

Finality Through Mootness: Protecting Capital Providers in Bankruptcy Cases¹

By: Ira L. Herman²

A. *Introduction*

Capital providers, whether they are buyers or lenders, are indispensable to the function of our bankruptcy system. Section 363(m)³ of the Bankruptcy Code⁴ protects a “good faith” buyer of property under Sections 363(b) or 363(c)⁵ of the Bankruptcy Code. Section 364(e)⁶ protects a “good faith” lender with respect to an extension of credit made under any of several sub-sections of Section 364 of the Bankruptcy Code. Sections 363(m) and 364(e) each operate to reward a party providing capital to a bankruptcy estate by limiting the ability of an aggrieved party to upset an approved transaction on appeal, once the non-debtor party has funded. Sections 363(m) and 364(c) of the Bankruptcy Code accomplish this through the doctrine known as “statutory mootness.”

Similarly, the courts have developed the doctrine of “equitable mootness” in bankruptcy cases to protect parties who have changed their position in reliance on a confirmed plan of reorganization, in the same way capital providers are protected by Section 363(m) and 364(e). Although Section 1129(a)(3) provides that a Chapter 11 plan of reorganization may not be confirmed unless “[t]he plan has been

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³ Section 363(m) of the Bankruptcy Code states:

The reversal or modification on appeal of an authorization under subsection (b) or (c) of this Section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

11 U.S.C. § 363(m) (2006).

⁴ 11 U.S.C. §§ 101-1330 (2006).

⁵ 11 U.S.C. § 363(b)-(c) (2006).

⁶ Section 364(e) of the Bankruptcy Code states:

The reversal or modification on appeal of an authorization under this Section to obtain credit or incur debt, or of a grant under this Section of a priority or a lien, does not affect the validity of any debt so incurred, or any priority or lien so granted, to an entity that extended such credit in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and the incurring of such debt, or the granting of such priority or lien, were stayed pending appeal.

11 U.S.C. § 364(e) (2006).

proposed in good faith,”⁷ the Bankruptcy Code does not contain a provision relating to a confirmed plan akin to the express protections provided to capital providers under Sections 363(m) and 364(e). Rather, such protections are found in the case law, as is more fully explored below. Thus, once a plan of reorganization is said to have been “substantially consummated,”⁸ and various parties have taken steps to implement it, the courts have acted to assure such parties that they will receive the benefit of their bargain by means of the judicially-crafted doctrine of “equitable mootness.”⁹

In the discussion that follows, we first examine the constitutional underpinnings and development of the equitable and statutory mootness doctrines. We then juxtapose constitutional, equitable and statutory mootness. Finally, the discussion focuses on the application of the equitable mootness and statutory mootness doctrines in bankruptcy cases, including the relevance and effect of concepts including good faith, substantial consummation, and the effect of obtaining or failing to obtain a stay pending appeal.

B. *Development of the Mootness Doctrine: From Cases and Controversies to Equitable and Statutory Mootness*

1. Constitutional Mootness

The mootness doctrine arises directly from the Article III Constitutional requirement that a “case or controversy” exist as a prerequisite to the exercise of jurisdiction over a matter by a federal court.¹⁰

⁷ 11 U.S.C. § 1129(a)(3). Courts construing Section 1129 have noted that the “requirement of good faith must be viewed in light of the totality of the circumstances surrounding establishment of a Chapter 11 plan, keeping in mind the purpose of the Bankruptcy Code is to give debtors a reasonable opportunity to make a fresh start.” *Mabey v. Sw. Power and Elec. Co. (In re Cajun Elec. Power Co-op., Inc.)*, 150 F.3d 503, 519 (5th Cir. 1998) (citing *Financial Sec. Assurance Inc. v. T-H New Orleans Ltd. P’ship (In re T-H New Orleans Ltd. P’ship)*, 116 F.3d 790, 802 (5th Cir. 1997)). See also *Jasik v. Conrad (In re Jasik)*, 727 F.2d 1379, 1383 (5th Cir. 1984) (“The ‘good faith’ of a reorganization plan must be ‘viewed in light of the totality of the circumstances surrounding confection’ of the plan.” (quoting *Public Fin. Corp. v. Freeman*, 712 F.2d 219, 221 (5th Cir. 1983)).

⁸ 11 U.S.C. § 1101(2) (2006).

⁹ *Mills v. Green*, 159 U.S. 651, 653 (1895).

¹⁰ U.S. CONST. art. III, § 2, cl.1. Clause 1 explains:

The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority;--to all Cases affecting Ambassadors, other public Ministers and Consuls;--to all Cases of admiralty and maritime Jurisdiction;--to Controversies to which the United States shall be a Party;--to Controversies between two or more States;--between a State and Citizens of another State;--between Citizens of different States;--between Citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.

Id.

The Supreme Court has articulated the essence of this doctrine in the case of *Mills v. Green*

The duty of this court, as of every other judicial tribunal, is to decide actual controversies by a judgment which can be carried into effect, and not to give opinions upon moot questions or abstract propositions, or to declare principles or rules of law which cannot affect the matter in issue in the case before it.¹¹

Under such doctrine, often referred to as “constitutional mootness” or “traditional mootness,” a case must be dismissed as moot when a court will be unable to provide effective relief to the litigants.¹² Thus, where there exists no “case or controversy” within the meaning of Article III of the Constitution, federal courts will not exercise their authority to adjudicate.¹³ Another way of stating the foregoing is that federal courts exercise their jurisdiction only to hear “live” controversies in order to avoid issuing advisory or academic opinions.¹⁴

2. *Equitable Mootness*

The constitutional mootness doctrine has been extended by the courts to encompass the situation where a “live” case is adjudicated by a trial court and events occurring during the pendency of a subsequent appeal make it impossible for the litigants to obtain effective relief. This extension of the mootness doctrine is known as “equitable mootness.” Thus,

It necessarily follows that when, pending an appeal from the judgment of a lower court, and without any fault of the defendant, an event occurs which renders it impossible for this court, if it should decide the case in favor of the plaintiff, to grant him any effectual relief whatever, the court will not proceed to a formal judgment, but will dismiss the appeal.¹⁵

¹¹ *Mills v. Green*, 159 U.S. at 653.

¹² *See Church of Scientology v. United States*, 506 U.S. 9, 12 (1992); *Murphy v. Hunt*, 455 U.S. 478, 481-82 (1982) (per curiam).

¹³ *See Honig v. Doe*, 484 U.S. 305, 317 (1988).

¹⁴ *Accord Trans World Airlines, Inc. v. Texaco, Inc. (In re Texaco, Inc.)*, 92 B.R. 38 (S.D.N.Y. 1988). The court in *In re Texaco* explained:

In the absence of a stay, events may have so progressed by the time a bankruptcy appeal is adjudicated that an appellate court is powerless to grant the appellant effective relief, thereby depriving that court of its constitutional jurisdiction over the matter. When such is the case, the appeal must, as a matter of law, be dismissed as moot.

