extend to matters where "a final decision by a court . . . establishe[d] that the Indemnitee did not act in good faith." *Id.* at 629.

C. Sackler Conduct Between 2007 and 2019

Starting in 2007, the Sacklers anticipated that the effects of litigation against Purdue would eventually impact them directly. *See, e.g.*, Deferred Joint App'x at 5059 (David Sackler emailed Jonathan and Richard Sackler, "We will be sued . . . . [A]sk yourself how long it will take these lawyers to figure out that we might settle with them if they can freeze our assets and threaten us."). From 2008 to 2016, Purdue distributed a significant proportion of the company's revenue—an approximated $11 billion in total—to Sackler family trusts and holding companies. This represented an increase in the distribution pattern from years prior and "drained Purdue's total assets by 75% and Purdue's 'solvency cushion' by 82%" during that same time period. Special App'x at 40. By 2018, Purdue defended the many lawsuits against it from a significantly weakened financial position, and, by 2019, all Sacklers had stepped down from Purdue's Board of Directors.

D. The DOJ Suit

In 2019, the United States Attorneys' Offices for the Districts of New Jersey and Vermont, and the United States Department of Justice ("DOJ") brought federal criminal and civil charges against Purdue. The criminal counts alleged that Purdue defrauded the government by inducing healthcare providers to prescribe OxyContin and violated the federal anti-kickback statute. The DOJ also brought civil claims under various federal statutes and common law doctrines (such as mistake, unjust enrichment, fraud, nuisance, and negligent entrustment).

In 2020, after filing for bankruptcy, Purdue entered into a plea agreement with the DOJ, the terms of which created future obligations on Purdue. First, in exchange for Purdue pleading guilty to violations of the federal anti-kickback statute, the DOJ agreed it would "not initiate any further criminal charges against Purdue." Deferred Joint App'x at 4798. Second, regarding its civil liability, Purdue agreed to a forfeiture judgment of $2 billion; the judgment gave the DOJ "superpriority" to collect on the forfeiture judgment in the event of a liquidation of Purdue's estate. Deferred Joint App'x at 4804. Thus, in any future bankruptcy proceedings, the plea required that Purdue satisfy the DOJ's $2 billion claim ahead of all other creditors' claims.

However, the plea agreement also stipulated that the DOJ would agree to release $1.775 billion of its $2 billion claim so long as a future distribution plan met certain requirements, specifically that an abatement trust for the public benefit would be established and a document repository created. Finally, while the plea agreement released Purdue from any additional civil or administrative monetary claims by the government for the covered conduct, it expressly did not release criminal liability.

E. Purdue Files for Bankruptcy

On September 15, 2019, Purdue and its related entities[5] declared bankruptcy; the Sacklers did not. The Estate of the Debtors (the "Estate" or the "*res*") is estimated at approximately $1.8 billion.

Three days after the bankruptcy filing, the Debtors sought an injunction halting all other lawsuits (almost 3,000 actions against Purdue and over 400 actions against the Sacklers concerning liability for OxyContin). On October 11, 2019, the

[5] Purdue consists of Purdue Pharma L.P., Purdue Pharma Inc., Purdue Transdermal Technologies L.P., Purdue Pharma Manufacturing L.P., Purdue Pharmaceuticals L.P., Imbrium Therapeutics L.P., Adlon Therapeutics L.P., Greenfield BioVentures L.P., Seven Seas Hill Corp., Ophir Green Corp., Purdue Pharma of Puerto Rico, Avrio Health L.P., Purdue Pharmaceutical Products L.P., Purdue Neuroscience Company, Nayatt Cove Lifescience Inc., Button Land L.P., Rhodes Associates L.P., Paul Land Inc., Quidnick Land L.P., Rhodes Pharmaceuticals L.P., Rhodes Technologies, UDF L.P., SVC Pharma L.P., and SVC Pharma Inc.

bankruptcy court enjoined all litigation. At the time, claims against the Debtors and Sacklers were estimated at more than $40 trillion.

II. Procedural History

A. The Mediation and Confirmation Process

Following discovery, as is typical in Chapter 11 bankruptcy, the bankruptcy court ordered mediation to reach a plan of reorganization and avoid liquidation of the Estate. In addition to Purdue and the Sacklers, there were a number of groups that participated in the mediation.[6]

The first phase of the mediation addressed the allocation of the Estate's available funds to non-federal public claimants, such as states and political subdivisions, and private claimants. The second phase largely focused on determining what the Sacklers would contribute to the Debtors' estate. While this second phase resulted in an agreement in principle among the Sacklers, the

[6] The Debtors, Official Committee of Unsecured Creditors of Purdue Pharma L.P., et al. (the "UCC"), Ad Hoc Committee of Governmental and Other Contingent Litigation Claimants ("AHC"), Ad Hoc Group of Non-Consenting States ("NCSG"), Multi-State Governmental Entities Group ("MSGE"), Ad Hoc Group of Individual Victims of Purdue Pharma, L.P. ("PI Ad Hoc Group"), Ad Hoc Committee of NAS Children ("NAS Children"), Ad Hoc Group of Hospitals ("Hospitals"), Third-Party Payor Group ("TPP Group"), and Ratepayer Mediation Participants ("Ratepayers") all participated in the mediation as official Mediation Parties. The Native American Tribes Group ("Tribes Group"), Public School District Claimants ("Public Schools"), the National Association for the Advancement of Colored People, and others also participated in mediation, although not as official Mediation Parties.

Debtors, and several creditors, a group of twenty-five non-consenting states, among others, rejected the agreement.

That agreement guaranteed that the Sacklers would contribute at least $4.275 billion to the Debtors' estate over approximately nine years. In exchange, the Debtors' plan of reorganization contained several nonconsensual releases (the "Shareholder Release," the "Release," or the "Releases") that, in effect, permanently enjoined certain third-party claims against the Sacklers. As initially proposed, the Release provisions were extremely broad and included the release of claims pertaining to, *inter alia*, the same subject matter as any claim treated in the plan; any business or other contractual arrangements including transfers; any employment-related conduct; any pending opioid actions and opioid-related activities; and the bankruptcy process.

In the third phase of the mediation, the Sacklers reached a modified agreement with fifteen out of the twenty-five non-consenting states.[7] The new terms of the modified settlement included additional payments of $50 million by the Sacklers, and the accelerated payment of an additional $50 million from a

[7] The majority of the non-consenting states (California, Connecticut, Delaware, Maryland, Oregon, Rhode Island, Vermont, Washington, and the District of Columbia) (the "Nine") maintained their objections to the plan and were parties to the appeal to the district court.

previously agreed-upon settlement payment. These modifications raised the Sacklers' aggregate contribution to the proposed plan to $4.325 billion. At that time, no changes were made to the Shareholder Release.

Following mediation, a vote on the proposed plan was set in motion. Notice of the confirmation hearing was published in the summer of 2021, with votes for or against confirmation due by mid-July 2021, and reached 98% of adults in the United States and 86% of adults in Canada. More than 120,000 votes were cast, and each voting class voted "overwhelmingly" in favor of the plan. Special App'x at 150–51 ("In the aggregate, the vote was over 95 percent in favor of confirmation . . . . In each class the percent voting in favor of the plan was above 93 percent with the exception of the class of hospital claims, which was over 88 percent . . . .").

Ultimately, on September 1, 2021—after a confirmation hearing that included the live testimony of 41 witnesses and extensive oral argument—the bankruptcy court rendered an oral ruling stating that it would confirm the proposed plan, but with a few changes. Most relevantly, the court modified the Shareholder Release to ensure that the Debtors' conduct must be a legal cause or a legally relevant factor of any released cause of action against the Sacklers:

> I . . . require that the shareholder releases . . . be further qualified than they now are. To apply [only] where . . . a debtor's conduct or the

> claims asserted against it [are] a legal cause or a legally relevant factor to the cause of action against the shareholder released party . . . .

Deferred Joint App'x at 1330–31. The new Shareholder Release thus read in pertinent part:

> [T]he Shareholder Released Parties . . . shall be conclusively, absolutely, unconditionally, irrevocably, fully, finally, forever and permanently released . . . from any and all Causes of Action, including any derivative claims [and future claims] . . . (x) based on or relating to, or in any manner arising from, in whole or in part, (i) the Debtors, . . . (ii) the Estates or (iii) the Chapter 11 Cases and (y) as to which any conduct, omission or liability of any Debtor or any Estate is the legal cause or is otherwise a legally relevant factor.

Special App'x at 920.

B. Bankruptcy Court Order Confirming the Plan[8]

The bankruptcy court confirmed its modified version of the proposed plan ("the Plan") on September 17, 2021, and issued an extensive opinion memorializing its decision. *See In re Purdue Pharma L.P.* ("*Purdue I*"), 633 B.R. 53 (Bankr. S.D.N.Y. 2021) (Robert D. Drain, *Bankr. J.*).

The bankruptcy court order began by describing its task as "resolv[ing] the collective problem presented by an insolvent debtor and a large body of creditors competing for its insufficient assets . . . especially when there are mass claims

[8] This opinion describes the bankruptcy court's opinion and the subsequent district court opinion only to the extent required to explain our reasoning today.

premised on . . . massive harm." *Purdue I*, 633 B.R. at 58. The court found that the confirmation hearing established that the Plan was the *only* "reasonably conceivable" way to resolve the issues in the case, *id*. at 59, and, in doing so, grounded its opinion on the principle that, in bankruptcy, courts "focus the solution away from individual litigations to a fair collective result subject to the unique ability under bankruptcy law to bind holdouts under well-defined circumstances who could not otherwise be bound under non-bankruptcy law." *Id.* at 58.

1. Equitable Considerations

From there, the bankruptcy court asked whether the terms of the Plan created an equitable plan and answered in the affirmative. *Purdue I*, 633 B.R. at 84–95. The court explained that to approve a settlement, a bankruptcy court must determine whether the proposed terms are fair, equitable, and in the estate's best interest. *Id*. at 84. Here, in exchange for the Shareholder Release, the terms included:

> $4.325 billion, coupled with the Sackler[s'] other agreements, including the dedication of the two charities worth at least $175 million for abatement purposes, the Sacklers' agreement to a resolution on naming rights, their agreement not to engage in any business with NewCo [Purdue's successor company], their agreement to exit their foreign companies within a prescribed time, their agreement to various 'snap back' protections to ensure the

> collectability of their settlement payments, and their agreement to an unprecedented extensive document depository accessible to the public that will archive in a comprehensive way the Debtors' history, including as it relates to the development, production, and sale of opioids.

Id. The bankruptcy court also highlighted the extensive mediation and discovery processes that led to the development of these terms. *Id.* at 85–87.

As a legal framework for balancing the equities and determining whether to approve the plan, the court was guided by the factors from *In re Iridium Operating LLC*, 478 F.3d 452, 464–66 (2d Cir. 2007):

> (1) The probability of success, should the issues be litigated, versus the present and future benefits of the settlement; (2) the likelihood of complex and protracted litigation if the settlement is not approved, with its attendant expense, inconvenience and delay, including the difficulty of collecting on a judgment; (3) the interests of the creditors, including the degree to which creditors support the proposed settlement; (4) whether other interested parties support the settlement; (5) the competence and experience of counsel supporting, and the experience and knowledge of the court in reviewing, the settlement; (6) the nature and breadth of the releases to be obtained by officers and directors or other insiders; and (7) the extent to which the settlement is the product of arms-length bargaining.

Purdue I, 633 B.R. at 85.

In applying the *Iridium* factors, the bankruptcy court observed that, in this case, counsel on both sides were experienced and formidable. *Id*. at 86–87. Over 95% of the voters approved the Plan, showing clear creditor support, and the potential difficulty in collecting from the Sacklers and their related entities on any successfully litigated claims was an issue of "significant concern." *Id.* at 89. The court noted that while the Sacklers are worth approximately $11 billion, they are a large family whose assets are "widely scattered and primarily held" in spendthrift trusts—both offshore and in the United States—that are largely unreachable via bankruptcy proceedings.[9] *Id*. at 88. Moreover, certain members of the Sackler family live "outside of the territorial jurisdiction of the United States and might not have subjected themselves sufficiently to the U.S." such that a U.S. court would have personal jurisdiction over them. *Id*. And, perhaps most importantly, according to the court, continued litigation—even if it were limited to the claims at issue—would be extremely expensive and lead to delays. *Id.* at 89–90. Thus, the court reasoned, an order against confirmation would not only destroy the entire settlement but would also result in a major escalation of costs and time. *Id*.

The bankruptcy court also noted that, in exchange for the Shareholder Release, the Sacklers were contributing "the largest amount that shareholders have ever paid in such a context of these types of third party claims and closely related

[9] Spendthrift trusts in the United States may be recovered from, however, if the transfers to such trusts are fraudulent. *Id.* at 88–89.

claims" and that "the non-monetary consideration under the settlement also is substantial." *Id*. at 107. And, according to the bankruptcy court's findings, without approval of the Plan including the Release, Purdue would be forced into liquidation, the DOJ would recover its $2 billion claim first, and recovery by all other creditors would be extremely limited because it would not be supplemented with Sackler funds. *Id*. at 108–09; *see also id*. at 84 ("Without the $4.325 billion being paid by the Sacklers under the plan and the other elements of the Sackler settlements, those other elements of the plan would not happen. The record is clear on that."). Thus, the court concluded that, in a world without the Plan, the Sacklers would likely be mired in litigation, but it would also be likely that they could successfully shield much of their estimated $11 billion fortune from creditors through spendthrift trusts and offshore accounts, and broader creditor recovery from Purdue's estate would be extremely limited due to the DOJ's superpriority. *Id*. at 84, 109.

2. <u>The Authority of the Bankruptcy Court to Release Third-Party Claims Against the Sacklers</u>

The bankruptcy court next turned to the Plan's release of third-party claims against the Sacklers, which included all claims that had by then been asserted in litigations against the Sacklers by third parties. The Release encompassed both those based on a direct injury to the third-party claimant and those where the claim properly lay with the Debtors (including, for example, whether the Sacklers fraudulently transferred Purdue funds to family spendthrift trusts and other offshore accounts). *Purdue I*, 633 B.R. at 91–95. This overview of claims led the court to the thornier legal issue: whether direct claims by a third-party against a non-debtor (here, the Sacklers) could ever be released through the bankruptcy process. *Id*. at 95.

In addressing the question of its own authority, the bankruptcy court first evaluated threshold arguments and determined that it had subject-matter jurisdiction over the released claims. *Id.* at 95–98. But, in so finding, the court narrowed the Release even further to cover only those claims that directly affect the *res*—these claims included "insurance rights" and "the shareholder released parties' rights to indemnification and contribution" from the Debtors. *Id*. at 97. Likewise, the court noted that "the Debtors' ability to pursue the estates' own closely related, indeed fundamentally overlapping, claims" against the Sacklers also directly affected the *res*. *Id.* at 97–98. The court did not exclude derivative claims from the Release, reasoning that those claims were similarly likely to affect the *res*. *Id.* at 98.

The bankruptcy court next addressed the objectors' due process arguments and found that they reduced to two claims—neither of which it found meritorious. *Id*. at 98–99. The first due process claim argued that the Release was an impermissible "adjudication of the claim." *Id*. at 98. The court disagreed, and instead characterized a release as "part of the settlement of the claim that channels the settlement funds to the estate." *Id*. As such, the bankruptcy court held that the Release did not rule on the underlying merits of the claims being released. *Id*. The objectors' second due process argument claimed that there was inadequate notice. *Id*. at 98–99. The court found adequate notice because the holders of claims against the Debtors had received notice of "the plan's intention to provide a broad release of third-party claims against the shareholders" and other "entities related to the Debtors." *Id*. at 98. As the final part of its due process analysis, the bankruptcy court also found that the claims released by the Plan were constitutionally core claims, so the bankruptcy court had the constitutional power to issue "a final order under Article III of the Constitution." *Purdue I*, 633 B.R. at 99–100.

After clearing the constitutional hurdles, the bankruptcy court began its analysis of statutory authority by noting that the majority of Circuits permit nonconsensual third-party releases, while only three Circuits—the Fifth, Ninth, and Tenth—do not. *Id.* at 100–01. The bankruptcy court concluded that the provision of the Bankruptcy Code relied upon by that minority, 11 U.S.C. § 524(e), is not a statutory impediment to third-party releases. *Id.* at 101–02.

The bankruptcy court instead looked to 11 U.S.C. § 105(a) and § 1123(b)(6) as two potential sources of a bankruptcy court's equitable authority to approve the releases. *Id.* at 102–05. Following a review of pertinent case law, the bankruptcy court held that so long as the releases are limited to those claims legally intertwined with the Debtors' conduct, they are appropriately subject to settlement under both statutory and common law frameworks. *Id.* at 103–05.

The bankruptcy court then looked to this Court's decision in *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136 (2d Cir. 2005), and other case law from this Circuit, to determine which factors a bankruptcy court should consider when determining whether third-party releases are appropriate. *Id.* at 105–06. The court identified the following factors: (1) the third-party releases were narrowly tailored; (2) monetary contributions were critical to the Plan; (3) the success of the Plan hinged on the third-party releases; (4) the affected class or classes overwhelmingly accepted the Plan; (5) the amount being paid under the Plan was substantial (which, the court noted, is not determined by the Sacklers' net worth because defendants' wealth should not dictate settlement terms); and (6) claimants would be compensated fairly under the Plan. *Id.* at 106–09.

Evaluating those factors, the bankruptcy court found that they supported approval of the Plan. It pointed to the significant overlap in third-party claims against both the Debtors and the Sacklers, chiefly that: (1) claims against both derived from the Debtors' conduct, and (2) to the extent that one or more of the Sacklers could be said to have directed that conduct, or to have possessed the knowledge and power to do so, the Sacklers' and Debtors' defenses would be the same. *Id.* at 108. And it added that the potential difficulty, as discussed above, of collecting on any judgment, the existence of spendthrift trusts, and the Estate's limited resources that the litigation process would likely deplete, also weighed in favor of approval of the Plan. *Id*. at 108–09.

In sum, the bankruptcy court predicated confirmation of the Plan on a few limitations to the third-party releases (namely that the Debtors' conduct amount to a legally relevant factor to a released cause of action and that the settled claims affect the *res*), but otherwise—having established its authority to do so—confirmed the Plan. *Id.* at 115.

3. Canadian Creditors' Objections

The bankruptcy court also rejected the objections of certain Canadian municipalities and First Nations (the "Canadian Creditors") to the Plan, which were essentially based on an argument that the Plan improperly classified their claims. *Id.* at 69–72. Specifically, they objected on the basis that those claims should have been classified like the claims of American non-federal governmental creditors and tribal entities, such that they could participate in abatement trusts. *Id.* at 69. Yet, the bankruptcy court observed that, even if the Canadian claims had been otherwise classified, notwithstanding the resulting change in the Canadian Creditors' voting status, the Plan still would have been approved. *Id.* The bankruptcy court's reasons for classifying the Canadian claims separately boiled down to: (1) different regulatory regimes of the United States and Canada, and (2) that the Canadian Creditors did not participate in the mediation process. *Id.* at 70. The bankruptcy court also noted that certain decisions to recognize or confirm the Plan would be left to the Canadian courts. *Id.* at 71.