Id. at 45.

¹⁵ *Mills v. Green*, 159 U.S. at 653.

In view of the foregoing, when events occur during the pendency of an appeal that make it impossible for the parties to obtain effective relief with respect to the underlying controversy, the appellate courts will vacate a trial court judgment and direct such trial court to dismiss a case as moot.¹⁶

Equitable mootness as developed by the federal courts is a doctrine distinct from constitutional mootness, although both concepts often are discussed in the same breath. In Chapter 11 cases, the courts have developed the mootness doctrine further and have forged it into a shield to be employed by reorganized debtors to prevent the disruption of their business and financial stability and to protect other parties in interest, who have relied on a confirmed plan of reorganization to govern their rights.¹⁷ As discussed below, equitable mootness involves case-specific equitable considerations that may result in an appeal of a confirmation order being dismissed as “moot,” notwithstanding the continued existence of an actual live “case or controversy.”¹⁸

The doctrine of equitable mootness has developed into a fundamental element of bankruptcy appellate jurisprudence. It remains rooted in its constitutional underpinnings, but it is applied far more liberally to prevent an inequitable outcome, notwithstanding the continued existence of a case or controversy.¹⁹

3. *Statutory Mootness*

In addition to the equitable mootness doctrine, as it is liberally applied in the bankruptcy context, Congress has chosen to codify the mootness concept in various Sections of the Bankruptcy Code to

¹⁶ 15 Laurence H. Tribe, *AMERICAN CONSTITUTIONAL LAW* § 82 (2d ed. 1988).

¹⁷ See Official Comm. of Unsecured Creditors of LTV Aerospace and Def. Co. v. Official Comm. of Unsecured Creditors of LTV Steel Co. (*In re Chateaugay Corp. I*), 988 F.2d 322, 325 (2d Cir. 1993); See, e.g., *In re UNR Indus.*, 20 F.3d 766, 769 (7th Cir. 1994) (“There is a big difference between inability to alter the outcome (real mootness) and unwillingness to alter the outcome (‘equitable mootness’).”); see also *MAC Panel Co. v. Va. Panel Corp.*, 283 F.3d 622, 625 (4th Cir. 2002) (“[E]quitable mootness is a pragmatic principle, grounded in the notion that, with the passage of time after a judgment in equity and implementation of that judgment, effective relief on appeal becomes impractical, imprudent, and therefore inequitable.” (emphasis omitted)); *In re Envirodyne Indus.*, 29 F.3d 301, 304 (7th Cir. 1994) (defining the doctrine as “merely an application of the age-old principle that in formulating equitable relief a court must consider the effects of the relief on innocent third parties.”).

¹⁸ See *Frito-Lay, Inc. v. LTV Steel Co., Inc. (In re Chateaugay Corp. II)*, 10 F.3d 944 (2d Cir. 1993).

¹⁹ *Deutsche Bank AG v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136 (2d Cir. 2005); *In re Adelphia Communications Corp.*, 333 B.R. 649 (S.D.N.Y. 2005) (“Pursuant to the doctrine, dismissal is appropriate when the appellant has made no effort to obtain a stay and has permitted such a comprehensive change of circumstances to occur as to render it inequitable for the appellate court to reach the merits of the appeal.”).

protect capital providers, i.e., purchasers and lenders acting pursuant to bankruptcy court orders.²⁰ This type of mootness is known as “statutory mootness.”

Statutory mootness presently resides in Sections 363(m) and 364(e) of the Bankruptcy Code.²¹ Bankruptcy Rule 8005,²² as derived from former Bankruptcy Rule 805, complements Sections 363(m) and 364(c),²³ and such Rule governs the process by which an aggrieved party may obtain a stay pending appeal of an order entered authorizing a sale or financing transaction to avoid the effects of such statutory mootness provisions.

Statutory mootness first found its way into bankruptcy law in the form of former Bankruptcy Rule 805, which stated in part

[u]nless an order approving a sale of property or issuance of a certificate of indebtedness is stayed pending appeal, the sale to a good faith purchaser of the issuance of a certificate to a good faith holder shall not be affected by the reversal or modification of such order on appeal, whether or not the purchaser or holder knows of the pendency of the appeal.²⁴

Pursuant to former Rule 805, appeals from a sale order entered by a Bankruptcy Referee became moot, if a party failed to obtain a stay pending appeal after a court approved the sale or lease in

²⁰ *Accord In re Vlasek*, 325 F.3d 955, 961 (7th Cir. 2003) (“The stay requirement bolsters third party purchaser reliance by ‘minimiz[ing] the chance that purchasers will be dragged into endless rounds of litigation to determine who has what rights in the property’ Thus, this Court and others have repeatedly held that an appeal of a bankruptcy sale is moot if the stay required by § 363(m) is not obtained.” (citations omitted)).

²¹ 11 U.S.C. § 363(m) (2006); 11 U.S.C. § 364(e) (2006).

²² Rule 8005 explains:

A motion for a stay of judgment, order, or decree of a bankruptcy judge, for approval of a supersedeas bond, or for other relief pending appeal must ordinarily be presented to the bankruptcy judge in the first instance. Notwithstanding Rule 7062 but subject to the power of the district court and the bankruptcy appellate panel reserved hereinafter, the bankruptcy judge may suspend or order the continuation of other proceedings in the case under the Code or make any other appropriate order during the pendency of an appeal on such terms as will protect the rights of all parties in interest. A motion for such relief, or for modification or termination of relief granted by a bankruptcy judge, may be made to the district court or the bankruptcy judge, may be made to the district court or the bankruptcy appellate panel, but the motion shall show why the relief, modification, or termination was not obtained from the bankruptcy judge. The district court or the bankruptcy appellate panel may condition the relief it grants under this Rule on the filing of a bond or other appropriate security with the bankruptcy court. When an appeal is taken by a trustee, a bond or other appropriate security may be required, but when an appeal is taken by the United States or an officer or agency thereof or by direction of any department of the Government of the United States a bond or other security shall not be required.

FED. R. BANKR. P. 8005.

²³ 11 U.S.C. §§ 363(m), 364(e) (2006).

²⁴ FED. R. BANKR. P. 805 (repealed 1978).

question.²⁵ The language of Rule 805, requiring a moving party to obtain a stay to avoid application of the mootness doctrine, was deleted from the current version of the rule, Bankruptcy Rule 8005.²⁶ Notwithstanding such omission, courts have continued to apply the mootness doctrine to sales and financing transactions, as if former Rule 805 had been included in the text of the Bankruptcy Code.²⁷

Bankruptcy Rule 8005 sets forth the procedures a moving party must follow to obtain a stay pending appeal to avoid application of the mootness doctrine.²⁸ Although all of the federal judicial circuits do not articulate identical criteria for application of the statutory mootness doctrine, the formulation cited in *In re Roth American, Inc.* is instructive in this regard.²⁹ In *Roth*, the court declared that under Rule 8005, “the standards for the issuance of a stay are: (1) Appellant is likely to succeed on the merits of the appeal; (2) Appellant will suffer irreparable injury; (3) No substantial harm will come to Appellee; (4) The stay will do no harm to the public interest.”³⁰ The *Roth* court further stated that “no one aspect will necessarily determine its outcome,” and that a bankruptcy court considering whether to issue a stay pending appeal should delicately balance all four elements.³¹

The underlying rationale for the requirement that a moving party obtain a stay pending appeal with regard to the effect of an order authorizing a sale or financing transaction in a bankruptcy case is to ensure finality.³² Stated succinctly, Congress recognized the need for parties to be able to proceed without concern that a reversal on appeal or collateral attack would allow for a loan or sales transaction

²⁵ *In re Info. Dialogic, Inc.*, 662 F.2d at 476-477.

²⁶ *First Mortgage Atrium Bldg., Ltd. v. Mut. Life Ins. Co. of N.Y.* (*In re First Mortgage Atrium Bldg., Ltd.*), 92 B.R. 202, 204 (E.D. Tex. 1988) (“Rule 805 . . . did not survive the 1983 changes to the Bankruptcy Rules.”). The court went on to explain:

Currently, the mootness Rule is partially codified at 11 U.S.C. § 363(m), a successor in some respects to Rule 805, but that provision applies only to sales by bankruptcy trustees. It does not apply to other foreclosure sales in bankruptcy proceedings, such as may occur when the bankruptcy court lifts the 11 U.S.C. § 362 Automatic Stay, allowing the creditor to foreclose its lien. Notwithstanding these partial codifications, therefore, the judicially-created mootness Rule is not limited to sales by trustees, but has broader application. The mootness Rule at issue here is non-statutory.

Id. (citations omitted).

²⁷ *Miami Center Ltd. P’ ship*, 838 F. 2d at 1550.

²⁸ FED. R. BANKR. P. 8005.

²⁹ *See In re Roth Am., Inc.*, 90 B.R. 94, 95 (Bankr. M.D. Pa. 1988).

³⁰ *Id.*

³¹ *Id.* (citing *In re Hotel Associates, Inc.*, 7 B.R. 130, 132 (Bankr. E.D. Pa. 1980)).

³² *In re Info. Dialogues, Inc.*, 662 F.2d at 477-78.

approved by a bankruptcy court to be unwound.³³ There is a need for finality, as purchasers and lenders providing capital that may be consumed by a bankruptcy estate will be more willing to act if they are assured that they will obtain bargained for consideration. Buyers require finality so that they can be certain they have irrevocably acquired property in consideration for the price paid. Lenders require finality so that they can be certain the bargained-for repayment terms for a loan (e.g., payment terms, collateral, covenants, etc.) are locked in place, once a transaction is funded.³⁴ Bankruptcy Code Sections 363(m) and 364(e), as complemented by Bankruptcy Rule 8005,³⁵ constitute the response to these policy and economic imperatives.³⁶

A strong competing public policy goal with the need for finality to protect capital providers is the policy of allowing an aggrieved party the opportunity to have an appellate court review a trial court order adversely affecting the interests of such party.³⁷ Cognizant of these competing interests, bankruptcy courts have held that the failure of a moving party to obtain a stay will not result in the *per se* disposition of all issues on mootness grounds, but rather only the provisions of an order governed by Sections 363(m) and 364(e).³⁸ Of course, in the right circumstances, a court may choose to issue a stay pending appeal to preserve the *status quo ante* and take a transaction out of the reach of the statutory mootness appellate bar.

C. Constitutional, Equitable and Statutory Mootness Distinguished

As discussed above, probably four related concepts of mootness exist in the bankruptcy litigation arena: constitutional mootness, general equitable mootness, bankruptcy-specific equitable mootness and

³³ *In re Vlasek*, 32 F.3d at 961.

³⁴ *See, e.g., Canzano v. Ragosa (In re Colarusso)*, 382 F.3d 51, 62 (1st Cir. 2004). The First Circuit explained:

While this case is a collateral attack rather than an appeal, the principle of finality embodied in § 363(m) still applies. This principle “reflects the salutary policy of affording finality of judgments approving sales in bankruptcy by protecting good faith purchasers, the innocent third parties who rely on the finality of bankruptcy judgments in making their offers and bids.”

Id. (citations omitted).

³⁵ FED. R. BANKR. P. 8005.

³⁶ *See In re Vlasek*, 325 F.3d at 961; *Boullioun Aircraft Holding Co. v. Smith Mgmt. (In re W. Pac. Airlines, Inc.)*, 181 F.3d 1191, 1195 (10th Cir. 1999) (“Such an interpretation stems from the language of § 364(e), as well as the purpose of this provision, which is to encourage lenders to advance funds to a bankrupt company in reliance on the unstayed order of [a] bankruptcy court, even if on appeal.”).

³⁷ *See Mission Iowa Wind Co., v. Enron Corp.*, 291 B.R. 39 (S.D.N.Y. 2003).

³⁸ *Id.*

statutory mootness. The Court in *Chamber of Commerce v. U.S. Dep't of Energy*³⁹ has described the two “cousins” of constitutional and equitable mootness as follows⁴⁰

[i]n its most basic sense, mootness concerns the jurisdictional limitations of Article III of the Constitution. According to that constitutional mandate, the existence of a “case or controversy” is a prerequisite for the exercise of federal judicial power; if a case is truly moot, the federal court is without the power to resolve the dispute [i.e., “constitutional mootness”]. The cousin of the mootness doctrine, in its strict Article III sense, is a melange of doctrines relating to the court’s discretion in matters of remedy and judicial administration [i.e., “equitable mootness”].⁴¹

The *Chamber* Court further distinguished equitable mootness from constitutional mootness as follows

[u]nlike Article III mootness, these doctrines address not the power to grant relief but the court’s discretion in the exercise of that power. In some circumstances, a controversy, not actually moot, is so attenuated that considerations of prudence and comity for coordinate branches of government counsel the court to stay its hand, and to withhold relief it has the power to grant.