4. *Pro Se* Objections

Several *pro se* parties also objected to the Plan, but the bankruptcy court similarly found their objections to be without merit. For example, one *pro se* objector asserted that it was improper and unfair that the Plan provided only $700–

$750 million to a particular claimant group's personal injury claims. *Id.* at 78. The bankruptcy court looked to the length of the mediation, rigor of the legal analysis and negotiation, and quality of mediators and lawyers, all to support that the valuation of personal injury claims was reasonable. *Id.* at 78–79. Another *pro se* objector claimed that releasing the Sacklers from civil liability under the Plan was unfair and should not be approved because this plan is "the Sacklers' plan." *Id.* at 82. However, the bankruptcy court disagreed and emphasized that the Plan was "*not* the Sacklers' plan" because it involved an arms-length negotiation among all interested parties with three experienced mediators. *Id.* at 82–83 (emphasis in original).

C. District Court Order Rejecting the Plan

In a December 16, 2021 opinion, the district court vacated the bankruptcy court's decision to confirm the Plan. *In re Purdue Pharma, L.P.* ("*Purdue II*"), 635 B.R. 26 (S.D.N.Y. 2021) (Colleen McMahon, *J.*). Principally, the court ruled that no statutory authority permits third-party releases such as the ones found in the Plan. *Id*. at 89–90. The court based its reasoning on two propositions: first, that the Bankruptcy Code does not expressly allow such releases; and second, that this Circuit's case law "has not yet been required to identify any source [in the Bankruptcy Code] for [the] authority" to grant such releases. *Id.*

1. Subject-Matter Jurisdiction

The district court's analysis of statutory authority was preceded by the preliminary question of the bankruptcy court's jurisdictional reach under the Bankruptcy Code to release the claims encompassed by the Shareholder Release. The district court agreed that the bankruptcy court had subject-matter jurisdiction over all claims because: (1) the third-party claims raised questions as to the distribution of the Estates' property, *id.* at 85; (2) the third-party claims might have altered the liabilities of the Debtors and changed the amount available from the *res*, *id.* at 85–86; (3) the claims had a high degree of interconnectedness with claims against the Debtors, *id.* at 86–87; and (4) Purdue's insurance obligations to members of the Sacklers who were officers of Purdue could have burdened the *res*. *Id.* at 87–88. Accordingly, having found that the release of the third-party claims "*might have* some conceivable effect on the estate of a debtor," the district court concluded that they fell within the bankruptcy court's jurisdiction. *Id*. at 89 (emphasis in original).

2. Statutory Power to Release Third-Party Claims

Turning to the primary issue in this appeal, the district court next ruled that the bankruptcy court did not have statutory authority to release third-party direct claims against the Sacklers because the Sacklers were not the Debtors, and the

Bankruptcy Code does not authorize the "non-consensual" release of "*direct/particularized* claims asserted by *third parties* against *non-debtors*." *Purdue II*, 635 B.R. at 90 (emphasis in original).

The district court's analysis on this issue considered the case law from this Court, the Supreme Court, and other circuit courts. It characterized this Court's holding in *Metromedia* as indicating that third-party releases could be permissible, but as being inconclusive as to whether "such releases [a]re consistent with or authorized by the Bankruptcy Code." *Purdue II*, 635 B.R. at 101. And, to the extent that *Metromedia* suggested that such releases would be permissible in "unique instances," the district court viewed the opinion as having failed to identify what those instances are. *Id*. (internal quotation marks omitted). Due to this perceived lack of clarity, the district court concluded that "while *Metromedia* said a great deal, the case did not hold much of anything," *id*., and thus a bankruptcy court's statutory authority to impose third-party releases is "questionable." *Id* at 89.

Moving on to the Supreme Court, the district court acknowledged that although the Court has never spoken directly on whether the Bankruptcy Code provides authority for these types of releases, it has held, "albeit in contexts different from the one at bar, that a bankruptcy court lacks the power to award relief that varies or exceeds the protections contained in the Bankruptcy Code," and it lacks such power "even in 'rare' cases, and [ ] even when those orders would help facilitate a particular reorganization." *Id*. at 94–96 (citing *Law v. Siegel*, 571 U.S. 415 (2014) and *Czyzewski v. Jevic Holding Corp.*, 580 U.S. 451 (2017)).

At bottom, the district court concluded that no section of the Bankruptcy Code expressly or impliedly provided the requisite statutory authority for the Releases. *Id.* at 115. The district court also rejected the argument that the bankruptcy court possessed residual equitable authority to impose the Releases. *Id.* at 112–14. The district court further ruled that the fact that the Plan required the Releases for confirmation did not vest the bankruptcy court with authority to approve them. *Id.* at 108–09.

3. <u>Classification of Canadian Claims</u>

Finally, the district court agreed with the bankruptcy court that the Canadian Appellants' claims were properly classified differently than those of the domestic claimants, and that all the Bankruptcy Code requires is a reasonable basis for differentiation. *Id.* at 116–17. The equal treatment mandate applies only to creditors within the same class, and the district court held that, under this Court's precedent, there was a reasonable basis to differentiate the Canadian creditors' claims because different regulatory regimes apply, and because the mediation solely involved U.S.-based claimants. *Id.*

This Appeal followed.

D. This Appeal

The Appellants include a variety of interests unified in favor of the confirmation of the Plan: the Debtors, the Official Committee of Unsecured Creditors (the "UCC"),[10] the Ad Hoc Committee of Governmental and Contingent Litigation Claimants (the "AHC"),[11] the Ad Hoc Group of Individual Victims of Purdue Pharma, L.P. ("Pl. Ad Hoc Group"),[12] the Multi-State Governmental

[10] The UCC is composed of eight dedicated members, including individuals who are themselves (or whose loved ones are) victims of the opioid epidemic, representatives of a trade association for 35 independent health insurance companies collectively insuring 110 million members, a member of one of the largest hospital systems in the United States, the Pension Benefit Guaranty Corporation (the federal entity responsible for insuring defined benefit pension plans), a co-defendant in opioid litigation that has asserted indemnification claims against the Debtors, and *three ex officio* members that represent political subdivisions, tribes, and public school districts.

[11] The AHC is composed of ten States, the court-appointed Plaintiffs' Executive Committee in the multi-district litigation captioned *In re National Prescription Opiate Litigation*, Case No. 17-md-02804 (DAP) (N.D. Ohio), six counties, cities, parishes, or municipalities, and one federally recognized American Indian Tribe.

[12] This group comprises over 60,000 individuals who were injured by direct exposure to Purdue's opioid products, who together make up approximately one-half of those who filed personal injury claims in Purdue's Chapter 11 Cases.

Entities Group (the "MSGE"),[13] the Mortimer-side Initial Covered Sackler Persons (the "Mortimer Sacklers"), and the Raymond Sackler Family (the "Raymond Sacklers," and together with the Mortimer Sacklers, the "Sacklers" or "Sackler family").

While this Appeal was pending, eight states—California, Connecticut, Delaware, Maryland, Oregon, Rhode Island, Vermont, and Washington—and the District of Columbia (the "Nine") that had appealed the confirmation of the original settlement, the Debtors, and the Sacklers filed a new settlement agreement with the bankruptcy court that provided for an additional $1.175–$1.675 billion in Sackler contributions (resulting in an aggregate $5.5 to $6.0 billion contribution to the Plan). *See* Order Pursuant to 11 U.S.C. §§ 105 and 363(b) Authorizing and Approving Settlement Term Sheet, *In re Purdue Pharma L.P.*, No. 19-23649 (Bankr. S.D.N.Y. Mar. 10, 2022), ECF No. 4503. The bankruptcy court granted the motion to confirm the revised plan but noted that its confirmation would require one or more orders by this Court or the district court. *Id*. As part of the revised settlement

[13] Members of the MSGE Group are creditors of the Debtors, and many filed prebankruptcy lawsuits against them for their role in fostering the nationwide opioid crisis.

agreement, the Nine agreed to withdraw their opposition to the Plan, including the Shareholder Releases. *Id*.

As a result, the Appellees currently left defending the district court's decision include only U.S. Trustee William K. Harrington ("the Trustee"),[14] several Canadian municipalities and indigenous nations (the "Canadian Creditors"), and several individual *pro se* personal injury claimants (Ronald Bass, Ellen Isaacs, Maria Ecke, Richard Ecke, Andrew Ecke, the Estate of David Jonathan Ecke, and Peter Sottile).

DISCUSSION

I. Standard of Review

A. The Bankruptcy Court's Adjudicatory Authority

As stated by the district court, to the extent claims encompassed by the third-party releases are non-core under *Stern v. Marshall*, the bankruptcy court was required to submit "proposed findings of fact and conclusions of law to the district

[14] Congress has authorized the Attorney General to appoint U.S. Trustees, who are Department of Justice officials, to supervise the administration of bankruptcy cases. 28 U.S.C. §§ 581–589a. U.S. Trustees "serve as bankruptcy watch-dogs to prevent fraud, dishonesty, and overreaching in the bankruptcy arena." H.R. Rep. No. 95-595, at 88 (1977). They "may raise and may appear and be heard on any issue in any case or proceeding" brought under the Bankruptcy Code. 11 U.S.C. § 307. Congress specifically empowered U.S. Trustees to comment on proposed disclosure statements and Chapter 11 plans of reorganization. 28 U.S.C. § 586(a)(3)(B).

court, for that court's [de novo] review and issuance of final judgment." 564 U.S. 462, 471 (2011). *Stern* defines core claims as those stemming "from the bankruptcy itself" or those which "would necessarily be resolved in the claims allowance process." *Id.* at 499. For substantially the same reasons articulated by the district court, *see Purdue II*, 635 B.R. at 79-83, we agree that the bankruptcy court lacked constitutional authority to finally approve of the releases, and, therefore, that the district court correctly construed the bankruptcy court's decision as setting forth its proposed findings of fact and conclusions of law for the district court's de novo review. In short, the released claims at issue here—which, pursuant to the Plan, are permanently enjoined, have res judicata effect, and, as such, are effectively finally resolved—do not stem "from the bankruptcy itself," *Stern*, 564 U.S. at 499, but are direct claims, arising under state law, against non-debtors held by third parties who have not sought to recover on those claims in bankruptcy, or otherwise consented to a bankruptcy court's adjudication of those claims.

It is true, as Debtors note, that the resolution of the third-party claims might impact the *res* of the Estate—a fact determinative of the district court's statutory jurisdiction under the Code—but the same was true for the counterclaims held in *Stern* to be beyond the bankruptcy court's constitutional reach to finally determine. To the point, had the debtor in *Stern* been successful on her counterclaim against the creditor, the value of the estate would have been impacted; she would have had a property interest in the resulting damages award, which would have, in turn, increased the value of her estate. *See id.* The focus of the constitutional analysis in *Stern* does not turn on the extent to which the non-core claim might alter the creditor-debtor relations in a given bankruptcy. That said, we agree with the district court that the practical import of the *Stern* issue is nonexistent given that only conclusions of law are at issue here, requiring our de novo review under any standard. *See Purdue II*, 635 B.R. at 82 n.54.

B. Appellate Review of the District Court

In an appeal from a district court's review of a bankruptcy court's decision, this Court "independently" reviews the bankruptcy court's conclusions of law de novo and its factual findings for clear error. *Morning Mist Holdings Ltd. v. Krys* (*In re Fairfield Sentry Ltd.*), 714 F.3d 127, 132 (2d Cir. 2013). A factual finding is clearly erroneous when "the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *United States v. U.S. Gypsum Co.*, 333 U.S. 364, 395 (1948). "[I]n reviewing factual findings for clear error, an appellate court is not confined to evidence cited in a lower court's opinion, but must instead review all of the record evidence." *Bankr. Servs, Inc. v. Ernst & Young* (*In re CBI Holding Co.*), 529 F.3d 432, 449 (2d Cir. 2008).

This Court may uphold a bankruptcy court decision on any ground—even one not relied upon by the district court. *Resol. Tr. Corp. v. Best Prods. Co.* (*In re Best Prods. Co.*), 68 F.3d 26, 30 (2d Cir. 1995). As such, we decide all pertinent issues necessary to confirm the Plan and do not limit our analysis solely to the issues addressed below.

II. Nonconsensual Third-Party Releases of Direct Claims

The two primary questions posed on appeal are: (1) whether the bankruptcy court had the authority to approve the nonconsensual release of direct third-party claims against the Sacklers, a non-debtor, through the Plan; and (2) whether the text of the Bankruptcy Code, factual record, and equitable considerations support the bankruptcy court's approval of the Plan. We answer both in the affirmative.

To explain our reasoning, we begin by describing the scope of the Shareholder Releases (including the types of claims covered and the claims at issue here). We then address the various statutory and constitutional arguments raised by the parties. Finally, we evaluate the bankruptcy court's findings regarding the fairness and equitable nature of the Plan, and we articulate factors to help guide future courts evaluating similar issues.

A. The Scope of the Releases

The original version of the Release from the September 2, 2021 Plan of Reorganization settles

> any and all Causes of Action, including . . . [present and future claims], (x) based on or relating to, or in any manner arising from, in whole or in part, (i) the Debtors, . . . (including the Debtors' Opioid-Related Activities, manufacture, marketing and sale of Products, interaction with regulators concerning Opioid-Related Activities or Products, and involvement in the subject matter of the Pending Opioid Actions, and the past, present or future use or misuse of any opioid by a Releasing Party) . . . and (y) as to which any conduct, omission or liability of any Debtor or any Estate is the legal cause or is otherwise a legally relevant factor.

Special App'x at 920. As discussed *supra*, the bankruptcy court subsequently limited the releases such that they only "apply where . . . a debtor's conduct or the claims asserted against it [are] a legal cause or a legally relevant factor to the cause of action against the shareholder released party," Deferred Joint App'x at 1330–31, and the released claims directly affect the *res*, *Purdue I*, 633 B.R. at 97–98.

The released claims can be grouped into two categories: direct claims and derivative claims. In this context, direct claims are causes of action brought to redress a direct harm to a plaintiff caused by a non-debtor third party. *See Marshall* *v. Picard* (*In re Bernard L. Madoff Inv. Secs. LLC*), 740 F.3d 81, 89 n.9 (2d Cir. 2014). By contrast, derivative claims are "ones that arise from harm done to the estate and that seek relief against [the] third part[y] that pushed the debtor[s] into bankruptcy." *Id*. at 89 (internal quotation marks and alterations omitted); *see also Tronox Inc. v. Kerr-McGee Corp.* (*In re Tronox Inc.*), 855 F.3d 84, 100-04 (2d Cir. 2017) (explaining the law of derivative claims in the bankruptcy context). The potential claims released against the Sacklers include, *inter alia*, fraudulent transfer, constructive fraudulent transfer, deceptive marketing, public nuisance, unfair competition, fraudulent misrepresentation, violation of state consumer protection acts, civil conspiracy, negligence, and unjust enrichment. Some of these claims are direct, and some are derivative. As conceded by the parties, fraudulent transfer claims, for example, are typically derivative claims in that the real injury is to the Debtors' estate,[15] and it is well-settled that a bankruptcy court may approve not only third-party releases which are consensual, but also third-party releases of derivative claims because those claims really belong to the estate of the

[15] Although the Plaintiff Ad Hoc Group contends that the district court erred in concluding the claims against the Sacklers are not all derivative, we find no error because certain consumer protection act claims at a minimum constitute direct claims in that the injury belongs directly to the claimant, and not to the Debtors. We need not define the exact claims which fall under the umbrella of direct claims but note that certain state law claims under consumer protection acts likely do.

debtor. *See, e.g.*, 11 U.S.C. § 1123(b)(3)(A) (permitting release of claims as to the estate's property); *Madoff*, 740 F.3d at 88 ("A claim based on rights derivative of, or derived from, the debtor's typically involves property of the estate. By contrast, a bankruptcy court generally has limited authority to approve releases of a non-debtor's independent claims." (internal citation and quotation marks omitted)). The more controversial issue, however, is this Plan's likely release of some direct claims against the Sacklers.

The bankruptcy court's ability to release claims at all derives from its power of discharge. *See generally* 11 U.S.C. § 524(a). Under the Bankruptcy Code, a bankruptcy discharge releases a debtor from personal liability with respect to any debt by enjoining creditors from attempting to collect on that debt, so long as the debtor discloses all its financial information and puts those assets towards its estate. 11 U.S.C. § 524; *Tenn. Student Assistance Corp. v. Hood*, 541 U.S. 440, 447 (2004) ("The discharge order releases a debtor from personal liability with respect to any discharged debt by voiding any past or future judgments on the debt and by operating as an injunction to prohibit creditors from attempting to collect or to recover the debt."); *see also* 11 U.S.C. §§ 521–523. This extraordinary remedy is based on bankruptcy courts' *in rem* jurisdiction over the property of the debtor.

While the Bankruptcy Code forbids a *discharge* of a non-debtor's claim under 11 U.S.C. § 524(e), the releases at issue on appeal do not constitute a discharge of debt for the Sacklers because the releases neither offer umbrella protection against liability nor extinguish all claims. *See MacArthur Co. v. Johns-Manville Corp.* ("*Manville I*"), 837 F.2d 89, 91 (2d Cir. 1988) (ruling that the bankruptcy court had the authority to enjoin third-party claims because "the injunctive orders d[id] not offer the umbrella protection of a discharge in bankruptcy" and were instead limited to suits "that ar[o]se out of or relate[d] to" specific issues central to the bankruptcy).

Thus, the primary dispute is whether direct claims brought by creditors of Purdue against the Sacklers (for which the Debtors' conduct is legally relevant) can be released. As described in the following sections, we conclude that the bankruptcy court possessed both jurisdiction and statutory authority to approve the Releases because the limitations on the scope of the releases are significant and no other argument bars their imposition.

B. Subject-Matter Jurisdiction

As an initial matter, we must ensure the bankruptcy court had subject-matter jurisdiction, pursuant to the Bankruptcy Code, over the released claims. *See Joseph v. Leavitt*, 465 F.3d 87, 89 (2d Cir. 2006) ("[W]e have an independent obligation to consider the presence or absence of subject matter jurisdiction *sua sponte*.").

A bankruptcy court's subject-matter jurisdiction under the Code is broad. It extends to all civil actions so long as "the action's outcome might have any conceivable effect on the bankrupt estate." *Parmalat Cap. Fin. Ltd. v. Bank of Am. Corp.*, 639 F.3d 572, 579 (2d Cir. 2011) (internal quotation marks omitted); *see also* 28 U.S.C. §§ 157(a), 1334. However, that jurisdictional reach is not endless: a bankruptcy court may only "enjoin third-party non-debtor claims that directly affect the *res* of the bankruptcy estate." *Johns-Manville Corp. v. Chubb Indemnity Ins. Co.* ("*Manville III*"), 517 F.3d 52, 66 (2d Cir. 2008). That limitation is in line with the goal that "extending bankruptcy jurisdiction to actions against certain third parties, as well as suits against debtors themselves, is to protect the assets of the estate so as to ensure a fair distribution of those assets at a later point in time." *Pfizer Inc. v. Law Offices of Peter G. Angelos* (*In re Quigley Co.*), 676 F.3d 45, 57 (2d Cir. 2012) (internal quotation marks and alteration marks omitted).

A direct claim brought against non-debtors, such as the Sacklers, "that nevertheless poses the specter of direct impact on the *res* of the bankrupt estate may just as surely impair the bankruptcy court's ability to make a fair distribution of the bankrupt's assets as a third-party suit alleging derivative liability." *Id.* at 58. Accordingly, if, for example, the litigation of the settled claims "would almost certainly result in the drawing down of . . . the bankruptcy estate of [the debtor], the exercise of bankruptcy jurisdiction to enjoin [third-party direct claims is] appropriate." *Id.* Thus, as to statutory jurisdiction, our key inquiry is into the likely impact on the *res*.

We agree with both the bankruptcy court and the district court that the bankruptcy court had statutory jurisdiction to impose the Releases because it is conceivable, indeed likely, that the resolution of the released claims would directly impact the *res*.