This distinction between mootness proper and its remedial counterpart has been long recognized and clearly articulated. In *United States v. W.T. Grant Co.*..., the United States had brought an antitrust suit alleging the existence of interlocking corporate directorates. Before trial, certain board members resigned, disentangling the interlocks. On defendants’ motion, the district court dismissed the action as moot. Although affirming the judgment of the district court, the Supreme Court viewed the case in a different light:

Both sides agree to the abstract proposition that voluntary cessation of allegedly illegal conduct does not deprive the tribunal of power to hear and determine the case, i.e., does not make the case moot.... For to say that the case has become moot means that the defendant is entitled to a dismissal as a matter of right....

The case may nevertheless be moot if the defendant can demonstrate that “there is no reasonable expectation that the wrong will be repeated.” The burden is a heavy one.

Along with its power to hear the case, the court’s power to grant injunctive relief survives discontinuance of the illegal conduct. . . . But the moving party must satisfy the court that relief is needed. The necessary determination is that there exists some cognizable danger of recurrent violation, something more than the mere possibility which serves to keep the case alive.⁴²

³⁹ 627 F.2d 289, 291 (D.C. Cir. 1980).

⁴⁰ *Id.*

⁴¹ *Id.* If constitutional and equitable mootness are cousins, it would probably be correct to say that equitable and statutory mootness are siblings.

⁴² *Id.* at 291-92 (citations omitted).

Additionally, the Fifth Circuit instructs that

[e]quitable mootness is not an Article III inquiry as to whether a live controversy is presented; rather, it is a recognition by the appellate courts that there is a point beyond which they cannot order fundamental changes in reorganization actions. Consequently, a reviewing court may decline to consider the merits of a confirmation order when there has been substantial consummation of the plan such that effective judicial relief is no longer available—even though there may still be a viable dispute between the parties on appeal.⁴³

In bankruptcy cases, the courts have come to examine three factors when called upon to consider a claim of equitable mootness: (i) whether a stay was granted, (ii) whether the plan was substantially consummated, and (iii) whether relief requested would affect the rights of parties not before the court or the plan's success.⁴⁴ Accordingly, the three-pronged test for equitable mootness in the Chapter 11 context is designed to reflect a court's concern for determining "the proper balance between the equitable considerations of finality and good faith reliance on a judgment and the competing interests that underlie the right of a party to seek review of a bankruptcy order adversely affecting him."⁴⁵

Bankruptcy equitable mootness addresses "the parties' reliance upon a substantially consummated plan of reorganization and the point at which modification of that plan would unduly impact innocent third parties."⁴⁶ Therefore, courts have reasoned that reversing a plan's confirmation might knock the "props out from under intricate and involved transactions, the consummation of which is relied on in the marketplace."⁴⁷ This explanation supports the public interest served by the doctrine of equitable mootness: "facilitat[ing] the important public policy favoring orderly reorganizations and settlement of debtor estates by affording finality to the judgments of the bankruptcy court."⁴⁸

⁴³ *In re GWI PCS I, Inc.*, 230 F.3d 788, 800 (5th Cir. 2000) (quoting *Manges v. Seattle-First Nat'l Bank (In re Manges)*, 29 F.3d 1034, 1038-39 (5th Cir. 1994) (internal citations omitted)).

⁴⁴ *Id.*

⁴⁵ *In re Manges*, 29 F.3d at 1039 (quoting *First Union Real Estate Equity and Mortgage Inv. v. Club Assoc. (In re Club Assoc.)*, 956 F.2d 1065, 1069 (1992)).

⁴⁶ *In re Milk Palace Dairy, LLC*, 327 B.R. 462 (B.A.P. 10th Cir. 2005).

⁴⁷ *United Artists Theatre Co. v. Walton*, 315 F.3d 217 (3rd Cir. 2003).

⁴⁸ *In re Manges*, 29 F.3d at 1038 n.6 (quoting *Rochman v. Ne. Util. Serv. Group (In re Public Serv. Co.)*, 963 F.2d 469, 471-72 (1st Cir.) (1992) (citation omitted)).

Accordingly, courts have used “equitable mootness” to protect parties who have acted in reliance on the terms of a confirmed reorganization plan.⁴⁹

Bankruptcy courts have taken the equitable mootness doctrine and essentially molded it into an equitable remedy to support judicial efficiency and fairness to the parties. Clearly, courts making an equitable mootness inquiry focus their attention on notions of equity and fairness, rather than on the “case or controversy” requirement associated with traditional mootness, and even equitable mootness in the context of general litigation matters. In the bankruptcy context, courts employ equitable mootness because “equitable principles of jurisprudence may dictate that a case be dismissed as moot even though a court may properly exercise its article III jurisdiction” (i.e., even when a “case or controversy” remains).⁵⁰ Consequently, at least one court has characterized “equitable mootness” in the bankruptcy litigation arena as a misnomer stating that “there is nothing equitable about the equitable mootness doctrine.... The matter is moot out of necessity, not application of equitable principles.... [T]he doctrine is more accurately denominated as ‘prudential mootness.’”⁵¹ No matter the moniker employed, the common thread is that courts in the bankruptcy context will apply equitable mootness when principles of fairness dictate that it is necessary to do so.⁵²

⁴⁹ Nordhoff Invs., Inc. v. Zenith Elecs. Corp., 258 F.3d 180, 185 (3rd Cir. 2001) (“[T]he equitable mootness doctrine prevents a court from unscrambling complex bankruptcy reorganizations when the appealing party should have acted before the plan became extremely difficult to retract.”); *In re PWS Holding Corp.*, 228 F.3d 224, 235-36 (3rd Cir. 2000) (“Under the doctrine of equitable mootness, an appeal should be dismissed, even if the court has jurisdiction and could fashion relief, if the implementation of that relief would be inequitable.”); *see also* Mac Panel Co. v. Virginia Panel Corp., 283 F.3d 622 (4th Cir. 2002).

Unlike the constitutional doctrine of mootness, which bars consideration of appeals because no Article III case or controversy remains, the doctrine of equitable mootness is a pragmatic principle, grounded in the notion that, with the passage of time after a judgment in equity and implementation of that judgment, effective relief on appeal becomes impractical, imprudent, and therefore inequitable. Applied principally in bankruptcy proceedings because of the equitable nature of bankruptcy judgments, equitable mootness is often invoked when it becomes impractical and imprudent to upset the plan of reorganization at this late date.

Id. (internal citations omitted).

⁵⁰ *In re Texaco*, 92 B.R. at 45.

⁵¹ *Griffin v. Box Brothers Holding Co. (In re Box Brothers Holding Co.)*, 194 B.R. 32, 45 (Bankr. D. Del. 1996).

⁵² Fairness, however, as the court in *Griffin* explained, is subjective:

From the vantage point of the disappointed creditor, there is nothing equitable about the equitable mootness doctrine. Invocation of the doctrine precludes merits review even if the bankruptcy court resolution was erroneous. This result occurs when the occurrence of facts and events in the commercial world cause a court to be unable to grant meaningful relief.

Id.

The doctrine of equitable mootness allows a reviewing court to “decline to consider the merits of a confirmation order when there has been substantial consummation of the plan such that effective judicial relief is no longer available – even though there may still be a viable dispute between the parties on appeal.”⁵³ Thus it has been said that

[i]f an event occurs while a case is pending on appeal that makes it impossible for the court to grant any effectual relief to a prevailing party, the appeal must be dismissed.... Within the bankruptcy context, an appeal should also be dismissed as moot when, even though effective relief could conceivably be fashioned, implementation of that relief would be inequitable.⁵⁴

Indeed, the Appellate Court in the *In re Continental Airlines* case administered in the District of Delaware stated that the importance of “allowing approved reorganizations to go forward in reliance on bankruptcy court confirmation orders may be the central animating force behind the equitable mootness doctrine.”⁵⁵ In this context, equitable mootness “is a recognition by the appellate courts that there is a point beyond which they cannot order fundamental changes in reorganization actions.”⁵⁶ Although the doctrine most often is applied in consideration of an appeal from a confirmation order, “it applies with equal force to actions brought to revoke a plan of reorganization.”⁵⁷

In light of the importance of finality in the Chapter 11 context, courts have recognized that “confirmation plans eventually reach a point of completion where to reverse the confirmation order” would be inequitable.⁵⁸ Furthermore, if the revocation of a plan of reorganization would adversely effect

⁵³ *In re Manges*, 29 F.3d at 1039 (5th Cir. 1994); see also *Salsberg v. Trico Marine Serv., Inc. (In re Trico Marine Serv., Inc.)*, 337 B.R. 811, 814 (Bankr. S.D.N.Y. 2006) (“a proceeding challenging a confirmation order should be dismissed as moot when, although relief could conceivably be fashioned, the implementation of the relief would be inequitable.”) (internal cites omitted); *Almeroth v. Innovative Clinical Solutions, Ltd. (In re Innovative Clinical Solutions, Ltd.)*, 302 B.R. 136, 141 (Bankr. D. Del. 2003) (Under th[e] widely recognized and accepted doctrine [of equitable mootness], the courts have held that [an action] should be dismissed as moot when, even though effective relief could conceivably be fashioned, implementation of that relief would be inequitable.”); *S&N Phelps and Co. v. Circle K Corp. (In re Circle K Corp.)*, 171 B.R. 666, 670 (Bankr. D. Ariz. 1994) (“The Court concludes that although plaintiffs timely filed their complaint, the confirmation process has sufficiently advanced that effective relief cannot be fashioned, even if plaintiffs prevail. [Thus] [t]he motion to dismiss is granted.”).

⁵⁴ *Frito Lay, Inc. v. LTV Steel Co. (In re Chateaugay Corp.)*, 10 F.3d 944, 949-50 (2d Cir. 1993).

⁵⁵ *In re Continental Airlines*, 91 F.3d 563, 565 (3d Cir. 1996).

⁵⁶ *In re Manges*, 29 F.3d at 1039; see also *Tor Husjord Shipping v. Port Isabel/San Benito Navigation Dist. (In re Burton Securities S.A.)*, 202 B.R. 411, 416 (S.D. Tex. 1996).

⁵⁷ *In re Innovative Clinical Solutions*, 302 B.R. at 141 (citing *In re Circle K Corp.*, 171 B.R. at 669 (“the doctrine of mootness does apply in Section 1144 cases if . . . no effective relief can be fashioned”)) (citing *Chang v. Servico, Inc. (In re Servico, Inc.)*, 161 B.R. 297, 300-301 (S.D. Fla. 1993)).

⁵⁸ *In re Servico, Inc.*, 161 B.R. at 301 (quoting *Miami Center Ltd. P’ship*, 838 F.2d at 1555).

the success of the plan and the rights of parties not before the court, even though an actual case or controversy may exist, the court will likely rule for equitable mootness, basing such outcome on equitable principles. The Fifth Circuit has explained that “it is the reliance interests engendered by the plan, coupled with the difficulty of reversing critical transactions, that counsels against attempts to unwind things.”⁵⁹

D. *Equitable Mootness and the Substantial Consummation Trigger*

Section 1129(a)(3) of the Bankruptcy Code provides that a court shall confirm a plan only if, *inter alia*, the “plan has been proposed in good faith.”⁶⁰ Neither Section 1129(a)(3), nor any other provision of the Bankruptcy Code, however, defines “good faith.”⁶¹ Courts have struggled to interpret this seemingly simple concept. The consensus is that the requisite good faith determination is based on the totality of the circumstances.⁶²

It is important to note that insolvency is not a prerequisite to a finding of good faith under Section 1129(a).⁶³ Also, the mere fact that a creditor’s contractual rights are adversely affected does not automatically net a bad faith finding by the court. Courts have recognized that in “enacting the Bankruptcy Code, Congress made a determination that an eligible debtor should have the opportunity to avail itself of a number of Code provisions that adversely alter creditors’ contractual and nonbankruptcy rights.... Thus, the fact that a debtor proposes a plan in which it avails itself of an applicable Code provision does not constitute evidence of bad faith.”⁶⁴

Sound strategy for a party aggrieved by entry of a confirmation order supports seeking a stay of the effect of such order, although imposition of a stay is not specifically required by the Bankruptcy Code

⁵⁹ *In re Manges*, 29 F.3d at 1040.

⁶⁰ 11 U.S.C. § 1129(a).

⁶¹ See *In re Madison Hotel Assocs.*, 749 F.2d 410, 425 (7th Cir. 1994).

⁶² *Id.* (“[F]or purposes of determining good faith under Section 1129(a)(3) . . . the important point of inquiry is the plan itself and whether such plan will fairly achieve a result consistent with the objectives and purposes of the Bankruptcy Code.”); see also *Platinum Capital, Inc. v. Sylmar Plaza, L.P. (In re Sylmar Plaza, L.P.)*, 314 F.3d 1070 (9th Cir. 2002) (“A plan is proposed in good faith where it achieves a result consistent with the objectives and purposes of the Code.” (citing *Ryan v. Loui (In re Corey)*, 892 F.2d 829, 835 (9th Cir. 1989))); *Stolrow v. Stolrow’s, Inc. (In re Stolrow’s, Inc.)*, 84 B.R. 167, 172 (B.A.P. 9th Cir.1988).

⁶³ 11 U.S.C. § 1129(a).