First, as both courts below noted, at least some of the third-party claims, although directly asserted against the Sacklers, are closely related to the derivative claims which the Estate might bring against the Sacklers. For example, many of the states that, below, objected to the Plan (but have since withdrawn their claims in favor of settlement) have laws which impose direct liability on individuals who, as officers of a corporation, personally participated in acts of corporate fraud. *See, e.g.*, U.S. Trustee's App'x at 2644–47, 2765, *In re Purdue Pharma L.P.*, No. 21-07532 (S.D.N.Y. Sept. 9, 2021), ECF Nos. 91-7, 91-8. However, although the various state statutes ensure that managerial personnel can be held independently liable for the same conduct that subjects the corporation to liability, those claims often "rely on detailed and virtually identical set of facts to make the claims" against both Purdue and the Sacklers. *Purdue II*, 635 B.R. at 86. As a result of that substantial overlap, the litigation of third-party direct claims against the Sacklers would likely impact the Debtor's ability to pursue, and the likelihood of recovering on, the Estate's own claims against the Sacklers.

Second, the Sacklers are covered by the Sackler-Purdue Indemnity Agreement, and, therefore, depending on the outcome of any given claims against them, would have a reasonable basis to seek indemnification from the Debtors.[16] That possibility is enough to implicate the bankruptcy court's "related to" jurisdiction under our precedent. *See SPV Osus Ltd. v. UBS AG*, 882 F.3d 333, 341-42 (2d Cir. 2018).[17]

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[16] In addition to indemnification claims, the Sacklers might also assert claims against the Estate for either insurance coverage or contribution. *See generally* Appellees' Suppl. App'x at 627–35, *Bryant Dunaway v. Purdue Pharma L.P.* (*In re Purdue Pharma L.P.*), No. 19-10941 (CM) (S.D.N.Y. June 22, 2020), ECF No. 24-2.

[17] In *SPV*, the plaintiffs asserted direct claims against, among other defendants, UBS AG, alleging principally that UBS had aided and abetted the infamous fraud perpetrated by the debtor, Bernard L. Madoff Investment Securities LLC. *See SPV*, 992 F.3d at 338. Although the plaintiffs sought recovery from UBS itself, UBS, in turn, had viable claims for indemnification and contribution against the debtor. *See id.* at 340–42. The possibility that those claims might have succeeded—and the fact that the debtor would incur

To be sure, the Indemnity Agreement plainly bars any indemnification obligation flowing from the Debtors to the Sacklers where a court determines the Sacklers "did not act in good faith." SA 629. Consequently, as to any successful claims against the Sacklers sounding in fraud (such as the state consumer protection claims), the Sacklers would not have any reasonable basis to seek indemnification. Yet, as the district court noted, "the question of bad faith in this case is hotly disputed." *Purdue II*, 635 B.R. at 88. In the end, the jurisdictional issue does not require us to resolve that question; the relevant inquiry is whether the claims for indemnification "*might have* any conceivable effect on the bankrupt estate." *SPV*, 883 F.3d at 339-40 (emphasis added) (internal citation omitted). That standard is plainly satisfied here.

C. Bankruptcy Code Authority

The ultimate authority for the imposition of nonconsensual releases of direct third-party claims against non-debtors is rooted—as it must be—in the Bankruptcy Code, specifically 11 U.S.C. §§ 105(a) and 1123(b)(6). Further bolstering this statutory authority is this Circuit's caselaw stating that a bankruptcy court has authority to impose such releases.

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expense in litigating such claims—was enough to confer jurisdiction on the bankruptcy court to enjoin the plaintiff's direct claims against UBS. *See id.* at 341-42.

1. Statutory Authority

The bankruptcy court correctly grounded its authority for approving the Releases in §§ 105(a) and 1123(b)(6), which provide the statutory basis for the bankruptcy court's equitable authority and permit the bankruptcy court's approval of the Plan. 11 U.S.C. § 105(a) states that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]." 11 U.S.C. § 1123(b)(6) states that "a plan may . . . include any other appropriate provision not inconsistent with the applicable provisions of this title." We deem Appellees' arguments—that since the Bankruptcy Code does not explicitly authorize third-party releases, they are outside of a bankruptcy court's statutory authority—unpersuasive.

First, although we have stated that § 105(a) gives "*broad equitable power* to the bankruptcy courts to carry out the provisions of the Bankruptcy Code," *Adelphia Bus. Sols., Inc. v. Abnos*, 482 F.3d 602, 609 (2d Cir. 2007) (emphasis added), we reject Appellants' suggestion that § 105(a) alone supports the imposition of the releases in this action. Indeed, our case law, and that of the majority of our sister circuits, support the proposition that § 105(a) alone cannot justify the imposition of third-party releases. *See New England Dairies, Inc. v. Dairy Mart Convenience Stores, Inc. (In re Dairy Mart Convenience Stores, Inc.)*, 351 F.3d 86, 92 (2d Cir. 2003) (ruling that an exercise of § 105(a) power must "be tied to another Bankruptcy Code section and not merely to a general bankruptcy concept or objective"); *see, e.g.*, *Brown v. Viegelahn* (*In re Brown*), 960 F.3d 711, 719–20 (5th Cir. 2020) (ruling that bankruptcy courts must link Section 105(a) with another provision of the Bankruptcy Code); *Bird v. Carl's Grocery Co.* (*In re NWFX, Inc.*), 864 F.2d 593, 595 (8th Cir. 1989) (same); *Southern Ry. Co. v. Johnson Bronze Co.* (*In re Johnson Bronze Co.*), 758 F.2d 137, 141 (3d Cir. 1985) (same). Thus, at least one other provision of the Bankruptcy Code must provide the requisite statutory authority. Section 1123(b)(6) does.

As previously stated, 11 U.S.C. § 1123(b)(6) permits the inclusion of "any other appropriate provision" in a plan so long as it is "not inconsistent" with other sections of the Bankruptcy Code. In *United States v. Energy Resources Co., Inc.*, the Supreme Court held that this provision—acting in tandem with § 105(a)—grants bankruptcy courts a "*residual authority*" consistent with "the traditional understanding that bankruptcy courts, as courts of equity, have broad authority to modify creditor-debtor relationships." 495 U.S. 545, 549 (1990) (emphasis added).[18] Thus, in *Energy Resources*, the Court, relying on § 1123(b)(6), permitted

[18] *Energy Resources* refers to 11 U.S.C. § 1123(b)(5). That provision was later recodified as § 1123(b)(6).

bankruptcy courts "to approve reorganization plans designating tax payments as either trust fund or nontrust fund"—even absent express authorization from the Bankruptcy Code. *Id*. at 545. Appellees, however, nevertheless argue that *Energy Resources* does not permit reliance on § 1123(b)(6) because the third-party releases at issue here are "not specifically authorized by the Code." Trustee Br. at 48. Appellees further maintain that *Energy Resources* only speaks to the ability of bankruptcy courts to modify "creditor-debtor" relationships, and that these releases go beyond such relationships. Trustee Br. at 54.

We are not persuaded by Appellees' arguments. First, as the Court's language in *Energy Resources* indicates, § 1123(b)(6) is limited only by what the Code expressly forbids, not what the Code explicitly allows. Second, and as the Seventh Circuit convincingly has held, bankruptcy courts' equitable powers under § 1123(b)(6) include the power "to release third parties from liability." *Airadigm Commc'ns, Inc. v. FEC* (*In re Airadigm Commc'ns, Inc.*), 519 F.3d 640, 657 (7th Cir. 2008). The Sixth Circuit has also ruled that the residual authority grounded in §§ 105(a) and 1123(b)(6) supports a bankruptcy court's power to impose third-party releases. *Class Five Nev. Claimants (00-2516) v. Dow Corning Corp.* (*In re Dow Corning Corp.*), 280 F.3d 648, 656–58 (6th Cir. 2002) (concluding that third-party releases can be appropriate, but that the factual findings presented did not support them). Although our case law has never expressly cited § 1123(b)(6) to support the imposition of third-party releases, we now explicitly agree with these Circuits and conclude that § 1123(b)(6), with § 105(a), permit bankruptcy courts' imposition of third-party releases.

Our sister circuits that have held that the Bankruptcy Code does not support the imposition of nonconsensual third-party releases rely upon the provisions limiting the discharge of debt under 11 U.S.C. § 524(e). *See Bank of N.Y. Tr. Co. v. Official Unsecured Creditors' Comm.* (*In re Pac. Lumber Co.*), 584 F.3d 229, 251–53 (5th Cir. 2009); *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 and Tr. Co. of Tulsa* (*In re W. Real Estate Fund, Inc.*), 922 F.2d 592, 600–02 (10th Cir. 1990). Section 524(e) states that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." 11 U.S.C. § 524(e).

This language assures that an entity also liable with a bankruptcy debtor for "such debt" remains liable notwithstanding the debtor's discharge of its obligation. For example, the entity might be jointly liable for the debt.

The circuits that have read § 524(e) as a bar to third-party releases have reasoned that "it is the debtor[] who has invoked and submitted to the bankruptcy process, that is entitled to its protections; Congress did not intend to extend such benefits to third-party bystanders." *In re W. Real Estate Fund, Inc.*, 922 F.2d at 600–02 (quoting 11 U.S.C. § 524(e)); *In re Pac. Lumber Co.*, 584 F.3d at 252 ("In a variety of contexts, this court has held that Section 524(e) only releases the debtor, not co-liable third parties. These cases seem broadly to foreclose non-consensual non-debtor releases and permanent injunctions." (internal citations omitted)); *In re Lowenschuss*, 67 F.3d at 1401 ("This court has repeatedly held, without exception, that § 524(e) precludes bankruptcy courts from discharging the liabilities of non-debtors.").

In contrast to these holdings, we do not consider 11 U.S.C. § 524(e) to be a bar to such releases. As explained by the Seventh Circuit in *Airadigm*:

> § 524(e) does not purport to limit the bankruptcy court's powers to release a non-debtor from a creditor's claims. If Congress meant to include such a limit, it would have used the mandatory terms "shall" or "will" rather than the definitional term "does." And it would have omitted the prepositional phrase "on, or . . . for, such debt," ensuring that the "discharge of a debt of the debtor *shall* not affect the liability of another entity"—whether related to a debt or not.

519 F.3d at 656. Moreover, "where Congress has limited the powers of the bankruptcy court, it has done so clearly—for example, by expressly limiting the court's power . . . or by creating requirements for plan confirmation." *Id*. (citing to 11 U.S.C. § 105(b) ("a court may not appoint a receiver in a case under this title") and 11 U.S.C. § 1129(a) ("The court shall confirm a plan only if the following requirements are met") as illustrative examples). Following this logic, we see no reason grounded in the text of the Bankruptcy Code to bar the inclusion of third-party releases in plans of reorganization.

2. <u>Second Circuit Case Law</u>

Despite the district court's pronouncement to the contrary, *Purdue II*, 635 at 89, this Court's precedents permit the imposition of nonconsensual third-party releases. Appellants uniformly agree that our precedents support the approval of a plan containing nonconsensual third-party releases. *See, e.g.*, AHC Br. at 18 ("This Court has held on multiple occasions that third-party releases are allowed in appropriate circumstances."); Debtors Br. at 32 ("For more than three decades, this Court has held that bankruptcy courts are authorized to enjoin and release third-party claims against non-debtors, as part of a plan of reorganization, in appropriate circumstances."). But Appellees contend that such releases are the equivalent of an inappropriate discharge, that this Circuit at no point has permitted the release of direct third-party claims in non-asbestos actions, and that no case supports a plan doing so here. Trustee Br. at 69–77; Canadian Creditors Br. at 27–35. That reading is incorrect in the face of our case law, most explicitly *Drexel*, where we concluded: "In bankruptcy cases, a court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtor's reorganization plan." *In re Drexel Burnham Lambert Group, Inc.* ("*Drexel*"), 960 F.2d 285, 293 (2d Cir. 1992). Our opinions in *Manville I* and *Metromedia* further confirm that such releases are neither discharges nor allowable only in the context of asbestos cases.

Manville I stated that injunctive orders barring third-party claims are not necessarily impermissible discharges. 837 F.2d at 91. There, we were presented with a Chapter 11 bankruptcy plan that released over $2 billion in asbestos victims' claims against the insurers of Manville, a distributor of asbestos products. 837 F.2d at 90. While Manville was a debtor in the bankruptcy, its insurers were not. *Id*. at 91. Thus, to obtain the releases, the insurers paid Manville a $770 million settlement. *Id.* at 94. Before this Court, the appellant (a distributor of Manville's products) challenged the bankruptcy court's jurisdiction and authority by arguing that the third-party releases operated as a bankruptcy discharge that cannot be granted to non-debtors under the Bankruptcy Code. *Id*. at 91. We disagreed and ruled that the releases did not constitute a bankruptcy discharge because they (1) did not offer the umbrella protection of a discharge, and (2) did not extinguish the claims against the insurer, but rather "channeled" them "away from the insurers and redirected [them to] the proceeds of the settlement." *Id.* at 91. Moreover, the insurers' rights were "completely derivative of" and "inseparable from" the debtor's rights. *Id.* at 92–93. Thus, plaintiffs' released claims fell well-within the bankruptcy court's jurisdiction over the debtor's estate. *Id*.

We also stated in *Manville I* that the bankruptcy court properly imposed the releases under the Bankruptcy Code. While the bankruptcy court primarily relied on § 363(f)—which permits channeling orders (the funneling of claims into one proceeding to preserve the debtors' estate) under certain circumstances applicable to *Manville I*—it also looked to § 105(a) for additional support. *Id.* at 93; *id.* at 94 (noting both statutory and equitable powers to dispose of the debtor's property free from third-party interests). Moreover, the releases there were "essential" to a "workable reorganization." *Id.* at 94. Thus, although *Manville I* was in the asbestos context, its premise that this Circuit permits third-party releases in bankruptcy still stands. *See In re Metromedia Fiber Network, Inc.* ("*Metromedia*"), 416 F.3d 136, 142

(2d Cir. 2005) (citing *Manville I*); *Drexel*, 960 F.2d at 293 (recognizing the propriety of third-party releases in a reorganization).

Appellees argue, however, that it is significant that *Manville I*, unlike the current appeal, concerned asbestos products because the Bankruptcy Code now explicitly authorizes releases in such circumstances. Trustee Br. at 41–42. That is because in 1994 Congress enacted 11 U.S.C. § 524(g), which expressly allows for the injunction of third-party claims against non-debtors in "actions seeking recovery for damages allegedly caused by the presence of, or exposure to, asbestos or asbestos-containing products." 11 U.S.C. § 524(g)(2)(B)(i)(I); *see* Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 (1994). Thus, under Appellees' view, "[h]ad Congress intended to allow bankruptcy courts to adjust the relationship between non-debtors and other non-debtors in this manner, it would have said so expressly—as it did when it authorized narrow non-debtor releases in the context of bankruptcies involving asbestos." Trustee Br. at 3.

The first blow to Appellees' restrictive reading of the statute comes from the text of the Bankruptcy Reform Act of 1994 itself, which states:

> RULE OF CONSTRUCTION.—Nothing in [the language since enacted as § 524(g)], shall be construed to modify, impair, or supersede any other authority the court has to issue injunctions in connection with an order confirming a plan of reorganization.

Pub. L. 103-394, § 111(b), 108 Stat. 4106, 4117 (1994). Thus, in enacting § 524(g), Congress expressly intended not to change the pre-existing powers of bankruptcy courts. Therefore, neither *Manville I* nor the subsequent adoption of § 524(g) supports a limitation of its reasoning to asbestos claims.

More importantly, this Court's opinion in *Metromedia* flatly rejects a restrictive interpretation of the Bankruptcy Code by stating that third-party releases can be valid outside of the asbestos context. 416 F.3d at 141. In that case, the debtor Metromedia's reorganization plan allowed certain non-debtor directors and officers of the company to "receive a full and complete release, waiver and discharge from . . . any holder of a claim of any nature . . . arising out of or in connection with any matter related to" Metromedia or its subsidiaries. *Id*. at 141 (alterations in original). Creditors challenged the imposition of these types of releases generally on statutory grounds, and specifically on equitable grounds. Although this Court ultimately rejected the imposition of the releases, we did so based on insufficient factual findings, *not* because we found that such releases could not ever be approved. *Id*. at 143.

Regarding the third-party releases themselves, the *Metromedia* court faced many of the same arguments we are presented with today. There, appellants had primarily contended that the non-debtor releases were unauthorized by the Bankruptcy Code, at least on the findings made by the bankruptcy court. *Id.* at 141. But in *Metromedia*, we did not accept those arguments. Instead, we noted that "[w]e have previously held that 'in bankruptcy cases, a court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtor's reorganization plan.'" *Id.* at 141 (alterations adopted) (quoting *Drexel*, 960 F.2d at 293); *see also Metromedia*, 416 F.3d at 141 ("it is clear that such a release is proper only in rare cases"). And, while we acknowledged that some circuits have permitted such releases only in the asbestos context, *id.*, we focused on the circumstances under which other circuits "have approved nondebtor releases," such as when: "the estate received substantial consideration," the plan channeled enjoined claims to a settlement fund as opposed to extinguishing them, "the enjoined claims would indirectly impact the debtor's reorganization" due to factors like indemnification, "the plan otherwise provided for the full payment of the enjoined claims," and affected creditors consent to such releases. *Id*. at 142. Following this review, we then articulated two requirements for the imposition of such releases in this Circuit. First, in order for the inclusion of a release to be approved, the release "*itself*" must be "important to the Plan." *Id*. at 143 (emphasis in the original). Second, the "breadth" of the release must also be "necessary to the Plan." *Id*.

Thus, while we ultimately ruled that the bankruptcy court's findings were insufficient for the imposition of releases under the facts of that case, *Metromedia* nevertheless rests upon the premise that such releases *may* be permitted so long as bankruptcy courts make sufficient factual findings and satisfy certain equitable considerations. *Id.* at 143.

For these reasons, our precedents permit the imposition of third-party releases *jointly* under 11 U.S.C. § 105(a) and 11 U.S.C. § 1123(b)(6).

D. Factors Relevant to Releasing Direct Third-Party Claims Against Non-Debtors

Having upheld the bankruptcy court's statutory authority and jurisdiction to impose such releases, we now turn to the circumstances under which releases may be approved. The Trustee appears to take issue with the fact that the Releases were approved despite their failing to satisfy certain factors stated in *Metromedia*. The Debtors, by contrast, contend that this is exactly the sort of case that epitomizes when third-party nonconsensual releases are proper because (1) the releases are essential to the confirmation of the Plan (including serving as its primary financing); (2) litigation of the settled claims would negatively impact the *res* of the Debtors' estates; (3) the bankruptcy court already narrowed the scope of the releases; and (4) this case is highly unusual and complex given the "inextricable interrelation between the claims against the Debtors and against the Sacklers," Debtors Br. at 65.

We now clarify any ambiguity and identify the factors that should be considered in order for a bankruptcy court to approve of nonconsensual third-party releases of direct claims against a non-debtor and to include them in a plan. In doing so, we remain conscious of the "heightened" "potential for abuse" posed by such releases, and our analysis of pertinent factors is informed by that risk.[19] *Metromedia*, 416 F.3d at 140. We wholeheartedly endorse the view that "third-party releases are not a merit badge that somebody gets in return for making a positive contribution to a restructuring," nor are they "a participation trophy" or "gold star for doing a good job." *In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 726–27 (Bankr. S.D.N.Y. 2019).

[19] This Court has also observed that it is abusive for a bankruptcy court to enjoin third-party claims against a non-debtor based solely on the non-debtor's financial contribution to the estate. *Manville III*, 517 F.3d at 66. "It is . . . precisely this conditioning of financial participation by non-debtors on releases that is subject to the sort of abuse foreseen in *Metromedia*." *Id*. (internal quotation marks omitted).

With that said, bankruptcy courts should look to the following seven factors before imposing nonconsensual third-party releases:

First, courts should consider whether there is an identity of interests between the debtors and released third parties, including indemnification relationships, "such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete the assets of the estate." *Dow Corning*, 280 F.3d at 658; *see also In re Master Mortgage Investment Fund*, 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994) (same).[20] This requirement reflects our observation in *Metromedia* that non-debtor releases have been allowed in circumstances including those where "the enjoined claims would indirectly impact the debtor's reorganization by way of indemnity or contribution." *Metromedia*, 416 F.3d at 142 (internal quotation marks omitted).

Second, courts should consider whether claims against the debtor and non-debtor are factually and legally intertwined, including whether the debtors and the released parties share common defenses, insurance coverage, or levels of

[20] The multifactor test articulated in *In re Master Mortgage Investment Fund* has been widely cited by courts in other circuits. *See, e.g.*, *Monarch Life Ins. Co. v. Ropes & Gray*, 65 F.3d 973, 980 (1st Cir. 1995); *Gillman v. Continental Airlines* (*In re Cont'l Airlines*), 203 F.3d 203, 217 n.17 (3d Cir. 2000); *In re Chicago Invs., LLC*, 470 B.R. 32, 95 (Bankr. D. Mass. 2012); *In re U.S. Fidelis, Inc.*, 481 B.R. 503, 519 (Bankr. E.D. Mo. 2012).

culpability. We note that although the bankruptcy court did not list this as a factor, it discussed that releases limited to those claims legally intertwined with the Debtors' conduct are appropriately subject to settlement. *Purdue I*, 633 B.R. at 104. We agree.

Third, courts should consider whether the scope of the releases is appropriate. This is the second factor evaluated in *Metromedia*. 416 F.3d at 143. In our view, a release is proper in scope when its "breadth" is "necessary to the Plan." *Id*.

Fourth, courts should consider whether the releases are essential to the reorganization, in that the debtor needs the claims to be settled in order for the *res* to be allocated, rather than because the released party is somehow manipulating the process to its own advantage. In other words, it must be the case that, without the releases, "there is little likelihood of [a plan's] success." *Master Mortg. Inv. Fund*, 168 B.R. at 935. This factor also reflects the first factor required by *Metromedia*—that the release be important to the plan. 416 F.3d at 143.

Fifth, courts should consider whether the non-debtor contributed substantial assets to the reorganization. This factor was mentioned by this Court in *Metromedia*, 416 F.3d at 142–43, and is emphasized in *Dow Corning*, 280 F.3d at 658, and *Master Mortgage Investment Fund*, 168 B.R. at 935.

Sixth, courts should consider whether the impacted class of creditors "overwhelmingly" voted in support of the plan with the releases. *Master Mortg. Inv. Fund*, 168 B.R. at 935. A reference point to define "overwhelmingly" can be found in 11 U.S.C. § 524(g)(2)(B)(ii)(IV)(bb), which requires approval by a minimum of 75% of voting creditors in favor of the plan. However, we consider that threshold to be the bare minimum, and instead express approval for requiring overwhelming approval of the plan.

Seventh, and finally, courts should consider whether the plan provides for the fair payment of enjoined claims. In *Metromedia*, we noted that other courts have found such releases permissible when "the plan . . . provided for the full payment of the enjoined claims." 416 F.3d at 142; *see also Dow Corning*, 280 F.3d at 658 (requiring that "[t]he plan provides a mechanism to pay for all, or substantially all, of the class or classes affected by the injunction"). While the full payment of the enjoined claims would of course tend to favor the approval of a plan containing such releases, we are concerned with the fairness of the payment, as opposed to the final amount of payment. Because the amount of the payment does not necessarily indicate its fairness, the determinative question is not whether there is full payment, but rather whether the contributed sum permits the fair resolution of the enjoined claims.

Although consideration of each factor is required, it is not necessarily sufficient—there may even be cases in which all factors are present, but the inclusion of third-party releases in a plan of reorganization should not be approved. Further, as contemplated by *Dow Corning*, the bankruptcy court is required to support each of these factors with specific and detailed findings. 280 F.3d at 658. For the bankruptcy court to make such findings, extensive discovery into the facts surrounding the claims against the released parties will most often be required.

Finally, as with any term in a bankruptcy plan, a provision imposing releases of claims like that at issue here must be imposed against a backdrop of equity. *See Energy Resources*, 495 U.S. at 549 (describing the authority conferred by § 1123(b)(6) as deriving from bankruptcy courts' status as "courts of equity"); *see also Adelphia Bus. Sols., Inc. v. Abnos*, 482 F.3d 602, 609 (2d Cir. 2007) ("Section 105(a) grants broad equitable power to the bankruptcy courts to carry out the provisions of the Bankruptcy Code so long as that power is exercised within the confines of the Bankruptcy Code."). Given the potential for abuse, courts should exercise particular care when evaluating these types of releases.

E. Application of These Factors Based Upon the Bankruptcy Court's Findings

In light of these factors, we now evaluate the bankruptcy court's findings supporting its approval of the Plan. The thorough bankruptcy court opinion, which indicated that it grounded its findings in the tens of millions of documents produced in discovery, informs our analysis.[21]

Factor 1. Identity of Interests Between Debtors and Released Parties

We have described *supra* the identity of interests between the Debtors and those Sacklers named as defendants in the litigations, chiefly that the named Sacklers were directors and officers of the Debtors. Purdue was a closely held corporation, and, according to the bankruptcy court, the record tended to show that the Sacklers "took a major role in corporate decision-making, including Purdue's practices regarding its opioid products that was more akin to the role of

[21] The extensive discovery provided by the parties is exactly the sort that bankruptcy courts should expect when permitting broad third-party releases.

senior management." *Purdue I*, 633 B.R. at 93. This overlap constitutes a sufficient identity of interests between the Debtors and the Sacklers.

Factor 2. Factual and Legal Overlap Between Claims Against Debtors and Settled Third-Party Claims

In the prior sections, we also discussed the factually and legally intertwined nature of the claims against both the Debtors and the Sacklers. More importantly, the bankruptcy court required that the releases only "apply where . . . a debtor's conduct or the claims asserted against it [are] a legal cause or a legally relevant factor to the cause of action against the shareholder released party," Deferred Joint App'x at 1330–31, and the released claims directly affect the *res*, *Purdue I*, 633 B.R. at 97–98. *Cf. Metromedia*, 416 F.3d at 141 (ruling that factual circumstances and equitable considerations did not support a broad release that included the "waiver and discharge from . . . *any* holder of a claim of *any* nature . . . of *any and all* claims . . . arising out of or in connection with *any matter* related to [the Debtor] or one or more subsidiaries . . . based in whole or in part upon *any act* or omission or transaction" (alterations in original, emphasis added)). By so narrowing the Releases, the bankruptcy court ensured sufficient overlap between claims against the Debtors and the settled third-party claims.

Factors 3. and 4. The Releases are Essential to the Reorganization & Proper in Scope

We next evaluate, in tandem with our analysis of the Releases' scope, whether the Releases are essential to reorganization.[22] *See Metromedia*, 416 F.3d at 143. The Releases are essential to reorganization for two reasons. First and foremost, as described *supra*, the Releases are required to ensure that the valuation of the *res* is settled. Otherwise, the Debtors would, in all likelihood, be required to litigate indemnity and contribution claims brought against them by the Sacklers, which would likely deplete the *res*, no matter the ultimate outcome of those claims. The bankruptcy court limited the Releases extensively in order not to exceed its jurisdiction, restricting their scope to ensure that the released claims related to the Debtors' conduct and the Estate. Second, the *res* itself amounted to only approximately $1.8 billion. Without the Plan, the government would recover its $2 billion first, thereby depleting the *res* completely. As a result, many victims of the opioid crisis would go without any assistance and face an uphill battle of

[22] Although we describe these as two separate factors, following *Metromedia*, we analyze them together in this case because the two factors are interrelated. We nevertheless acknowledge that a case with a different factual record might require them to be considered separately.

litigation (in which a single claimant might disproportionately recover) without fair distribution.

On the question of what is essential to the Plan, the Trustee argues that the Sacklers themselves created the conditions that make these releases essential, and that, as a term of their contribution, the Sacklers had insisted upon these releases before the Debtors even entered bankruptcy. Per the Trustee, these facts demonstrate the Sacklers' unworthiness of receiving the benefit of the releases. First, we are not called upon to determine whether the Sacklers are worthy of receiving the benefit of the releases. As noted *supra*, the various equities of the Plan were carefully considered by the bankruptcy court. However, to the extent that there is a fear that this opinion could be read as a blueprint for how individuals can obtain third-party releases in the face of a tsunami of litigation, we caution that the key fact regarding the indemnity agreements at issue is that they were entered into by the end of 2004—well before the contemplation of bankruptcy. Acts taken "'in contemplation of' bankruptcy ha[ve] long been, and continue[] to be, associated with abusive conduct." *Milavetz, Gallop & Milavetz, P.A. v. United States,* 559 U.S. 229, 240 (2010). We would be far less persuaded if the party seeking to be released entered into this type of indemnity agreement in contemplation of such a third-party release in bankruptcy. Of course, this similar restriction falls in line with our decision in *Manville I*, where we approved of releases in favor of insurance companies. 837 F.2d at 90. Similarly, in that action, there was no suggestion that the insurance policies were taken out in contemplation of bankruptcy. *See id*. at 90–91.

As our precedents have suggested, and as we make clear today, if the only reason for the inclusion of a release is the non-debtor's financial contribution to a restructuring plan, then the release is not essential to the bankruptcy. *See Manville III*, 517 F.3d at 66 (cautioning against this type of situation as abusive). But that is not the present case. Here, the Releases are both needed for the distribution of the *res* and to ensure the fair distribution of any recovery for claimants. Thus, we deem the scope of the Releases—as limited by the bankruptcy court—appropriate and the Releases essential to the reorganization.

<u>Factor 5. Substantial Contribution to the Reorganization</u>

When evaluating the substantial nature of the released parties' contribution, our primary focus is on the impact of the financial contribution. The bankruptcy court found the financial contribution by the Sacklers, which totaled approximately $4.325 billion, to be substantial and of course did not change its mind when the Sacklers agreed, after the initial approval of the Plan and during the pendency of this appeal, to increase their contribution to make the settlement equal approximately $5.5-6.0 billion. Order Pursuant to 11 U.S.C. §§ 105 and 363(b) Authorizing and Approving Settlement Term Sheet, *In re Purdue Pharma L.P.*, No. 19-23649-shl (Bankr. S.D.N.Y. Mar. 10, 2022), ECF No. 4503. The bankruptcy court stated its belief that this is one of the largest contributions to bankruptcy anywhere in the country. *Purdue I*, 636 B.R. at 107; *cf. In re Mallinckrodt PLC*, 639 B.R. 837, 852 (Bankr. D. Del. 2022) (approving of bankruptcy plan with releases where the non-debtor third-party contributed $1.6 billion).

The Trustee primarily argues that the Plan is inequitable because it improperly provides a *quid pro quo* to the Debtors, and that if the Sacklers had declared bankruptcy, under the Bankruptcy Code they would have had to dedicate substantially all of their net worth (an estimated $11 billion) to the Estate—well more than the approximately $5.5-6.0 billion they have agreed at this point to fund.[23] It is not for this Court to determine whether a greater contribution from the Sacklers would be desirable, but rather our role is simply to decide

[23] At oral argument, answering a question from the Court, the Trustee conceded that it would oppose the releases even if the Sacklers contributed $10 billion. Oral Arg. Hr'g at 1:27:45–58.

whether the bankruptcy court erred in finding the Sacklers' contribution substantial. It did not. Five and a half billion dollars—purportedly the largest contribution in history for such releases—is a significant sum.

Factor 6. Overwhelming Approval by Creditors

The claimants voted overwhelmingly to approve the Plan. Over 95% of the personal injury classes voted to accept the plan, which is well above the 75% benchmark. Moreover, with the Nine no longer pursuing their objection, the main challenge to this appeal is not by creditors, but by the Trustee—a government entity without a financial stake in the litigation.

Factor 7. Fair Payment of Enjoined Claims

Finally, the Plan provides for the fair payment of claims. As Appellees concede, the valuation of the claims—estimated at $40 trillion—far exceeds the total funds available, as well as the Sacklers' personal wealth. The bankruptcy court also acknowledged that although "in a vacuum the ultimate judgments that could be achieved on the estates' claims (and the closely related third-party claims that are being settled under the plan) might well be higher than" the Sacklers' contribution to the plan, "the vast size of the claims against the Debtors and the vast number of claimants creates the need for the plan's intricate settlements."

Purdue I, 633 B.R. at 93. Thus, as it is not possible to require the full payment of all claims, we do prioritize fair allocation over the full payment of any one claim. The Trustee has not alleged any unequal treatment of claimants, and no party gives us reason to disturb the bankruptcy court's findings that the settlements and allocations were "fair and equitable." *Purdue I*, 633 B.R. at 84 (internal quotation marks omitted).

* * *

For the reasons stated, the bankruptcy court's detailed findings support approval of the Plan under each of the seven factors that we announce in this opinion. We would also note the additional concessions made by the Sacklers—including governance requirements, abatement trusts, the public document archive, and divestment of the Sacklers from the opioid business worldwide—contribute to the Plan's equity. *Purdue I*, 636 B.R. at 107. We therefore find no error with the bankruptcy court's weighing of the equitable considerations.

III. Due Process

Although the bankruptcy court found that there was adequate notice to impose the releases,[24] on appeal, the Trustee asserts that the releases in this action did not comply with due process. We, however, find no due process violation.

A procedural due process claim entails a two-part inquiry: whether claimants were deprived of a protected interest and, if so, whether claimants received adequate notice and a meaningful opportunity to be heard. *Spinelli v. City of New York*, 579 F.3d 160, 168 (2d Cir. 2009). The releases extinguish causes of action, which, as the parties impliedly concede, are a constitutionally protected property interest. *See Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 428 (1982) ("a cause of action is a species of property protected by the Fourteenth Amendment's Due Process Clause"); *Rosu v. City of New York*, 742 F.3d 523, 526 (2d Cir. 2014) ("[T]he cause of action itself constitutes a cognizable property interest."). Thus, the only remaining question is whether claimants lacked adequate notice or a meaningful opportunity to be heard. *Spinelli*, 579 F.3d at 168.[25]

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[24] The district court did not reach this issue.

[25] In this respect, the Trustee is correct that the Release "permanently extinguish[es] virtually all opioid-related claims against the Sacklers and other non-debtors without the consent of every affected claimant." Trustee Br. at 50. Certainly, that aspect of the Release raises due process concerns—but it does not resolve them. "Once due process is triggered, the question becomes what process is due." *In Matter of Motors Liquidation Co.*,

The Trustee argues that there was a denial of due process because the bankruptcy court failed to provide adequate notice of the confirmation hearing and because the language of the Release is dense. "Due process requires notice reasonably calculated . . . to apprise interested parties of the pendency of the action." *Burda Media, Inc. v. Viertel*, 417 F.3d 292, 303 (2d Cir. 2005) (alteration in original, internal quotation marks omitted). "There is no rigid formula as to the kind of notice that must be given; notice required will vary with circumstances and conditions." *Baker v. Latham Sparrowbush Assocs.*, 72 F.3d 246, 254 (2d Cir. 1995) (internal quotation marks omitted). Here, the bankruptcy court made detailed findings that notice of the confirmation hearing was widespread through a variety of media and that direct notice was provided to any creditors of the Debtors (potential claimants here). The bankruptcy court further observed that although legal training may have been helpful to understanding the initial wording of the releases, the narrowed releases were written more clearly and in "simple . . . plain English." *Purdue I*, 633 B.R. at 60. The Trustee has given no reason to consider such findings error. *See also Mallinckrodt*, 639 B.R. at 876–77 (rejecting similar arguments by the Trustee because of the extensive notice, the representation of the

829 F.3d 135, 158 (2d Cir. 2016). The Trustee's focus on the effect of the Release only gets it so far.

victims by a UCC, the lack of a deadline on claims that can access the opioid trusts, and the fact that the court considered those who might not have received or understood notice). Moreover, the bankruptcy court gave process—*i.e.*, meaningful opportunity to be heard—at the confirmation hearing, which lasted for six days.

The Trustee also questions whether such a release, without an ability to opt-out, can comply with due process because it effectively denies claimants their day in court. But, again, the Due Process Clause does not absolutely protect against the deprivation of property; it instead ensures that a deprivation does not occur without due process. In bankruptcy, the sufficiency of process turns on the adequacy of notice and a meaningful opportunity to be heard, both of which, as explained above, occurred here.[26] The Trustee's argument would essentially call into question all releases through bankruptcy, including bankruptcy discharges (which are one of the most important features of bankruptcy). We decline to so undermine such a critical component of bankruptcy. As described *supra*, the bankruptcy court here acted within its jurisdiction over the bankruptcy estate—

[26] Whatever other constitutional concerns might be raised by the extinguishing of state law claims in bankruptcy, the parties have not argued them here.

even if the third-party claims were not actually the property of the estate—and therefore did not violate due process.

*   *   *

In sum, we reverse the district court's holding that the bankruptcy court lacked the authority to approve the Plan that included the nonconsensual third-party releases. We instead hold that the bankruptcy court properly approved the Plan and made the requisite detailed factual findings to approve of the Shareholder Releases.

IV. The Canadian Creditors' Foreign Sovereign Immunity Act Claim

The Canadian Creditors raise various arguments based upon their contention that Section 10.7(b) of the Plan imposes liability personal to the Canadian Creditors in a manner that violates their sovereign immunity.

As a threshold matter, it is not clear that sovereign immunity is even implicated by the releases. To the contrary, at least in the context of discharging claims against a debtor, "[a] debtor does not seek monetary damages or any affirmative relief from a State by seeking to discharge a debt; nor does he subject an unwilling State to a coercive judicial process. He seeks only a discharge of his debts." *Tenn. Student Assistance Corp. v. Hood*, 541 U.S. 440, 450 (2004). The releases here do not require a suit to be maintained against the Canadian Creditors. Nor do they seek to impose personal liability on the Canadian Creditors. The Canadian Creditors also cannot be described as unwilling with regard to this judicial process, in which they have fully and voluntarily participated. *S.G. Phillips Constructors, Inc. v. City of Burlington* (*In re S.G. Phillips Constructors, Inc.*), 45 F.3d 702, 707 (2d Cir. 1995) ("The Supreme Court and this court have consistently held that in filing a proof of claim the petitioner submits to the bankruptcy court's equitable jurisdiction."). Moreover, the Foreign Sovereign Immunities Act also does not protect the Canadian municipalities because 28 U.S.C. § 1605(a)(1) provides that a foreign state will not be immune from jurisdiction of the courts where the foreign state has waived its immunity either explicitly or by implication. For these reasons, we find that the Plan does not violate the sovereign immunity of the Canadian Creditors.

V. The Cross-Appeal

The bankruptcy court and the district court both determined that the Plan properly differentiated the Canadian objectors' claims from their domestic counterparts. The Canadian Creditors contend it is inequitable that they do not have access to the abatement trusts, but domestic creditors do. Thus, in their view, because § 1129(a)(1) requires equal treatment, the Plan fails. We do not find those arguments persuasive and affirm the district court.