⁶⁴ *In re PPI Enters., Inc.*, 228 B.R. 339, 344-45, 347 (Bankr. D. Del. 1998) (citation omitted).

or Bankruptcy Rules as a prerequisite to judicial review of such order. The case law in the Southern District of New York and Second Circuit, among other courts, dictates that the “failure to seek a stay of a confirmation order may render an appeal moot as a result of constitutional⁶⁵ and equitable considerations.”⁶⁶

What event will trigger application of the equitable mootness doctrine with regard to a confirmed reorganization plan? Where a plan has been substantially consummated, there is a “‘strong presumption’ that appellants’ challenges have been rendered moot due to their inability or unwillingness to seek a stay.”⁶⁷ “The primary purpose of the equitable mootness doctrine is to encourage finality....”⁶⁸ Thus, “substantial consummation of a plan of reorganization raises the ‘strong presumption’ that an appellate court will not be able to fashion an equitable and effective remedy.”⁶⁹ While prudential factors considered by a bankruptcy appellate court in deciding whether an appeal is equitably moot are given varying weight depending upon the particular circumstances of the case, “the foremost consideration is whether the reorganization plan has been substantially consummated.”⁷⁰ Under the Bankruptcy Code, a

⁶⁵ Constitutional considerations in the mootness analysis continue to be relevant concerns. See *In re Servico, Inc.*, 161 B.R. at 300 (citing *Miami Center Ltd. P’ship*, 838 F.2d at 1553-56. The court in *In re Servico, Inc.* reasoned:

The constitutional principle of mootness retains its vitality in the context of a bankruptcy appeal. It is appropriate for a court to dismiss a bankruptcy appeal when the reorganization plan has been substantially consummated and it has become legally and practically impossible to unwind the consummation of the plan or otherwise to restore the status quo before the confirmation.

Id. (citations and quotations omitted).

⁶⁶ *Id.*; *In re Texaco*, 92 B.R. at 44-45 (“It may be incumbent upon a party appealing a bankruptcy court’s ruling to seek a stay lest the appeal in question be rendered moot by constitutional or related equitable/jurisprudential considerations”); *In re Revere Copper & Brass Inc.*, 78 B.R. at 23 (“It is obligatory upon an appellant from a confirmation order to pursue with diligence all available remedies to obtain a stay of the implementation of that order prior to the occurrence of comprehensive changes made in reliance on the unstayed order”) (citations and quotations omitted). Other circuits also employ such rationale: see *Hoese Corp. v. Vetter Corp.* (*In re Vetter Corp.*), 724 F.2d 52, 55-56 (7th Cir. 1983); see also *Sulmeyer v. Karbach Enter.* (*In re Exennium, Inc.*), 715 F.2d 1401, 1403-04 (9th Cir. 1983), *Tompkins v. Frey* (*In re Bel Air Assoc., Ltd.*), 634 F.2d 1383, 1389-90 (5th Cir. 1981).

⁶⁷ *Resolution Trust Corp. v. Best Prods., Co.* (*In re Best Prods. Co.*), 177 B.R. 791, 803 (S.D.N.Y. 1995) (quoting *In re Texaco, Inc.*, 92 B.R. 38, 46 (S.D.N.Y. 1988)).

⁶⁸ *Deloitte and Touche, LLP v. Aquila Biopharmaceuticals, Inc.* (*In re Cambridge Biotech Corp.*), 214 B.R. 429, 431 (D. Mass. 1997) (citing *Anheuser Busch, Inc. v. Miller* (*In re Stadium Mgmt. Corp.*), 895 F.2d 845, 848 (1st Cir. 1990)).

⁶⁹ *In re Cambridge Biotech Corp.*, 214 B.R. at 431 (citing *Public Serv. Co. of N.H. v. Ne. Util. Serv. Group* (*In re Public Service Co. of N.H.*), 963 F.2d, 469, 474 n. 13; see *Met. Life. Ins. Co. v. Olsen* (*In re Olsen*), 861 F.2d 188, 190 (8th Cir. 1988) (stating that once a plan is substantially consummated, neither the parties nor the bankruptcy court can make changes to the confirmed plan).

⁷⁰ *In re PWS Holding Corp.*, 228 F.3d at 236 (stating that prudential concerns include “whether the plan has been substantially consummated or stayed, whether the requested relief would affect the rights of other parties, whether the requested relief would affect the success of the plan, and whether it would further the public policy of affording finality to bankruptcy judgments.”).

bankruptcy court's "power to modify a plan of reorganization extends only from confirmation to substantial consummation."⁷¹

The Bankruptcy Code defines substantial consummation as:

- (a) transfer of all or substantially all of the property proposed by the plan to be transferred;
- (b) assumption by the debtor or by the successor to the debtor under the plan of the business or of the management of all or substantially all of the property dealt with by the plan; and
- (c) commencement of distributions under the plan.⁷²

Substantial consummation, however, need not be absolute or complete consummation of the plan of reorganization; it is merely used as a "yardstick" for deciding when an appeal from the bankruptcy court's plan confirmation order should be dismissed as equitably moot.⁷³

The substantial consummation inquiry is important as it allows the Court to determine when the finality of a confirmation order implicates the reliance interest of third parties concerning the finality of a reorganization plan.⁷⁴ Courts have found there is a point of no return beyond which the courts cannot equitably order fundamental changes in a reorganization case. Thus, where a reorganization plan has been substantially consummated, even though there may still exist a live dispute between the parties, a court typically will invoke the equitable mootness doctrine and decline to consider an appeal.⁷⁵ Conversely, where effective relief is possible without upsetting the terms of a confirmed reorganization plan, even if substantially consummated, equitable mootness will not serve to bar appellate review.⁷⁶

⁷¹ See 11 U.S.C. § 1127(b) (allowing proponent of the plan or the reorganized debtor to modify any time after confirmation and before substantial consummation); *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) ("[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.").

⁷² 11 U.S.C. § 1101(2) (2006).

⁷³ *In re GWI PCS I, Inc.*, 230 F.3d 788, 801 (5th Cir. 2000) ("We have adopted the 'substantial consummation' yardstick because it informs our judgment as to when finality concerns and the reliance interests of third parties upon the plan as effectuated have become paramount to a resolution of the dispute between the parties on appeal.") (citation omitted); see also *Kearns v. Vineyard Bay Dev. Co. (In re Vineyard Bay Dev. Co.)*, 132 F.3d 269, 271 (5th Cir. 1998) (noting that the Fifth Circuit interprets the equitable mootness doctrine to be "prudential rather than jurisdictional.").

⁷⁴ *Id.*

⁷⁵ *Id.*

⁷⁶ See *Spirtos v. Moreno (In re Spirtos)*, 992 F.2d 1004, 1007 (9th Cir. 1993).