Section 1123(a)(1) provides that "[n]otwithstanding any otherwise applicable non-bankruptcy law, a plan shall designate, subject to section 1122 of this title, classes of claims." 11 U.S.C. § 1123(a)(1). Under 11 U.S.C. § 1122(a), plans may classify claims in a particular class so long as those claims are "substantially similar to the other claims or interests of such class." Yet, the statute itself "does not explicitly address whether similar claims *must* be placed in the same class." *Boston Post Rd. Ltd. P'Ship v. FDIC* (*In re Boston Post Rd. Ltd. P'ship*), 21 F.3d 477, 481 (2d Cir. 1994). Looking to other circuits, which "have generally held that separate classification of similar claims is permissible only upon proof of a legitimate reason for separate classification, and that separate classification to gerrymander an affirmative vote is impermissible," *id.*, this Court has held that "similar claims may not be separately classified solely to engineer an assenting impaired class," *id.* at 482. Instead, the separation of similar claims can only be justified by a legitimate reason. *Id.* at 483; s*ee also In re W.R. Grace & Co.*, 729 F.3d 311, 329 (3d Cir. 2013) (ruling that the separate classification of Canadian claims is appropriate because the "Canadian and U.S. property damage claimants . . . operate under separate tort regimes[] and reached separate settlement agreements"); *Dow Corning*, 280 F.3d at 662 (approving the separate classification of foreign claims because "the bankruptcy court determined that the evidence supported the factual assumptions upon which the classifications are based," including clear expert witness testimony about tort recovery in other nations). Here, both the bankruptcy court and the district court found that the claims were properly differentiated in the Plan because the claims are subject to different regulatory regimes that result in different types of recovery and the Canadian creditors did not participate in the mediation allocation. *Purdue I*, 633 B.R. at 70; *Purdue II*, 635 B.R. at 117.

The Cross-Appellants argue regulatory differences do not suffice to account for the different classification. However, we see no reason to disturb the conclusions of the bankruptcy court and the district court. There are substantive differences among the claims, including both the types of claims and elements of causes of action. Moreover, the Canadian objectors have another source of recovery: Purdue Canada.[27] We believe those reasons alone provide enough

[27] Of note, Purdue Canada reached a separate settlement of $150 million. *See Settlement reached with Purdue Pharma (Canada) for opioid damages*, British Columbia Government News (June 29, 2022), https://news.gov.bc.ca/releases/2022AG0044-001031.

support to differentiate the claims, and thus to affirm the district court's holding on the cross-appeal.

CONCLUSION

For the reasons set forth above, we **REVERSE** the district court's order holding that the Bankruptcy Code does not permit nonconsensual third-party releases of direct claims, and **AFFIRM** the bankruptcy court's approval of the Plan, including the modification made on March 10, 2022, and the case is **REMANDED** to the district court for such further proceedings as may be required, consistent with this opinion. We also **AFFIRM** the district court's denial of the Canadian Creditors' cross-appeal.

RICHARD C. WESLEY, *Circuit Judge*, concurring in the judgment:

Does a bankruptcy court have the power to release direct or particularized claims asserted by third parties against nondebtors without the third parties' consent? Yes—this Court said so in *In re Drexel Burnham Lambert Grp., Inc.*, 960 F.2d 285, 293 (2d Cir. 1992). *Drexel* has not been overruled either by the Supreme Court or by this Court sitting *en banc*. It is binding. Consequently, although the parties have sacrificed a forest on the matter—and rightly so, weighty as it is—that ship has, for better or worse, sailed. I therefore reluctantly concur with the majority's conclusion that a bankruptcy court has the authority to approve a Chapter 11 reorganization plan that includes nonconsensual nondebtor releases. Again: *Drexel* says so.

That said, neither *Drexel*, nor our subsequent discussion of nonconsensual nondebtor releases in *Metromedia*, traces that power back to any provision of the Bankruptcy Code. *See In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005). In fact, although *Metromedia* acknowledged that *Drexel* had already crossed the bridge, it also appreciated its questionable structure, and was wary to traverse it once more. To the point, Judge Jacobs carefully explained "the reluctance to approve nondebtor releases," and cautioned that nowhere—apart from asbestos-related bankruptcies—does the Code authorize them. *See id*. The majority concedes as much; it recognizes that "whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." *Law v. Siegel*, 571 U.S. 415, 421 (2014). Today, it fills that gap with §§ 105 and 1123(b)(6).

Those provisions of the Bankruptcy Code say nothing about nondebtor releases, and I am not convinced that statutory footing is up to the task. Accordingly, although mindful that, for this Court, the issue has already been settled (albeit without any basis in the Code), I write separately to highlight my concerns.

Those concerns are, in brief: extinguishing direct, particularized claims against nondebtors without the claimholder's consent, and without compensating the claimholder, is an extraordinarily powerful tool for a bankruptcy court to wield—indeed, for any court to wield. Congress once before provided clarity on the propriety of third-party releases in bankruptcy. It could do so again, but, since 1994, has not. Absent any movement on that front, the question, which has divided the courts of appeals for decades, would benefit from nationwide resolution by the Supreme Court. In that event, a uniform view of the problem would emerge.

I

The majority's overview of the facts, procedural history, and opinions below, is thorough and well stated. For present purposes, it is sufficient to emphasize exactly what the Shareholder Release[1] purports to do.

Prior to Purdue's Chapter 11 filing, widespread efforts to hold Purdue legally accountable for its role in the opioid epidemic eventually revealed, at least in the eyes of countless plaintiffs, that certain members of the Sackler family were heavily involved with unlawful efforts to boost Purdue's opioid sales. *See In re Purdue Pharma, L.P.* ("*Purdue II*"), 635 B.R. 26, 50–51 (S.D.N.Y. 2021). Seeking to hold the Sackler family members directly liable for their part in perpetuating the opioid epidemic, both private litigants as well as state Attorneys General turned to various state statutes, including consumer protection laws, which, notwithstanding considerable factual overlap with allegations of corporate liability, impose a separate and independent duty on individuals who, by virtue

[1] Defined terms here coincide with the those in the majority opinion.

of their role as either officer, manager, or director of a corporation, personally participated in corporate wrongdoing. *See id.* As Judge McMahon aptly put it:

> [I]t is undisputed that these laws impose liability, and even penalties, on such persons independent of any corporate liability (or lack of same), and independent of any claim the corporation could assert against them for faithless service as a result of those same acts.

Id. at 91. These claims "arise out of the Sacklers' own conduct." *Id.*

The Shareholder Release forever halts those proceedings in their tracks. It permanently enjoins the private and state litigants, as well as all future plaintiffs, from pursuing those claims against the Sacklers—indeed, any claim "of any kind, character[,] or nature whatsoever, Special App'x 798—so long as the Debtors' "conduct, omission, or liability" is "the legal cause or is otherwise a legally relevant factor."[2] *Id.* at 920. No carveout exists for claims based on fraud—claims

[2] The limiting effect of the "legally relevant" requirement is elusive, and its precise reach has, understandably, not been articulated either by the parties, the bankruptcy court, or the majority. Their failure to do so is no fault of their own; it is difficult to predict the various claims which might be asserted directly against the Sacklers, and future litigation will determine whether any given claim falls within the provision. Still, one can envision an exceedingly broad understanding of "legal relevance," and I, for one, am skeptical of the requirement's limiting effect. To illustrate, at issue in *Manville III* were direct claims against Manville's primary insurer alleging that the insurer violated purported state-imposed duties to disclose certain asbestos-related information it learned from Manville. *See In re Johns-Manville Corp.* ("*Manville III*"), 517 F.3d 52, 66 (2d Cir. 2008) *rev'd and remanded on other grounds sub nom. Travelers Indem. Co. v. Bailey*, 557 U.S. 137 (2009). We held that notwithstanding the factual overlap of those claims with claims which might be asserted against Manville, or by Manville against the insurer, the bankruptcy

from which a debtor *could not* seek a discharge under the Code. *See* 11 U.S.C. § 523(a)(2)(A); *see also Archer v. Warner*, 538 U.S. 314, 321 (2003) ("[The Code] ensure[s] that all debts arising out of fraud are excepted from discharge no matter their form." (quotation omitted)). Appellants seek a release broader than that which Congress decided was wise to make available to a debtor in bankruptcy.

On top of that, the Release does not "channel[]" the enjoined claims "to a settlement fund" for compensation, *Metromedia*, 416 F.3d at 142, but instead mandates that any value paid to personal injury claimants regarding, for example, the opioid-related death of another person, be based only upon claims "held against the Debtors, and not to any associated . . . Channeled Claim against a non-Debtor party." Special App'x 634, 693, 734–35. In other words, the value of a channeled claim is only the value of claims against the estate.[3]

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court was without jurisdiction to release the direct claims against the insurer. *See id.* As to those direct claims, Manville's "conduct" or "omission" might be described as legally relevant: they were based on what the insurer learned *from Manville*. I am concerned that "legal relevance" might release claims mirroring those which we have previously held did not fall within bankruptcy jurisdiction.

[3] Consider this example. Someone has a claim against only Purdue and it's worth $100,000. They file a proof of claim and receive a check for some percentage of that claim. Another person has the same claim for the same amount, *and* a direct claim against the Sacklers worth another $100,000. Under the Plan, that party receives only the same amount as the first claimant; they receive no payout on their direct claim against the Sacklers, even though the Sacklers are released from that claim.

This aspect of the Release substantially broadens its reach as compared with the release approved in *Manville I*. *See MacArthur Co. v. Johns-Manville Corp.* ("*Manville I*"), 837 F.2d 89 (2d Cir. 1988). There, we rejected the notion that a release constituted a bankruptcy discharge because the released claims were not extinguished, but were "channeled away from the insurers and redirected at the proceeds of the settlement." *Id.* at 91. Here, the Plan expressly disallows value being paid based on claims against nondebtors, that is, the Sacklers.[4] *Manville I* therefore does not lay the groundwork for the Release's approval.

Finally, the Release is non-consensual; it binds consenting and objecting parties, without providing an opt-out option to those who object.

In summary, the Release enjoins a broader swath of claims than a debtor himself could seek to discharge under the Bankruptcy Code, and it does so without providing any compensation to the claimholders, who must abide by its terms whether they like it or not. The Release encompasses a potentially wide range of

[4] Appellants dispute that characterization; they point to the Plan's language that any distribution "is deemed to be a distribution in satisfaction of all [personal injury] Channeled Claims," and argue that payments from the personal injury trust is in satisfaction of claims both against the Debtors and Sacklers. Mortimer Side Br. at 49 (quoting Special App'x 693). Yet simply stating as much does not make it so where, as here, the amount of distribution is based only upon claims as against the Debtors.

claims and cloaks the Sacklers with blanket immunity. It is "in effect . . . a [] discharge." *Metromedia*, 416 F.3d at 142.

In exchange, the Sacklers have agreed, under the Plan, to offer a substantial sum of money to the Debtors' estate.[5] No doubt, those funds help make possible (a) a more meaningful distribution of the Debtors' estate to its creditors and (b) recovery for those who hold claims against the Debtors. It is equally apparent that the Sacklers mean what they've said: no release, no money. However, our task today is not to decide whether, as a policy matter, the Release is justified. Instead, without ignoring that the Sacklers' substantial contribution will likely play a meaningful role in providing some measure of finality to the countless families who have suffered as a result of the opioid crisis, the dispositive question is whether, under the Bankruptcy Code, a bankruptcy court is authorized to approve the Release.[6]

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[5] Again, however, their contribution is not directed at the satisfaction of third parties' direct claims against them in their individual capacity, but, instead, at the satisfaction of either claims against the Debtors, or claims held by the estate against the Sacklers. As to the latter set of claims, the Sacklers have, in essence, settled derivative claims belonging to the estate and, in return, received a release not just from those derivative claims, but also from claims independently held by third parties.

[6] Of course, the majority correctly recognizes that the antecedent question to the statutory authority analysis is whether the bankruptcy court had jurisdiction under the Code to approve the Release. I do not dispute its conclusion that it did; it is settled law in this

II

The Bankruptcy Code is silent on the matter. That is no surprise. Bankruptcy is the "subject of the relations between a[] . . . debtor[] and his creditors, extending to his and their relief." *Wright v. Union Cent. Life Ins. Co.*, 304 U.S. 502, 513–14 (1938). To that end, Congress created a "comprehensive federal system . . . to govern the orderly conduct of debtors' affairs and creditors' rights." *Eastern Equip. & Servs. Corp. v. Factory Point Nat'l Bank*, 236 F.3d 117, 120 (2d Cir. 2001). In short, the Bankruptcy Code's central focus is on the adjustment of the debtor-creditor relationship. Of course, that adjustment can implicate the interests

Circuit that a bankruptcy court has broad "related to" jurisdiction over any civil proceedings that "might have any conceivable effect" on the estate. *See SPV OSUS Ltd. v. UBS AG*, 882 F.3d 333, 339–40 (2d Cir. 2018). In the easy case, that effect can be direct, as it was in *Manville I*. There, the claims asserted against the insurer sought recovery from the *res* itself. *See Manville I*, 837 F.2d at 93. The bankruptcy court had jurisdiction to prevent the third party from "collect[ing] out of the proceeds of Manville's insurance policies…." *Id.* In the harder case, the effect is less direct. In *SPV*, for example, the plaintiffs asserted direct claims against, among other defendants, UBS AG, alleging principally that UBS had aided and abetted the infamous fraud perpetrated by the debtor, Bernard L. Madoff Investment Securities LLC. *See SPV*, 992 F.3d at 338. Although the plaintiffs sought recovery from UBS itself, UBS, in turn, had viable claims for indemnification and contribution against the debtor. *See id.* at 340–42. The possibility that those claims might succeed—and the fact that the debtor would incur expense in litigating such claims—was enough to confer jurisdiction on the bankruptcy court to enjoin the plaintiff's direct claims against UBS. *See id.* at 341–42. This case looks more like *SPV*, and the majority's explanation as to how the direct claims against the Sacklers might affect the Debtors' estate is sound.

of third-party nondebtors.[7] But as to their own independent obligations, third-party nondebtors are, simply, a nonconcern.

Against that backdrop, there is little to glean from Congressional silence where, as Judge McMahon put it, "one would not expect Congress to speak." *Purdue II*, 635 B.R. at 110. Appellants ask us to accept the remarkable premise that Congress, while believing it wise to except certain claims (*i.e.*, claims for fraud) from a debtor's discharge, took no issue with the idea that such claims could be effectively discharged for nondebtors, who might contribute funds to settle claims against the *debtor*, but who would face *no* consequences from their own, independent liability—even though state laws mandate otherwise. Not only that, appellants ask us to ground this grant of authority in congressional silence, as, again, the Bankruptcy Code does not expressly authorize the practice.

And yet that silence is, effectively, what the majority sees as granting the bankruptcy court a power that is nothing short of extraordinary. It points to 11 U.S.C. § 1123(b)(6), which it says encompasses a bankruptcy court's residual

[7] For example, the automatic stay triggered by a debtor's bankruptcy filing can apply to nondebtors in certain circumstances. *See, e.g.*, *Queenie, Ltd. v. Nygard Int'l*, 321 F.3d 282, 287 (2d Cir. 2003).

equitable authority, and empowers a bankruptcy court to do all but that which the Code expressly forbids. Maj. Op. at 52–53.[8]

To be sure, the Court in *Energy Resources* characterized § 1123(b)(6) as Congress's recognition of a bankruptcy court's residual equitable authority. But it did so in connection with its observation that "bankruptcy courts, as courts of equity, have broad authority to modify *creditor-debtor relationships*." *United States v. Energy Resources Co., Inc.*, 495 U.S. 545, 549 (1990) (emphasis added). That case concerned whether a *debtor's* tax liabilities could be satisfied in an order as determined by the bankruptcy court, over the objection of the Internal Revenue Service. Nothing in *Energy Resources* suggests that within § 1123(b)(6)'s equitable repository is the power to extinguish an individual's claims against a nondebtor without their consent, and without providing them any value in return. Indeed, that case says nothing about a nondebtor's obligations under the Bankruptcy Code whatsoever.

[8] The majority recognizes that the Release cannot be justified solely by § 105. *See Metromedia*, 416 F.3d at 142 ("Any power that a judge enjoys under § 105 must derive ultimately from some other provision of the Bankruptcy Code." (internal citation omitted)). In other words, the Release turns on § 1123(b)(6). I focus my analysis there.

Instead, *Energy Resources* reminds us that bankruptcy courts are courts of equity, and that their ability to carry out the Code's provisions must be understood with that principle in mind. But it does not answer whether under that umbrella of equitable authority exists the power to release, on a nonconsensual basis, nondebtors from direct claims held by third parties. Nor does *Energy Resources* suggest that a bankruptcy court's well of residual equitable authority, so long as it does not run up against a more specific provision of the Code, is bottomless.

Again: that case concerned the adjustment of a creditor-debtor relationship, which, as provided above, is a bankruptcy court's *raison d'etre*. Courts should understand any congressional grant of equitable authority to the bankruptcy court with that principal purpose in mind. Releasing nondebtors from their own liability—provided for under state law—over the objection of a claimholder and without compensating that claimholder is so far afield from that purpose that plugging-and-playing *Energy Resources*' description of § 1123(b)(6) can't be right.[9]

[9] The decisions from our sister circuits cited by the majority are no more persuasive. Those decisions also rely on *Energy Resources'* characterization of § 1123(b)(6). *See, e.g.*, *In re Airadigm Commc'ns, Inc.*, 519 F.3d 640, 657 (7th Cir. 2008). In any event, in *Airadigm* itself, the release did not cover, as the Release here does, claims for willful misconduct, a fact emphasized by the Seventh Circuit as justifying its confirmation. *See id.* That case does not signal a green light to the approval of the Shareholder Release. Neither does *In re Dow Corning Corp.*, 280 F.3d 648 (6th Cir. 2002). There, the Sixth Circuit rejected the

Moreover, the Court has, in other contexts, explained that a bankruptcy court's equitable authority is not "unlimited," but instead incorporates "traditional standards in equity practice," and that courts can look to "cases outside the bankruptcy context" to help understand the limits of that authority. *Taggart v. Lorenzen*, 139 S. Ct. 1795, 1801–02 (2019).[10] The majority does not liken the equitable authority recognized today to anything traditionally recognized at equity. I too am at a loss. Indeed, the idea that bankruptcy courts can order the involuntary release of direct claims against nondebtors is "an extraordinary thing" that is "different . . . from what courts ordinarily do." *In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 723 (S.D.N.Y. 2019).

At bottom, if Congress intended so extraordinary a grant of authority, it should say so. *See Czyzewski v. Jevic Holding Corp.*, 580 U.S. 451, 465 (2017) (requiring "more than simple statutory silence if, and when, Congress were to

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third-party release *because* it did not provide an opportunity for objecting claimholders to recover in full. *See id.* at 659–61.

[10] In *Taggart*, the Court drew on traditional equitable standards for civil contempt sanctions outside the bankruptcy context to define a bankruptcy court's authority to hold a party in civil contempt for violating § 523(a)(2)'s discharge injunction. If, as the majority and appellants would have us believe, a bankruptcy court's ability to enforce its injunction were limited only by that which the Code did not forbid, then *Taggart*'s invocation of traditional civil contempt standards would seem misplaced.

intend a major departure" from the Code). It has before; in 1994, it amended the Bankruptcy Code to provide express authorization for nondebtor releases in asbestos-related bankruptcies, subject to a stringent set of requirements. *See* 11 U.S.C. 524(g).[11] That amendment occurred when, at that time, courts, such as in *Drexel*, were then approving nondebtor releases in non-asbestos bankruptcies. Yet Congress endorsed nondebtor releases in only the asbestos context. The parties debate whether Congress' express but limited approval in § 524(g) was an implicit rejection of nondebtor releases in non-asbestos contexts. The majority says no. Regardless of the right answer, the majority's answer pins this Circuit firmly on one side of a weighty issue that, for too long, has split the courts of appeals.