The key to the inquiry is reliance. When third parties detrimentally rely on a confirmed plan, a court must treat the interests of such third parties as paramount to the resolution of the dispute on appeal.⁷⁷ “This presumption is undergirded by the common sense notion that the piecemeal dismantling of the [r]eorganization [p]lan in subsequent appeals of individual transactions is, in practical terms if nothing else, a virtually impossible task.”⁷⁸

The principal way to avoid substantial consummation and the likelihood that an aggrieved party’s appeal will be dismissed as moot, as set forth above, is to obtain a stay pending appeal under Bankruptcy Rule 8005. Yet, just as the failure to obtain a stay does not result in a *per se* dismissal, substantial consummation of a reorganization plan does not automatically render it “impossible or inequitable for an appellate court to grant effective relief.”⁷⁹ Accordingly, the Second Circuit has stated that it considers whether the following constitutional and equitable considerations exist, and if all exist, “substantial consummation will not moot an appeal”:

- (a) whether the court can still order some effective relief;
- (b) whether such relief will not affect the re-emergence of the debtor as a revitalized corporate entity;
- (c) whether such relief will not unravel intricate transactions so as to knock the props out from under the authorization for every transaction that has taken place and create an unmanageable, uncontrollable situation for the Bankruptcy Court;

⁷⁷ *In re Manges*, 29 F.3d at 1041 (explaining that in the context of a bankruptcy proceeding, equitable mootness is not an Article III inquiry as to whether live controversy is presented, but, rather, it is a recognition by appellate courts that there is point beyond which they cannot order fundamental changes in reorganization actions. Accordingly, a reviewing court may decline to consider the merits of a confirmation order when there has been substantial consummation of the plan such that effective judicial relief is no longer available, even though there may still be viable dispute between parties on appeal. Therefore, the concept of “mootness”, from a prudential standpoint, protects the interests of third parties who have acted upon the plan as confirmed.)

⁷⁸ *In re Texaco, Inc.*, 92 B.R. at 46 (quoting *In re AOV Indus., Inc.*, 792 F.2d 1140, 1149 (D.C. Cir. 1986) (citations omitted). The Court also noted that:

Even when the moving party is not entitled to dismissal on [A]rticle III grounds, common sense or equitable considerations may justify a decision not to decide a case on the merits. . . . Determinations of mootness in this latter sense cannot be cabined by inflexible, formalistic rules, but instead require a case-by-case judgment regarding, the feasibility or futility of effective relief should a litigant prevail.

Id. at 1147-48 (citations omitted); *see also* *Lawrence v. Revere Copper and Brass, Inc.* (*In re Revere Copper & Brass Inc.*), 78 B.R. 17, 21 (S.D.N.Y. 1987) (“[P]olicy reasons underlying the mootness doctrine is [sic] simply that where substantial elements of the reorganization plan have been implemented in the absence of a stay, any appeal of the confirmation order is moot because it is very doubtful that effective relief could be afforded.”) (internal quotations omitted).

⁷⁹ *In re Best Prods. Co.*, 177 B.R. at 803 (citations omitted); *see also In re Texaco, Inc.*, 92 B.R. at 46-47 (“Substantial consummation in the absence of a stay, however, does not automatically discharge this court of its appellate jurisdiction. We remain bound to scrutinize each individual claim, testing the feasibility of granting the relief against its potential impact on the reorganization scheme as a whole.”).

- (d) whether the parties who would be adversely affected by the modification have notice of the appeal and an opportunity to participate in the proceedings; and
- (e) whether the appellant pursued with diligence all available remedies to obtain a stay of execution of the objectionable order . . . if the failure to do so creates a situation rendering it inequitable to reverse the orders appealed from.⁸⁰

E. *Statutory Mootness and the “Good Faith” Trigger*

1. *Section 363(m) and “Good Faith” Purchaser Defined*

Courts generally apply the same principles of fairness interpreting the statutory mootness provisions of Section 363 and 364 of the Bankruptcy Code. Bankruptcy Code Section 363(m), governing the good faith purchase of assets, provides

the reversal or modification on appeal of an authorization under subsection (b) or (c) of this Section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in *good faith*, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale were stayed pending appeal.⁸¹

The purpose of this Bankruptcy Code Section appears to be twofold. First, it works to bring finality to the sale process under the Bankruptcy Code, and it permits a buyer at a bankruptcy sale to be unconcerned with a reversal on appeal, months or years after a closing. Such finality enhances value and facilitates an orderly sale process.⁸² Second, Section 363(m), which protects buyers where a sale has been conducted in good faith, along with 363(n), which prohibits collusive bidding, serve to enhance value and to protect the integrity of the sale process in Title 11 cases.

Most courts consider the totality of the circumstances with regard to good faith in the sale context, and have found that the term “good faith purchaser” means a party who acquires property (a) in good faith, (b) for value, and (c) without knowledge of adverse claims.⁸³ A party may be a good faith

⁸⁰ *In re Chateaugay Corp.*, 10 F.3d at 952-53.

⁸¹ 11 U.S.C. § 363(m) (2006) (emphasis added).

⁸² *In re Vlasek*, 325 F.3d at 961. The Court stated:

The ability to appeal immediately these validity-of-sale decisions benefits both the debtor’s estate and creditors. The uncertainty that would be fostered by a lack of timely review would undoubtedly lower the market price for estate assets, resulting in diminished creditor restitution per asset and necessitating the liquidation of more estate assets to cover the same amount of creditor claims.

Id. (citation omitted).

⁸³ *T.C. Investors v. Joseph (In re M Capital Corp.)*, 290 B.R. 743, 746 (B.A.P. 9th Cir. 2003); *see, e.g. Licensing by Paulo, Inc. v. Sinatra (In re Gucci)*, 126 F.3d 380, 390 (2d Cir. 1997); *Badami v. Burgess (In re Burgess)*, 246 B.R. 352 (B.A.P. 8th Cir. 2000).

purchaser under Section 363(m), regardless of whether such party has knowledge that a sale may have been procedurally defective.⁸⁴ The issue of a buyer’s “good faith” status is a mixed question of law and fact.⁸⁵

The conduct of the buyer prior to and throughout the sales process is germane to the good faith inquiry.⁸⁶ “Typically, misconduct that would destroy a purchaser’s ‘good faith’ status involves fraud, collusion between the purchaser and other bidders or the trustee [or DIP], or an attempt to take grossly unfair advantage of other bidders.”⁸⁷ At least one court has stated that the conduct must be “extremely egregious” to destroy the good faith status of a buyer.⁸⁸ Although the burden of proof regarding good faith does not appear to be too rigorous, appellate courts will not presume a purchaser’s good faith; the burden of proof falls on the proponents of the sale to present evidence to the trial court to support a finding of good faith and to obtain a specific finding of good faith in the sale or lease order.⁸⁹

Clearly, the purchaser is the focus of the good faith inquiry. However, it appears that the question of the purchaser’s good faith actually in many instances turns on the trustee’s or debtor-in-possession’s conduct in connection with a transaction.⁹⁰ Among the types of conduct found to effect good faith purchaser status are the failure to disclose certain material terms of the purchase, secret or undisclosed “side deals” between seller’s management and the purchaser, and the manipulation of information so that a favored bidder is privy to information not generally available to all other bidders.⁹¹ Unless an aggrieved party obtains a stay of a sale order, the appeal of the sale or lease of a debtor’s property likely will be

⁸⁴ *In re Cable One CATV*, 169 B.R. 488 (Bankr. D. N.H. 1994).