This difference in views has consequences. As it stands, a nondebtor's ability to be released through bankruptcy turns on where a debtor files. Forum-dependent results are anathema to the establishment of "uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8,

[11] Even there, however, the injunction may extend to nondebtors only where the nondebtor is "directly liable or indirectly liable for the conduct of, claims against, or demands on the debtor…." 11 U.S.C. § 524(g)(4)(A)(ii). The Release here is broader; it covers claims aimed at the Sacklers' liability even if it is *independent* from the Debtors' liability. Even under § 524(g), it's far from clear the Release would survive.

cl. 4. Finding implicit grants of extraordinary powers in congressional silence is at cross purposes with the Code's "comprehensive scheme." *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 645 (2012). Absent direction from Congress—and, since 1994, there has been none—or the High Court, the answer is a function of geography.

United States Court of Appeals for the Fifth Circuit

United States Court of Appeals
Fifth Circuit
FILED
September 7, 2022
Lyle W. Cayce
Clerk

No. 21-10449

In the Matter of: Highland Capital Management, L.P.,

Debtor,

NexPoint Advisors, L.P.; Highland Capital Management Fund Advisors, L.P.; Highland Income Fund; NexPoint Strategic Opportunities Fund; Highland Global Allocation Fund; NexPoint Capital, Incorporated; James Dondero; The Dugaboy Investment Trust; Get Good Trust,

Appellants,

versus

Highland Capital Management, L.P.,

Appellee.

Appeal from the United States Bankruptcy Court
for the Northern District of Texas
USDC No. 19-34054
USDC No. 3:21-CV-538

Before Wiener, Graves, and Duncan, *Circuit Judges*.

ON PETITION FOR REHEARING

Stuart Kyle Duncan, *Circuit Judge*:

The petition for panel rehearing is GRANTED. We withdraw our previous opinion, reported at 2022 WL 3571094, and substitute the following:

Highland Capital Management, L.P., a Dallas-based investment firm, managed billion-dollar, publicly traded investment portfolios for nearly three decades. By 2019, however, myriad unpaid judgments and liabilities forced Highland Capital to file for Chapter 11 bankruptcy. This provoked a nasty breakup between Highland Capital and its co-founder James Dondero. Under those trying circumstances, the bankruptcy court successfully mediated with the largest creditors and ultimately confirmed a reorganization plan amenable to most of the remaining creditors.

Dondero and other creditors unsuccessfully objected to the confirmation order and then sought review in this court. In turn, Highland Capital moved to dismiss their appeal as equitably moot. First, we hold that equitable mootness does not bar our review of any claim. Second, we affirm the confirmation order in large part. We reverse only insofar as the plan exculpates certain non-debtors in violation of 11 U.S.C. § 524(e), strike those few parties from the plan's exculpation, and affirm on all remaining grounds.

I. Background

A. Parties

In 1993, Mark Okada and appellant James Dondero co-founded Highland Capital Management, L.P. ("Highland Capital") in Dallas. Highland Capital managed portfolios and assets for other investment advisers and funds through a complex of entities under the Highland umbrella. Highland Capital's ownership-interest holders included Hunter Mountain Investment Trust (99.5%); appellant The Dugaboy Investment

Trust, Dondero's family trust (0.1866%);[1] Okada, personally and through trusts (0.0627%); and Strand Advisors, Inc. (0.25%), the only general partner, which Dondero wholly owned.

Dondero also manages two of Highland Capital's clients—appellants Highland Capital Management Fund Advisors, L.P. and NexPoint Advisors, L.P. (the "Advisors"). Both the Advisors and Highland Capital serviced and advised billion-dollar, publicly traded investment funds for appellants Highland Income Fund, NexPoint Strategic Opportunities Fund, Highland Global Allocation Fund, and NexPoint Capital, Inc. (collectively, the "Funds"), among others. For example, on behalf of the Funds, Highland Capital managed certain investment vehicles known as collateral loan obligations ("CLOs") under individualized servicing agreements.

B. Bankruptcy Proceedings

Strapped with a series of unpaid judgments, Highland Capital filed for Chapter 11 bankruptcy in the District of Delaware in October 2019. The creditors included Highland Capital's interest holders, business affiliates, contractors, former partners, employees, defrauded investors, and unpaid law firms. Among those creditors, the Office of the United States Trustee appointed a four-member Unsecured Creditors' Committee (the "Committee").[2] *See* 11 U.S.C. § 1102(a)(1), (b)(1). Throughout the

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[1] The Dugaboy Investment Trust appeals alongside Dondero's other family trust Get Good Trust (collectively, the "Trusts").

[2] First, Redeemer Committee of the Highland Crusader Fund had obtained a $191 million arbitration award after a decade of litigation against Highland Capital. Second, Acis Capital Management, L.P. and Acis Capital Management GP, LLC had sued Highland Capital after facing an adverse $8 million arbitration award, arising in part from its now-extinguished affiliation. Third, UBS Securities LLC and UBS AG London Branch had received a $1 billion judgment against Highland Capital following a 2019 bench trial in New

bankruptcy proceedings, the Committee investigated Highland Capital's past and current operations, oversaw its continuing operations, and negotiated the reorganization plan. *See id.* § 1103(c). Upon the Committee's request, the court transferred the case to the Northern District of Texas in December 2019.

Highland Capital's reorganization did not proceed under the governance of a traditional Chapter 11 trustee. Instead, the Committee reached a corporate governance settlement agreement to displace Dondero, which the bankruptcy court approved in January 2020. Under the agreed order, Dondero stepped down as director and officer of Highland Capital and Strand to be an unpaid portfolio manager and "agreed not to cause any Related Entity . . . to terminate any agreements" with Highland Capital. The Committee selected a board of three independent directors to act as a quasi-trustee and to govern Strand and Highland Capital: James Seery Jr., John Dubel, and retired Bankruptcy Judge Russell Nelms (collectively, the "Independent Directors"). The order also barred any claim against the Independent Directors in their official roles without the bankruptcy court's authorizing the claim as a "colorable claim[] of willful misconduct or gross negligence." Six months later, at the behest of the creditors, the bankruptcy court appointed Seery as Highland Capital's Chief Executive Officer, Chief Restructuring Officer, and Foreign Representative. The order contained an identical bar on claims against Seery acting in these roles. Neither order was appealed.

Throughout summer 2020, Dondero proposed several reorganization plans, each opposed by the Committee and the Independent Directors.

York. Fourth, discovery vendor Meta-E Discovery had $779,000 in unpaid invoices. The Committee members are not parties on appeal.

Unpersuaded by Dondero, the Committee and Independent Directors negotiated their own plan. When Dondero's plans failed, he and other creditors began to frustrate the proceedings by objecting to settlements, appealing orders, seeking writs of mandamus, interfering with Highland Capital's management, threatening employees, and canceling trades between Highland Capital and its clients. *See Highland Cap. Mgmt., L.P. v. Dondero (In re Highland Cap. Mgmt., L.P.)*, Ch. 11 Case No. 19-34054-SGJ11, Adv. No. 20-03190-SGJ11, 2021 WL 2326350, at *1, *26 (Bankr. N.D. Tex. June 7, 2021) (holding Dondero in civil contempt, sanctioning him $100,000, and comparing this case to a "nasty divorce"). In Seery's words, Dondero wanted to "burn the place down" because he did not get his way. The Independent Directors insisted Dondero resign from Highland Capital, which he did in October 2020.

Highland Capital, meanwhile, proceeded toward confirmation of its reorganization plan—the Fifth Amended Plan of Reorganization of Highland Capital Management, L.P. (the "Plan"). In August 2020, the Independent Directors filed the Plan and an accompanying disclosure statement with the support of the Committee. *See* 11 U.S.C. §§ 1121, 1125. The bankruptcy court approved the statement as well as proposed notice and voting procedures for creditors, teeing up confirmation. Leading up to the confirmation hearing, the Advisors and the Funds asked the court to bar Highland Capital from trading or disposing of CLO assets pending confirmation. The bankruptcy court denied the request, and Highland Capital declined to voluntarily abstain and continued to manage the CLO assets.

Before confirmation, Dondero and other creditors (including several non-appellants) filed over a dozen objections to the Plan. Like Dondero, the United States Trustee primarily objected to the Plan's exculpation of certain non-debtors as unlawful. Highland Capital voluntarily modified the Plan to resolve six such objections. The Plan proposed to create eleven classes of creditors and equity holders and three classes of administrative claimants. *See* 11 U.S.C. § 1122. Of the voting-eligible classes, classes 2, 7, and 9 voted to accept the Plan while classes 8, 10, and 11 voted to reject it.

C. Reorganization Plan

The Plan works like this: It dissolves the Committee, and creates four entities—the Claimant Trust, the Reorganized Debtor, HCMLP GP LLC,[3] and the Litigation Sub-Trust. Administered by its trustee Seery, the Claimant Trust "wind[s]-down" Highland Capital's estate over approximately three years by liquidating its assets and issuing distributions to class-8 and -9 claimants as trust beneficiaries. Highland Capital vests its ongoing servicing agreements with the Reorganized Debtor, which "among other things" continues to manage the CLOs and other investment portfolios. The Reorganized Debtor's only general partner is HCMLP GP LLC. And the Litigation Sub-Trust resolves pending claims against Highland Capital under the direction of its trustee Marc Kirschner.

The whole operation is overseen by a Claimant Trust Oversight Board (the "Oversight Board") comprised of four creditor representatives and one restructuring advisor. The Claimant Trust wholly owns the limited partnership interests in the Reorganized Debtor, HCMLP GP LLC, and the Litigation Sub-Trust. The Claimant Trust (and its interests) will dissolve either at the soonest of three years after the effective date (August 2024) or (1) when it is unlikely to obtain additional proceeds to justify further action, (2) all claims and objections are resolved, (3) all distributions are made, and (4) the Reorganized Debtor is dissolved.

[3] The Plan calls this entity "New GP LLC," but according to the motion to dismiss as equitably moot, the new general partner was later named HCMLP GP LLC. For the sake of clarity, we use HCMLP GP LLC.

Anticipating Dondero's continued litigiousness, the Plan shields Highland Capital and bankruptcy participants from lawsuits through an exculpation provision, which is enforced by an injunction and a gatekeeper provision (collectively, "protection provisions"). The protection provisions extend to nearly all bankruptcy participants: Highland Capital and its employees and CEO; Strand; the Independent Directors; the Committee; the successor entities and Oversight Board; professionals retained in this case; and all "Related Persons"[4] (collectively, "protected parties").[5]

The Plan exculpates the protected parties from claims based on any conduct "in connection with or arising out of" (1) the filing and administration of the case, (2) the negotiation and solicitation of votes preceding the Plan, (3) the consummation, implementation, and funding of the Plan, (4) the offer, issuance, and distribution of securities under the Plan before or after the filing of the bankruptcy, and (5) any related negotiations, transactions, and documentation. But it excludes "acts or omissions that constitute bad faith, fraud, gross negligence, criminal misconduct, or willful misconduct" *and* actions by Strand and its employees predating the appointment of the Independent Directors.

Under the Plan, bankruptcy participants are enjoined "from taking any actions to interfere with the implementation or consummation of the

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[4] The Plan generously defines "Related Persons" to include all former, present, and future officers, directors, employees, managers, members, financial advisors, attorneys, accountants, investment bankers, consultants, professionals, advisors, shareholders, principals, partners, heirs, agents, other representatives, subsidiaries, divisions, and managing companies.

[5] The Plan expressly excludes from the protections Dondero and Okada; NexPoint Advisors, L.P.; Highland Capital Management Fund Advisors, L.P; their subsidiaries, managed entities, managed entities, and members; and the Dugaboy Investment Trust and its trustees, among others.

Plan" or filing any claim related to the Plan or proceeding. Should a party seek to bring a claim against any of the protected parties, it must go to the bankruptcy court to "first determin[e], after notice and a hearing, that such claim or cause of action represents a colorable claim of any kind." Only then may the bankruptcy court "specifically authoriz[e]" the party to bring the claim. The Plan reserves for the bankruptcy court the "sole and exclusive jurisdiction to determine whether a claim or cause of action is colorable" and then to adjudicate the claim if the court has jurisdiction over the merits.

D. Confirmation Order

At a February 2021 hearing, the bankruptcy court confirmed the Plan from the bench over several remaining objections. *See* FED R. BANKR. P. 3017–18; 11 U.S.C. §§ 1126, 1128, 1129. In its later-written decision, the bankruptcy court observed that Highland Capital's bankruptcy was "not a garden variety chapter 11 case." The type of debtor, the reason for the bankruptcy filing, the kinds of creditor claims, the corporate governance structure, the unusual success of the mediation efforts, and the small economic interests of the current objectors all make this case unique.

The confirmation order criticized Dondero's behavior before and during the bankruptcy proceedings. The court could not "help but wonder" if Highland Capital's deficit "was necessitated because of enormous litigation fees and expenses incurred" due to Highland Capital's "culture of litigation." Recounting Highland Capital's litigation history, it deduced that Dondero is a "serial litigator." It reasoned that, while "Dondero wants his company back," this "is not a good faith basis to lob objections to the Plan." It attributed Dondero's bad faith to the Advisors, the Trusts, and the Funds, given the "remoteness of their economic interests." For example, the bankruptcy court "was not convinced of the[] [Funds'] independence" from Dondero because the Funds' board members did not testify and had "engaged with the Highland complex for many years." And so the bankruptcy court "consider[ed] them all to be marching pursuant to the orders of Mr. Dondero." The court, meanwhile, applauded the members of the Committee for their "wills of steel" for fighting "hard before and during this Chapter 11 Case" and "represent[ing] their constituency . . . extremely well."

On the merits of the Plan, the bankruptcy court again approved the Plan's voting and confirmation procedures as well as the fairness of the Plan's classes. *See* 11 U.S.C. §§ 1122, 1125(a)–(c). The court held the Plan complied with the statutory requirements for confirmation. *See id.* §§ 1123(a)(1)–(7), 1129(a)(1)–(7), (9)–(13). Because classes 8, 10, and 11 had voted to reject the Plan, it was confirmable only by cramdown.[6] *See id.* § 1129(b). The bankruptcy court found that the Plan treated the dissenting classes fairly and equitably and satisfied the absolute-priority rule, so the Plan was confirmable. *See id.* § 1129(b)(2)(B)–(C). The court also concluded that the protection provisions were fair, equitable, and reasonable, as well as "integral elements" of the Plan under the circumstances, and were within both the court's jurisdiction and authority. The court confirmed the Plan as proposed and discharged Highland Capital's debts. *Id.* § 1141(d)(1). After confirmation and satisfaction of several conditions precedent, the Plan took effect August 11, 2021.

[6] The bankruptcy court must proceed by nonconsensual confirmation, or "cramdown," 11 U.S.C. § 1129(b), when a class of unsecured creditors rejects a Chapter 11 reorganization plan, *id.* § 1129(a)(8), but at least one impaired class accepts it, *id.* § 1129(a)(10). A cramdown requires that the plan be "fair and equitable" to dissenting classes and satisfy the absolute priority rule—that is, dissenting classes are paid in full before any junior class can retain any property. *Id.* § 1129(b)(2)(B); *see Bank of Am. Nat'l Tr. & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 441–42 (1999).

E. The Appeal

Dondero, the Advisors, the Funds, and the Trusts (collectively, "Appellants") timely appealed, objecting to the Plan's legality and some of the bankruptcy court's factual findings.[7] Together with Highland Capital, Appellants moved to directly appeal the confirmation order to this court, which the bankruptcy court granted. *See* 28 U.S.C. § 158(d). A motions panel certified and consolidated the direct appeals. *See ibid.* Both the bankruptcy court and the motions panel declined to stay the Plan's confirmation pending appeal. Given the Plan's substantial consummation since its confirmation, Highland Capital moved to dismiss the appeal as equitably moot, a motion the panel ordered carried with the case.

* * *

We first consider equitable mootness and decline to invoke it here. We then turn to the merits, conclude the Plan exculpates certain non-debtors beyond the bankruptcy court's authority, and affirm in all other respects.

II. Standard of Review

A confirmation order is an appealable final order, over which we have jurisdiction. *Bullard v. Blue Hills Bank*, 575 U.S. 496, 502 (2015); *see* 28 U.S.C. §§ 158(d), 1291. This court reviews a bankruptcy court's factual findings for clear error and legal conclusions *de novo*. *Evolve Fed. Credit Union v. Barragan-Flores (In re Barragan-Flores)*, 984 F.3d 471, 473 (5th Cir. 2021) (citation omitted).

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[7] The Trusts adopt the Funds' and the Advisors' briefs in full, and Dondero adopts the Funds' brief in full and the Advisors' brief in part. Fed. R. App. P. 28(i).

III. Equitable Mootness

Highland Capital moved to dismiss this appeal as equitably moot. It argues we should abstain from appellate review because clawing back the implemented Plan "would generate untold chaos." We disagree and deny the motion.

The judge-made doctrine of equitable mootness allows appellate courts to abstain from reviewing bankruptcy orders confirming "complex plans whose implementation has substantial secondary effects." *New Indus., Inc. v. Byman (In re Sneed Shipbuilding, Inc.)*, 916 F.3d 405, 409 (5th Cir. 2019) (citing *In re Trib. Media Co.*, 799 F.3d 272, 274, 281 (3d Cir. 2015)). It seeks to balance "the equitable considerations of finality and good faith reliance on a judgment" and "the right of a party to seek review of a bankruptcy order adversely affecting him." *In re Manges*, 29 F.3d 1034, 1039 (5th Cir. 1994) (quoting *First Union Real Estate Equity & Mortg. Inv. v. Club Assocs. (In re Club Assocs.)*, 956 F.3d 1065, 1069 (11th Cir. 1992)); *see In re Hilal*, 534 F.3d 498, 500 (5th Cir. 2008); *see also* 7 Collier on Bankruptcy ¶ 1129.09 (16th ed.), LexisNexis (database updated June 2022) (observing "the equitable mootness doctrine is embraced in every circuit").[8]

This court uses equitable mootness as a "scalpel rather than an axe," applying it claim-by-claim, instead of appeal-by-appeal. *In re Pac. Lumber*

[8] The doctrine's atextual balancing act has been criticized. *See In re Pac. Lumber Co.*, 584 F.3d 229, 240 (5th Cir. 2009) ("Despite its apparent virtues, equitable mootness is a judicial anomaly."); *In re One2One Commc'ns, LLC*, 805 F.3d 428, 438–54 (3rd Cir. 2015) (Krause, J., concurring); *In re UNR Indus., Inc.*, 20 F.3d 766, 769 (7th Cir. 1994) (banishing the term "equitable mootness" as a misnomer); *In re Cont'l Airlines*, 91 F.3d 553, 569 (3d Cir. 1996) (en banc) (Alito, J., dissenting); *see also* Bruce A. Markell, *The Needs of the Many: Equitable Mootness' Pernicious Effects*, 93 Am. Bankr. L.J. 377, 393–96 (2019) (addressing the varying applications between circuits). *But see In re Trib. Media*, 799 F.3d at 287–88 (Ambro, J., concurring) (highlighting some benefits of the equitable mootness doctrine).

Co.(Pacific Lumber), 584 F.3d 229, 240–41 (5th Cir. 2009). For each claim, we analyze three factors: "(i) whether a stay has been obtained, (ii) whether the plan has been 'substantially consummated,' and (iii) whether the relief requested would affect either the rights of parties not before the court or the success of the plan." *In re Manges*, 29 F.3d at 1039 (citing *In re Block Shim Dev. Co.*, 939 F.2d 289, 291 (5th Cir. 1991); and *Cleveland, Barrios, Kingsdorf & Casteix v. Thibaut*, 166 B.R. 281, 286 (E.D. La. 1994)); *see also, e.g.*, *In re Blast Energy Servs.*, 593 F.3d 418, 424–25 (5th Cir. 2010); *In re Ultra Petroleum Corp.*, No. 21-20049, 2022 WL 989389, at *5 (5th Cir. Apr. 1, 2022). No one factor is dispositive. *See In re Manges*, 29 F.3d at 1039.

Here, the bankruptcy court and this court declined to stay the Plan pending appeal, and it took effect August 11, 2021. Given the months of progress, no party meaningfully argues the Plan has not been substantially consummated.[9] *See Pacific Lumber*, 584 F.3d at 242 (observing "consummation includes transferring all or substantially all of the property

[9] Since the Plan's effectuation, Highland Capital paid $2.2 million in claims to a committee member and $525,000 in "cure payments" to other counterparties. The independent directors resigned. The Reorganized Debtor, the Claimant Trust, HCMLP GP LLC, and the Litigation Sub-Trust were created and organized in accordance with the Plan. The bankruptcy court appointed the Oversight Board members, the Litigation Sub-Trust trustee, and the Claimant Trust trustee. Highland Capital assumed certain service contracts, including management of twenty CLOs with approximately $700 million in assets, and transferred its assets and estate claims to the successor entities. Highland Capital's pre-petition partnership interests were cancelled and cease to exist. A third party, Blue Torch Capital, infused $45 million in exit financing, fully guaranteed by the Reorganized Debtor, its operating subsidiaries, the Claimant Trust, and most of their assets. From the exit financing, an Indemnity Trust was created to indemnify claims that arise against the Reorganized Debtor, Claimant Trust, Ligation Sub-Trust, Claimant Trustee, Litigation Trustee, or Oversight Board members. The lone class-1 creditor withdrew its claim against Highland Capital. The lone class-2 creditor has been fully paid approximately $500,000 and issued a note of $5.2 million secured by $23 million of the Reorganized Debtor's assets. Classes 3 and 4 have been paid $165,412. Class 7 has received $5.1 million in distributions from the Claimant Trust, totaling 77% of class-7 claims filed.

covered by the plan, the assumption of business by the debtors' successors, and the commencement of plan distributions" (citing 11 U.S.C. § 1141; and *In re Manges*, 29 F.3d at 1041 n.10)). But that alone does not trigger equitable mootness. *See In re SCOPAC*, 624 F.3d 274, 281–82 (5th Cir. 2010). Instead, for each claim, the inquiry turns on whether the court can craft relief for that claim that would not have significant adverse consequences to the reorganization. Highland Capital highlights four possible disruptions: (1) the unraveling of the Claimant Trust and its entities, (2) the expense of disgorging disbursements, (3) the threat of defaulting on exit-financing loans, and (4) the exposure to vexatious litigation.

Each party first suggests its own all-or-nothing equitable mootness applications. To Highland Capital, Appellants' broad requested remedy with only a minor economic stake demands mooting the entire appeal. To Appellants, the type of reorganization plan categorially bars equitable mootness, or, alternatively, Highland Capital's joining the motion to certify the appeal estops it from asserting equitable mootness. These arguments are unpersuasive and foreclosed by *Pacific Lumber*.

First, Highland Capital contends the entire appeal is equitably moot because Appellants, with only a minor economic stake and questionable good faith, "seek[] nothing less than a complete unravelling of the confirmed Plan." It claims the court cannot "surgically excise[]" certain provisions, as the Funds request, because the Bankruptcy Code prohibits "modifications to confirmed plans after substantial consummation." *See* 11 U.S.C. § 1127(b). Not so.

"Although the Bankruptcy Code . . . restricts post-confirmation plan modifications, it does not expressly limit appellate review of plan confirmation orders." *Pacific Lumber*, 584 F.3d at 240 (footnote omitted) (citing 11 U.S.C. § 1127). This court may fashion "fractional relief" to minimize an appellate disturbance's effect on the rights of third parties. *In re Tex. Grand Prairie Hotel Realty, L.L.C.*, 710 F.3d 324, 328 (5th Cir. 2013) (denying dismissal on equitable mootness grounds because the court "could grant partial relief . . . without disturbing the reorganization"); *cf. In re Cont'l Airlines*, 91 F.3d 553, 571–72 (3d Cir. 1996) (en banc) (Alito, J., dissenting) (observing "a remedy could be fashioned in the present case to ensure that the [debtor's] reorganization is not undermined"). In short, Highland Capital's speculations are farfetched, as the court may fashion the remedy it sees fit without upsetting the reorganization.

Second, Appellants contend that equitable mootness cannot apply—full-stop—because this appeal concerns a liquidation plan, not a reorganization plan. We reject that premise. *See infra* Part IV.A. Even if it were correct, however, this court has conducted the equitable-mootness inquiry for a Chapter 11 liquidation plan in the past. *See In re Superior Offshore Int'l, Inc.*, 591 F.3d 350, 353–54 (5th Cir. 2009). And other circuits have squarely rejected the categorical bar proposed by Appellants. *See In re Abengoa Bioenergy Biomass of Kan., LLC*, 958 F.3d 949, 956–57 (10th Cir. 2020); *In re BGI, Inc.*, 772 F.3d 102, 107–09 (2d Cir. 2014). We do the same.

Finally, Appellants assert that because Highland Capital and NexPoint Advisors, L.P. jointly moved to certify the appeal, it should be estopped from arguing the appeal is equitably moot. They cite no legal support for that approach. We decline to adopt it.

Instead, we proceed with a claim-by-claim analysis, as our precedent requires. Highland Capital suggests only two claims are equitably moot: (1) the protection-provisions challenge and (2) the absolute-priority-rule challenge. Neither provides a basis for equitable mootness.

For the protection provisions, Highland Capital anticipates that, without the provisions, its officers, employees, trustees, and Oversight Board members would all resign rather than be exposed to Dondero-initiated litigation. Those resignations would disrupt the Reorganized Debtor's operation, "significant[ly] deteriorat[ing] asset values due to uncertainty." Appellants disagree, offering several instances when this court has reviewed release, exculpation, and injunction provisions over calls for equitable mootness. *See, e.g.*, *In re Hilal*, 534 F.3d at 501; *Pacific Lumber*, 584 F.3d at 252; *In re Thru Inc.*, 782 F. App'x 339, 341 (5th Cir. 2019) (per curiam). In response, Highland Capital distinguishes this case because the provisions are "integral to the consummated plans." *See In re Charter Commc'ns, Inc.*, 691 F.3d 476, 486 (2d Cir. 2012). We again reject that premise. *See infra* Part IV.E.1. In any event, Appellants have the better argument.

We have before explained that "equity strongly supports appellate review of issues consequential to the integrity and transparency of the Chapter 11 process." *In re Hilal*, 534 F.3d 498, 500 (5th Cir. 2008). That is so because "the goal of finality sought in equitable mootness analysis does not outweigh a court's duty to protect the integrity of the process." *Pacific Lumber*, 584 F.3d at 252. As in *Pacific Lumber*, the legality of a reorganization plan's non-consensual non-debtor release is consequential to the Chapter 11 process and so should not escape appellate review in the name of equity. *Ibid.* The same is true here. Equitable mootness does not bar our review of the protection provisions.

For the absolute-priority-rule challenge,[10] Highland Capital contends our review requires us to "rejigger class recoveries." *Pacific Lumber* is again instructive. There, the court declined to apply equitable mootness to a secured creditor's absolute-priority-rule challenge, as no other panel had

[10] While the issue is nearly forfeited for inadequate briefing, it fails on the merits regardless. *See Roy v. City of Monroe*, 950 F.3d 245, 251 (5th Cir. 2020).

extended the doctrine so far. *Id.* at 243. Similarly, Highland Capital fails to identify a single case in which this court has declined review of the treatment of a class of creditor's claims resulting from a cramdown. *See id.* at 252. Regardless, Appellants challenge the distributions to classes 8, 10, and 11. According to Highland Capital's own declaration, "Class 8 General Unsecured Claims have received their Claimant Trust Interests." But there is no evidence that classes 10 or 11 have received any distributions. *Contra Pacific Lumber*, 584 F.3d at 251 (holding certain claims equitably moot where "the smaller unsecured creditors" had already "received payment for their claims"). As a result, the relief requested would not affect third parties or the success of the Plan. *See In re Manges*, 29 F.3d at 1039. The doctrine of equitable mootness does not bar our review of the cramdown and treatment of class-8 creditors.

We DENY Highland Capital's motion to dismiss the appeal as equitably moot.

IV. Discussion

As to the merits, Appellants fire a bankruptcy-law blunderbuss. They contest the Plan's classification as a reorganization plan, the Plan's satisfaction of the absolute priority rule, the Plan's confirmation despite Highland Capital's noncompliance with Bankruptcy Rule 2015.3, and the sufficiency of the evidence supporting the court's factual finding that the Funds are "owned/controlled" by Dondero. For each, we disagree and affirm. We do, however, agree with Appellants that the bankruptcy court exceeded its statutory authority under § 524(e) by exculpating certain non-debtors, and so we reverse and vacate the Plan only to that extent.

A. Discharge of Debt

We begin with the Plan's classification as a reorganization plan, allowing for automatic discharge of the debts. The confirmation of a Chapter

11 restructuring plan "discharges the debtor from any [pre-confirmation] debt" unless, under the plan, the debtor liquidates its assets, stops "engag[ing] in [its] business after consummation of the plan," and would be denied discharge in a Chapter 7 case. 11 U.S.C. § 1141(d)(1), (3); *see In re Sullivan*, No. 99-11107, 2000 WL 1597984, at *2 (5th Cir. Sept. 26, 2000) (per curiam). The bankruptcy court concluded Highland Capital continued to engage in business after plan consummation, so its debts are automatically discharged. The Trusts call foul because, in their view, Highland Capital's "wind down" of its portfolio management is not a continuation of its business. We disagree.

Whether a corporate debtor "engages in business" is "relatively straightforward." *Um v. Spokane Rock I, LLC*, 904 F.3d 815, 819 (9th Cir. 2018) (contrasting the more complex question for individual debtors); *see Grausz v. Sampson (In re Grausz)*, 63 F. App'x 647, 650 (4th Cir. 2003) (per curiam) (same). That is, "a business entity will not engage in business post-bankruptcy when its assets are liquidated and the entity is dissolved." *Um*, 904 F.3d at 819 (collecting cases).[11] But even a temporary continuation of business after a plan's confirmation is sufficient to discharge a Chapter 11 debtor's debt. *See In re T-H New Orleans Ltd. P'ship*, 116 F.3d 790, 804 n.15 (5th Cir. 1997) (recognizing a debtor's "conducting business for two years following Plan confirmation satisfies § 1141(d)(3)(B)" (citation omitted)). That is the case here.

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[11] *See, e.g.*, *In re W. Asbestos Co.*, 313 B.R. 832, 853 (Bankr. N.D. Cal. 2003) (holding corporate debtor was not engaging in business by merely having directors and officers, rights under an insurance policy, and claims against it); *In re Wood Fam. Ints., Ltd.*, 135 B.R. 407, 410 (Bankr. D. Colo. 1989) (holding corporate debtor was not engaging in business when the plan called for liquidation and discontinuation of its business upon confirmation).

By the plain terms of the Plan, Highland Capital has and will continue its business as the Reorganized Debtor for several years. Indeed, much of this appeal concerns objections to Highland Capital's "continu[ing] to manage the assets of others." Because the Plan contemplates Highland Capital "engag[ing] in business after consummation," 11 U.S.C. § 1141(d)(1), the bankruptcy court correctly held Highland Capital was eligible for automatic discharge of its debts.[12]

B. Absolute Priority Rule

Next, we consider the Plan's compliance with the absolute-priority rule. When assessing whether a plan is "fair and equitable" in a cramdown scenario, courts must invoke the absolute-priority rule. 11 U.S.C. § 1129(b)(1); *see* 7 COLLIER ON BANKRUPTCY ¶ 1129.04. Under that rule, if a class of unsecured claimants rejects a plan, the plan must provide that those claimants be paid in full on the effective date *or* any junior interest "will not receive or retain under the plan . . . any property." 11 U.S.C. § 1129(b)(2)(B).[13]

Because class-8 claimants voted against the Plan, the bankruptcy court proceeded by nonconsensual confirmation. The court concluded the Plan was fair and equitable to class 8 and its distributions were in line with the absolute-priority rule. 11 U.S.C. § 1129(b)(2)(B). The Advisors claim the Plan violates the absolute priority rule by giving class-10 and -11 claimants a

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[12] For the same reasons, we reject the Trusts' follow-on argument extending the same logic to the protection provisions.

[13] *See Pacific Lumber*, 584 F.3d at 244 (noting the rule "enforces a strict hierarchy of [creditor classes'] rights defined by state and federal law" to protect dissenting creditor classes); *see also In re Geneva Steel Co.*, 281 F.3d 1173, 1180 n.4 (10th Cir. 2002) ("[U]nsecured creditors stand ahead of investors in the receiving line and their claims must be satisfied before any investment loss is compensated." (citations omitted)).

"Contingent Claimant Trust Interest" without fully satisfying class-8 claimants. We agree the absolute-priority rule applies, and the Plan plainly satisfies it.

The Plan proposed to pay 71% of class-8 creditors' claims with *pro rata* distributions of interest generated by the Claimant Trust and then *pro rata* distributions from liquidated Claimant Trust assets. Classes 10 and 11 received a *pro rata* share of "Contingent Claimant Trust Interests," defined as a Claimant Trust Interest vesting only when the Claimant Trustee certifies that all class-8 claimants have been paid indefeasibly in full and all disputed claims in class 8 have been resolved. Voilà: no interest junior to class 8 will receive any property until class-8 claimants are paid.

But the Advisors point to Highland Capital's testimony and briefs to suggest the Contingent Claimant Trust Interests (received by classes 10 and 11) are property in some sense because they have value. That argument is specious. Of course, the Contingent Claimant Trust Interests have some small probability of vesting in the future and, thus, has some *de minimis* present value. *See Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 207-08 (1988) (holding a junior creditor's receipt of a presently valueless equity interest is receipt of property). But the absolute-priority rule has never required us to bar junior creditors from ever receiving property. By the Plan's terms, no trust property vests with class-10 or -11 claimants "unless and until" class-8 claims "have been paid indefeasibly in full." *See* 11 U.S.C. § 1129(b)(2)(B)(ii). That plainly comports with the absolute-priority rule.

C. Bankruptcy Rule 2015.3

We turn to whether the failure to comply with Bankruptcy Rule of Procedure 2015.3 bars the Plan's confirmation. The Independent Directors failed to file periodic financial reports per Federal Rule of Bankruptcy Procedure 2015.3(a) about entities "in which the [Highland Capital] estate holds a substantial or controlling interest." The Advisors claim the failure dooms the Plan's confirmation because the Plan proponent failed to comply "with the applicable provisions of this title." 11 U.S.C. § 1129(a)(2). We disagree.

Rule 2015.3 cannot be an applicable provision of Title 11 because the Federal Rules of Bankruptcy Procedure are not provisions of the Bankruptcy Code. *See Bonner v. Adams (In re Adams)*, 734 F.2d 1094, 1101 (5th Cir. 1984) ("The Bankruptcy Rules Enabling Act, 28 U.S.C. § 2075, provides that the Supreme Court may prescribe 'by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure' in bankruptcy courts."); *cf. In re Mandel*, No. 20-40026, 2021 WL 3642331, at *6 n.7 (5th Cir. Aug. 17, 2021) (per curiam) (noting "Rule 2015.3 implements section 419 of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005," which amended 28 U.S.C. § 2073). The Advisors' attempt to tether the rule to the bankruptcy trustee's general duties lacks any legal basis. *See* 11 U.S.C. §§ 704(a)(8), 1106(a)(1), 1107(a). The bankruptcy court, therefore, correctly overruled the Advisors' objection.

D. Factual Findings

One factual finding is in dispute, but we see no clear error. The bankruptcy court found that, despite their purported independence, the Funds are entities "owned and/or controlled by [Dondero]." The Funds ask the court to vacate the factual finding because it threatens the Funds' compliance with federal law and damages their reputations and values. According to the Funds, the characterization is unfair, as *they* are not litigious like Dondero and are completely independent from him. Highland Capital maintains Dondero has sole discretion over the Funds as their portfolio manager and through his control of the Advisors, so the finding is supported by the record.

"Clear error is a formidable standard: this court disturbs factual findings only if left with a firm and definite conviction that the bankruptcy court made a mistake." *In re Krueger*, 812 F.3d 365, 374 (5th Cir. 2016) (cleaned up). We defer to the bankruptcy court's credibility determinations. *See Randall & Blake, Inc. v. Evans (In re Canion)*, 196 F.3d 579, 587–88 (5th Cir. 1999).

Here, the bankruptcy court drew its factual finding from the testimony of Jason Post, the Advisors' chief compliance officer, and Dustin Norris, an executive vice president for the Funds and the Advisors. Post testified that the Funds have independent board members that run them. But the bankruptcy court found Post not credible because "he abruptly resigned" from Highland Capital at the same time as Dondero and is currently employed by Dondero. Norris testified that Dondero "owned and/or controlled" the Funds and Advisors. The bankruptcy court found Norris credible and relied on his testimony. The bankruptcy court also observed that none of the Funds' board members testified in the bankruptcy case and all "engaged with the Highland complex for many years." Because nothing in this record leaves us with a firm and definite conviction that the bankruptcy court made a mistake in finding that the Funds are "owned and/or controlled by [Dondero]," we leave the bankruptcy court's factual finding undisturbed.

E. The Protection Provisions

Finally, we address the legality of the Plan's protection provisions. As discussed, the Plan exculpates certain non-debtor third parties supporting the Plan from post-petition lawsuits not arising from gross negligence, bad faith, or willful or criminal misconduct. It also enjoins certain parties "from taking any actions to interfere with the implementation or consummation of the Plan." The injunction requires that, before any lawsuit is filed, the plaintiff must seek the bankruptcy court's approval of the claim as "colorable"—*i.e.*, the bankruptcy court acts as a gatekeeper. Together, the provisions screen and prevent bad-faith litigation against Highland Capital, its successors, and other bankruptcy participants that could disrupt the Plan's effectiveness.

The bankruptcy court deemed the provisions legal, necessary under the circumstances, and in the best interest of all parties. We agree, but only in part. Though the injunction and gatekeeping provisions are sound, the exculpation of certain non-debtors exceeds the bankruptcy court's authority. We reverse and vacate that limited portion of the Plan.

1. *Non-Debtor Exculpation*

We start with the scope of the non-debtor exculpation. In a Chapter 11 bankruptcy proceeding, "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." 11 U.S.C. § 524(e). Contrary to the bankruptcy court's holding, the exculpation here partly runs afoul of that statutory bar on non-debtor discharge by reaching beyond Highland Capital, the Committee, and the Independent Directors. *See Pacific Lumber*, 584 F.3d 251–53. We must reverse and strike the few unlawful parts of the Plan's exculpation provision.

The parties agree that *Pacific Lumber* controls and also that the bankruptcy court had the power to exculpate both Highland Capital and the Committee members. Appellants, however, submit the bankruptcy court improperly stretched *Pacific Lumber* to shield other non-debtors from breach-of-contract and negligence claims, in violation of § 524(e). Highland Capital counters that the exculpation provision is a commonplace Chapter 11 term, is appropriate given Dondero's litigious nature, does not implicate § 524(e), and merely provides a heightened standard of care.

To support that argument, Highland Capital highlights the distinction between a concededly unlawful release of all non-debtor liability and the

Plain's limited exculpation of non-debtor post-petition liability. *See, e.g.*, *In re PWS Holding Corp.*, 228 F.3d 224, 246–47 (3d Cir. 2000) (describing releases as "eliminating" a covered party's liability "altogether" while exculpation provisions "set[] forth the applicable standard of liability" in future litigation). According to Highland Capital, the Third and Ninth Circuits have adopted that distinction when applying § 524(e). *See Blixseth v. Credit Suisse*, 961 F.3d 1074, 1084 (9th Cir. 2020), *cert. denied*, 141 S. Ct. 1394 (2021); *In re PWS Holding*, 228 F.3d at 246–47. Under those cases, narrow exculpations of post-petition liability for certain critical third-party non-debtors are lawful "appropriate" or "necessary" actions for the bankruptcy court to carry out the proceeding through its statutory authority under § 1123(b)(6) and § 105(a). *See* 11 U.S.C. § 1123(b)(6) ("[A] plan may . . . include any other appropriate provision not inconsistent with the applicable provisions of this title."); *id* § 105(a) ("The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.").

Highland Capital reads *Pacific Lumber* as "in step with the law in [those] other circuits" by allowing a limited exculpation of post-petition liability. *Cf. Blixseth*, 961 F.3d at 1084. We disagree. As the Ninth Circuit acknowledged, our court in *Pacific Lumber* arrived at "a conclusion opposite [the Ninth Circuit's]." 961 F.3d at 1085 n.7. Moreover, the Ninth Circuit expressly disavowed *Pacific Lumber*'s rationale—that an exculpation provision provides a "fresh start" to a non-debtor in violation of § 524(e)—because, in the Ninth Circuit's view, the post-petition exculpation "affects only claims arising from the bankruptcy proceedings themselves." *Ibid.* We are not persuaded, as Highland Capital contends, that the Ninth Circuit was "sloppy" and simply "misread *Pacific Lumber*." *See* O.A. Rec. 19:45–21:38.

The simple fact of the matter is that there is a circuit split concerning the effect and reach of § 524(e).[14] Our court along with the Tenth Circuit hold § 524(e) categorically bars third-party exculpations absent express authority in another provision of the Bankruptcy Code. *Pacific Lumber*, 584 F.3d at 252–53; *Landsing Diversified Props. v. First Nat'l Bank & Tr. Co. of Tulsa (In re W. Real Estate Fund, Inc.)*, 922 F.2d 592, 600 (10th Cir. 1990) (per curiam). By contrast, the Ninth Circuit joins the Second, Third, Fourth, Sixth, Seventh, and Eleventh Circuits in reading § 524(e) to allow varying degrees of limited third-party exculpations. *Blixseth*, 961 F.3d at 1084; *accord In re PWS Holding*, 228 F.3d at 246–47 (allowing third-party releases for "fairness, necessity to the reorganization, and specific factual findings to support these conclusions"); *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 143 (2d Cir. 2005); *In re A.H. Robins Co.*, 880 F.2d 694, 702 (4th Cir. 1989); *In re Dow Corning Corp.*, 280 F.3d 648, 658 (6th Cir. 2002); *In re Airadigm Commc'ns., Inc.*, 519 F.3d 640, 657 (7th Cir. 2008); *In re Seaside Eng'g & Surveying, Inc.*, 780 F.3d 1070, 1078 (11th Cir. 2015).

Our *Pacific Lumber* decision was not blind to the countervailing view, as it twice cites the Third Circuit's contrary holding in other contexts. *See* 584 F.3d at 241, 253 (citing *In re PWS Holding*, 228 F.3d at 236–37, 246). But we rejected the parsing between limited exculpations and full releases that Highland Capital now requests. We are obviously bound to apply our own precedent. *See Hidalgo Cnty. Emergency Serv. Found. v. Carranza (In re Hidalgo Cnty. Emergency Serv. Found.)*, 962 F.3d 838, 841 (5th Cir. 2020)

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[14] Amicus's contention that failing to adopt the Ninth Circuit's holding "would generate a clear circuit split" is wrong. There already is one. *See* Petition for Writ of Certiorari, *Blixseth v. Credit Suisse*, 141 S. Ct. 1394 (No. 20-1028) (highlighting the circuits' divergent approaches to the non-debtor discharge bar under § 524(e)).

("Under our well-recognized rule of orderliness, . . . a panel of this court is bound by circuit precedent." (citation omitted)).

Under *Pacific Lumber*, § 524(e) does not permit "absolv[ing] the [non-debtor] from any negligent conduct that occurred during the course of the bankruptcy" absent another source of authority. 584 F.3d at 252–53; *see also In re Zale Corp.*, 62 F.3d 746, 760 (5th Cir. 1995). At oral argument, Highland Capital pointed only to § 1123(b)(6) and § 105(a) as footholds. *See* O.A. Rec. 16:45–17:28. But in this circuit, § 105(a) provides no statutory basis for a non-debtor exculpation. *In re Zale*, 62 F.3d at 760 (noting "[a] § 105 injunction cannot alter another provision of the code" (citing *In re Oxford Mgmt., Inc.*, 4 F.3d 1329, 1334 (5th Cir. 1993))). And the same logic extends to § 1123(b)(6), which allows a plan to "include any other appropriate provision *not inconsistent with the applicable provisions of this title*." 11 U.S.C. § 1123(b)(6) (emphasis added).

Pacific Lumber identified two sources of authority to exculpate non-debtors. *See* 584 F.3d at 252–53. The first is to channel asbestos claims (not present here). *Id.* at 252 (citing 11 U.S.C. § 524(g)). The second is to provide a limited qualified immunity to creditors' committee members for actions within the scope of their statutory duties. *Pacific Lumber*, 584 F.3d at 253 (citing 11 U.S.C. § 1103(c)); *see In re Vitro S.A.B. de CV*, 701 F.3d 1031, 1069 (5th Cir. 2012). And, though not before the court in *Pacific Lumber*, we have also recognized a limited qualified immunity to bankruptcy trustees unless they act with gross negligence. *In re Hilal*, 534 F.3d at 501 (citing *In re Smyth*, 207 F.3d 758, 762 (5th Cir. 2000)); *accord Baron v. Sherman (In re Ondova Ltd.)*, 914 F.3d 990, 993 (5th Cir. 2019) (per curiam). If other sources exist, Highland Capital failed to identify them. So we see no statutory authority for the full extent of the exculpation here.

The bankruptcy court read *Pacific Lumber* differently. In its view, *Pacific Lumber* created an additional ground to exculpate non-debtors: when the record demonstrates that "costs [a party] might incur defending against suits alleging such negligence are likely to swamp either [it] or the consummated reorganization." 584 F.3d at 252. We do not read the decision that way. The bankruptcy court's underlying factual findings do not alter whether it has statutory authority to exculpate a non-debtor. That is the holding of *Pacific Lumber*.

That leaves one remaining question: whether the bankruptcy court can exculpate the Independent Directors under *Pacific Lumber*. We answer in the affirmative. As the bankruptcy court's governance order clarified, nontraditional as it may be, the Independent Directors were appointed to act together as the bankruptcy trustee for Highland Capital. Like a debtor-in-possession, the Independent Directors are entitled to all the rights and powers of a trustee. *See* 11 U.S.C. § 1107(a); 7 Collier on Bankruptcy ¶ 1101.01. It follows that the Independent Directors are entitled to the limited qualified immunity for any actions short of gross negligence. *See In re Hilal*, 534 F.3d at 501. Under this unique governance structure, the bankruptcy court legally exculpated the Independent Directors.

In sum, our precedent and § 524(e) require any exculpation in a Chapter 11 reorganization plan be limited to the debtor, the creditors' committee and its members for conduct within the scope of their duties, 11 U.S.C. § 1103(c), and the trustees within the scope of their duties, *see Baron*, 914 F.3d at 993. And so, excepting the Independent Directors and the Committee members, the exculpation of non-debtors here was unlawful.

Accordingly, the other non-debtor exculpations must be struck from the Plan. *See Pacific Lumber*, 584 F.3d at 253.[15]

As it stands, the Plan's exculpation provision extends to Highland Capital and its employees and CEO; Strand; the Reorganized Debtor and HCMLP GP LLC; the Independent Directors; the Committee and its members; the Claimant Trust, its trustee, and the members of its Oversight Board; the Litigation Sub-Trust and its trustee; professionals retained by the Highland Capital and the Committee in this case; and all "Related Persons." Consistent with § 524(e), we strike all exculpated parties from the Plan except Highland Capital, the Committee and its members, and the Independent Directors.

[15] Highland Capital, like the bankruptcy court, claims the *res judicata* effect of the January and July 2020 orders appointing the independent directors and appointing Seery as CEO binds the court to include the protection provisions here. We lack jurisdiction to consider collateral attacks on final bankruptcy orders even when it concerns whether the court properly exercised jurisdiction or authority at the time. *See Travelers Indem. Co. v. Bailey*, 557 U.S. 137 (2009); *In re Linn Energy, L.L.C.*, 927 F.3d 862, 866–67 (5th Cir. 2019) (quoting *Bailey*, 557 U.S. at 152). To the extent Appellants seek to roll back the protections in the bankruptcy court's January 2020 and July 2020 orders (which is not clear from their briefing), such a collateral attack is precluded.

As a result, the bankruptcy court was correct insofar as *those* orders have the effect of exculpating the Independent Directors and Seery in his executive capacities, but it was incorrect that *res judicata* mandates their inclusion in the Plan's new exculpation provision. Despite removal from the exculpation provision in the confirmation order, the Independent Directors' agents, advisors, and employees, as well as Seery in his official capacities are all exculpated to the extent provided in the January and July 2020 orders, given the orders' ongoing *res judicata* effects and our lack of jurisdiction to review those orders. But that says nothing of the effect of the Plan's exculpation provision.

2. *Injunction & Gatekeeper Provisions*

We now turn to the Plan's injunction and gatekeeper provisions. Appellants object to the bankruptcy court's injunction as vague and the gatekeeper provision as overbroad. We are unpersuaded.

First, Appellants' primary contention—that the Plan's injunction "is broad" by releasing non-debtors in violation of § 524(e)—is resolved by our striking the impermissibly exculpated parties. *See supra* Part IV.E.1.

Second, Appellants dispute the permanency of the injunction for the legally exculpated parties by enjoining conduct "on and after the Effective Date." Even assuming the issue was preserved,[16] permanency alone is no reason to alter a bankruptcy court's otherwise-lawful injunction on appeal. *See In re Zale*, 62 F.3d at 759–60 (recognizing the bankruptcy court's jurisdiction to issue an injunction in the first place allowed it to issue a permanent injunction).

Third, the Advisors argue that the injunction is "overbroad and vague" because it does not define what it means to "interfere" with the "implementation or consummation of the Plan." That is unsupported by the record. As the bankruptcy court recognized, the Plan defined what constitutes interference: (i) filing a lawsuit, (ii) enforcing judgments, (iii) enforcing security interests, (iv) asserting setoff rights, or (v) acting "in any manner" not conforming with the Plan. The injunction is not unlawfully overbroad or vague.

Finally, Appellants maintain that the gatekeeper provision impermissibly extends to unrelated claims over which the bankruptcy court

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[16] *See Roy*, 950 F.3d at 251 ("Failure adequately to brief an issue on appeal constitutes waiver of that argument." (citation omitted)).

lacks subject-matter jurisdiction. *See In re Craig's Stores of Tex., Inc.*, 266 F.3d 388, 390 (5th Cir. 2001) (noting a bankruptcy court retains jurisdiction post-confirmation only over "matters pertaining to the implementation or execution of the plan" (citations omitted)). While that may be the case, our precedent requires we leave that determination to the bankruptcy court in the first instance.

Courts have long recognized bankruptcy courts can perform a gatekeeping function. Under the "*Barton* doctrine," the bankruptcy court may require a party to "obtain leave of the bankruptcy court before initiating an action in district court when the action is against the trustee or other bankruptcy-court-appointed officer, for acts done in the actor's official capacity." *Villegas v. Schmidt*, 788 F.3d 156, 159 (5th Cir. 2015) (emphasis added) (quoting *Carter v. Rodgers*, 220 F.3d 1249, 1252 (11th Cir. 2000)); *accord Barton v. Barbour*, 104 U.S. 126 (1881).[17] In *Villegas*, we held "that a party must continue to file with the relevant bankruptcy court for permission to proceed with a claim against the trustee." 788 F.3d at 158. Relevant here, we left to the bankruptcy court, faced with pre-approval of a claim, to determine whether it had subject matter jurisdiction over that claim in the first instance. *Id.* at 158–59; *see, e.g.*, *Carroll v. Abide*, 788 F.3d 502, 506–07 (5th Cir. 2015) (noting *Villegas* "rejected an argument that the *Barton* doctrine does not apply when the bankruptcy court lacked jurisdiction"). In other words, we need not evaluate whether the bankruptcy court would have

[17] The Advisors also maintain that Highland Capital is neither a receiver nor a trustee, so *Barton* has no application here. We disagree. Highland Capital, for all practical purposes, was a debtor in possession entitled to the rights of a trustee. *See* 7 COLLIER ON BANKRUPTCY ¶ 1101.01 ("The debtor in possession is generally vested with all of the rights and powers of a trustee as set forth in section 1106 . . . ."); *see also Carter*, 220 F.3d at 1252 n.4. (finding no distinction between bankruptcy court "approved" and bankruptcy court "appointed" officers).

jurisdiction under every conceivable claim falling under the widest interpretation of the gatekeeper provision. We leave that to the bankruptcy court in the first instance.[18]

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In sum, the Plan violates § 524(e) but only insofar as it exculpates and enjoins certain non-debtors. The exculpatory order is therefore vacated as to all parties *except* Highland Capital, the Committee and its members, and the Independent Directors for conduct within the scope of their duties. We otherwise affirm the inclusion of the injunction and the gatekeeper provisions in the Plan.[19]

V. Conclusion

Highland Capital's motion to dismiss the appeal as equitably moot is DENIED. The bankruptcy court's judgment is AFFIRMED in part, REVERSED in part, and REMANDED for further proceedings consistent with this opinion.

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[18] For the same reasons, we also leave the applicability of *Barton*'s limited statutory exception to the bankruptcy and district courts in the first instance. *See* 28 U.S.C. § 959(a) (allowing suit, without leave of the appointing court, if the challenged acts relate to the trustee or debtor in possession "carrying on business connected with [their] property").

[19] Nothing in this opinion should be construed to hinder the bankruptcy court's power to enjoin and impose sanctions on Dondero and other entities by following the procedures to designate them vexatious litigants. *See In re Carroll*, 850 F.3d 811, 815 (5th Cir. 2017) (per curiam). But non-debtor exculpation within a reorganization plan is not a lawful means to impose vexatious litigant injunctions and sanctions.

Faculty

Hon. Melanie L. Cyganowski is a partner with Otterbourg P.C. in New York and chairs its Bankruptcy practice. She joined the firm in 2008 after serving a full 14-year term as a U.S. Bankruptcy Judge for the Eastern District of New York and as its Chief Judge from 2005-08, and she now is a commercial and bankruptcy law litigator, mediator, arbitrator and expert witness. She also serves as a fiduciary (examiner, trustee, receiver, referee, monitor or special master) in bankruptcy and civil litigation. Judge Cyganowski is currently co-counsel to the Ad Hoc Committee in *Purdue Pharma*, and was appointed as a member of a blue-ribbon committee by the Rockville Center Diocese with former Chief Bankruptcy Judge Arthur Gonzalez and former Comptroller of the City of New York Harrison J. Goldin. Judge Cyganowski's fiduciary appointments include receiver in *SEC v. Platinum Partners*; CRO and temporary operator of Brooklyn's Interfaith Medical Center; patient care ombudsman in *Randolph Hospital Inc.*, *Promise Healthcare*, *Orianna Health Systems*, *21st Century Oncology* and *California Proton*; auditor of Capital One; and various trusteeships. She also served as special master in *Vivendi* and *Neogenix Oncology*, a court-appointed expert in Orion HealthCorp, and an arbitrator/mediator in cases including *Madoff* and *Lehman*. Judge Cyganowski has testified as an expert in international cases involving U.S. bankruptcy laws. She is a Fellow in the American College of Bankruptcy, sits on the editorial advisory board of the *Norton Journal of Bankruptcy Practice & Law*, and is an adjunct professor at St. John's University School of Law in the Bankruptcy LL.M. Program. She also is active in philanthropic organizations, including Tina's Wish, and *The National Law Journal* named her one of the nation's 75 "Outstanding Women Lawyers." Judge Cyganowski received her J.D. *magna cum laude* from the State University of New York at Buffalo School of Law in 1981.

Matthew Dundon is the principal of Dundon Advisers LLC in White Plains, N.Y., and founded the firm in 2016. He has been a global credit, litigation and distressed investment leader for more than 13 years, having served as research head at Miller Tabak Roberts Securities from 2006-10 and portfolio manager at Pine River Capital and Advent Capital from 2010-16, and has been involved in dozens of litigation-intensive investments and trading opportunities. Mr. Dundon was a corporate finance lawyer and analyst from 1998-2006. He received his B.A. from the University of California at Berkeley and his J.D. from the University of Chicago.

Paul Hinton is a principal with The Brattle Group, Inc. in New York and provides expert testimony and summary witness testimony in securities and finance litigation, enforcement matters involving trading abuse, and in cases involving alleged white collar crime. His recent white collar cases include allegations of insider trading, sanctions evasion, and investment fraud involving cryptocurrency and the tracing of ICO proceeds via blockchain transactions. Mr. Hinton regularly employs data analytics and network analysis in white-collar investigations to trace funds and to assess allegedly collusive communications. He also testifies in mass tort bankruptcies and litigation on the valuation and forecasting of tort claim liabilities. Mr. Hinton's prior professional experience includes project finance at London investment bank Morgan Grenfell. He received his B.A. in engineering science from Oxford University and his Master's in public policy from the Harvard Kennedy School of Government.

Chad J. Husnick is a partner in Kirkland & Ellis LLP's Restructuring Practice Group in Chicago and represents debtors, creditors, equity-holders and other stakeholders in all aspects of corporate liability management, restructuring, bankruptcy and insolvency proceedings. He has represented clients in a variety of industries, including energy, retail, real estate, infrastructure, manufacturing, transportation and distribution, hospitality and gaming, automotive and printing. Mr. Husnick regularly advises clients on corporate governance issues facing financially distressed companies, including liability management strategies, fiduciary duties and executive compensation. He has been recognized in the 2017–23 editions of *Chambers USA, America's Leading Lawyers for Business* and in the 2022-23 editions of *The Legal 500 U.S.* In addition, he was recognized as an "Outstanding Restructuring Lawyer – 2022" and an "Outstanding Young Restructuring Lawyer – 2017" by *Turnarounds & Workouts*. Mr. Husnick is a member of ABI's 2018 class of "40 Under 40," and he was named a "Dealmaker of the Year – 2016" by *The American Lawyer* for his role in the $40+ billion restructuring of Energy Future Holdings Corp. He is a Conferee in the National Bankruptcy Conference, a Fellow in the American College of Bankruptcy, and a member of ABI and the Turnaround Management Association. In addition, he is a lecturer in the law at the University of Chicago Law School and a contributing author for *Collier on Bankruptcy*. Mr. Husnick received his B.S. in 2001 in political science and behavioral science and law, with distinction, from the University of Wisconsin-Madison and his J.D. with honors in 2004 from the University of Chicago Law School.