⁸⁵ *In re Gucci*, 126 F.3d at 390; *Mark Bell Furniture Warehouse, Inc. v. D. M. Reid Assocs., Ltd. (In re Mark Bell Furniture Warehouse, Inc.)*, 992 F.2d 7, 8 (1st Cir. 1993).

⁸⁶ *In re Abbotts Dairies of Pa., Inc.*, 788 F.2d 143, 147 (3rd Cir. 1986); *see also, In re Gucci*, 126 F.3d at 390-393; *Ferrari N. Am., Inc. v. Sims (In re R.B.B. Inc.)*, 211 F.3d 475 (9th Cir. 2000) (where the identity of the buyer is ambiguous, the bankruptcy court was precluded from making the “good faith purchaser” finding).

⁸⁷ *In re Abbotts Dairies of Pa. Inc.*, 788 F.2d at 147; *See also Paulman v. Gateway Venture Partners III, L.P. (In re Filtercorp, Inc.)*, 163 F.3d 570, 577 (9th Cir. 1998).

⁸⁸ S. Rep. No. 989, 95th Cong., 2d Sess. 57, July 14, 1978, reprinted in 1978 U.S.C.C.A.N. 5787, 5843.

⁸⁹ *In re Abbotts Dairies of Pa. Inc.*, 788 F.2d at 143; *see In re M Capital Corp.*, 290 B.R. at 746.

⁹⁰ *See, e.g., Crowder v. Given (In re Crowder)*, 314 B.R. 445 (B.A.P. 10th Cir. 2004).

⁹¹ *See, e.g., In re Abbotts Dairies of Pa., Inc.*, 788 F.2d at 148-49 (managed “emergencies” and managed information evident to taint the sale process); *but see In re Sasson Jeans, Inc.*, 90 B.R. 608 (S.D.N.Y. 1988) (purchaser as creditor does not impair good faith status).

dismissed as moot, if the following requirements are met: (a) the court has entered an order authorizing the sale or lease of a debtor's property, and (b) a good faith purchaser bought or leased the property for value. Thus, Section 363(b) and 363(c) transactions are treated much like those subject to equitable mootness in the term of analysis employed by the courts and may be insulated from reversal or modification on appeal, unless the effect or the sale order, and the closing of the sale transaction contemplated by the sale order, are stayed pending appeal. Perhaps the Second Circuit said it best when it cautioned, "The party who appeals without seeking to avail himself of [the protections afforded by Bankruptcy Rule 8005] does so at his own risk."⁹²

2. Section 364(e) and "Good Faith" Lender Defined

Section 364(e) provides that:

The reversal or modification on appeal of an authorization under this Section to obtain credit or to incur debt, or of a grant under this Section of a priority or a lien, does not affect the validity of any debt so incurred, or any priority or lien so granted, to an entity that extended such credit in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and the incurring of such debt, or granting of such priority or lien, were stayed pending appeal.⁹³

"Good faith" also is not defined in the Bankruptcy Code with reference to loan transactions. Courts generally have found a party to be a good faith lender under Section 364(e)⁹⁴ using a totality of the circumstances analysis similar to the analysis employed by courts when the inquiry is good faith purchaser status under Section 363(m).⁹⁵ "The requirement that a purchaser act in good faith speaks to the integrity of his conduct in the course of the sale proceedings."⁹⁶ Conduct that will vitiate good faith

⁹² Deutsche Bank AG v. Metromedia Fiber Network, Inc. (*In re Metromedia Fiber Network, Inc.*), 416 F.3d 136, 145 (2d Cir. 2005) (citing *Chateaugay I*, 988 F.2d at 326); *see also, e.g.*, Aetna Cas. & Sur. Co. v. LTV Steel Co. (*In re Chateaugay Corp.*), 94 F.3d 772, 776 (2d Cir. 1996) (reasoning that it is "inequitable or impractical to grant relief after substantial consummation," unless, among other things, "the entity seeking relief has diligently pursued a stay of execution of the plan throughout the proceedings"); *Retired Pilots Ass'n of U.S. Airways, Inc. v. U.S. Airways Group, Inc.* (*In re U.S. Airways Group, Inc.*), 369 F.3d 806, 810 (4th Cir. 2004) (failure to seek a stay or expedited appeal "weighs strongly in favor of a finding of equitable mootness"); *In re Texaco, Inc.*, 92 B.R. at 46 ("[T]here fairly exists a strong presumption that appellants' challenges have been rendered moot due to their inability or unwillingness to seek a stay." (quotation omitted)).

⁹³ 11 U.S.C. § 364(e).

⁹⁴ *See, e.g.*, *Cinicola v. Scharffenberger*, 248 F.3d 110, 124-26 (3rd Cir. 2001); 11 U.S.C. § 364(e).

⁹⁵ *Id.* at 128; 11 U.S.C. § 363(m).

⁹⁶ *In re Abbotts Dairies of Pa., Inc.*, 788 F. 2d at 147.

lender status includes fraud, collusion between lender and debtor or trustee for an improper purpose, or an attempt to take or acquire unfair advantage.⁹⁷

Section 364(e) of the Bankruptcy Code is crafted to protect a lender extending credit to a debtor-in-possession or trustee, pending an appeal of a Bankruptcy Court order authorizing such a loan transaction, similar to the protection offered to sale orders by Section 363(m).⁹⁸ Just as buyers are afforded finality under 363(m), lenders are accorded finality under 363(e) to encourage them to extend credit to debtors-in-possession and trustees.⁹⁹

An appeal of a financing order entered under Section 364 will be dismissed as moot, pursuant to Section 364(e), if (i) the extension of credit is authorized by the presiding Bankruptcy Court, and (ii) the creditor is a “good faith lender.”¹⁰⁰ A creditor can be a good faith lender under Section 364(e) regardless of its knowledge of a pending appeal.¹⁰¹ Thus, the undefined element of good faith can essentially make or break an appeal for equitable mootness purposes.

F. Conclusion

The statutory mootness doctrine codified in Sections 363(m) and 364(e) of the Bankruptcy Code and equitable mootness as it applies to bankruptcy cases are powerful tools used by bankruptcy courts to ensure that debtors-in-possession and trustees are able to efficiently dispose of assets and obtain needed credit.¹⁰² These bankruptcy-specific concepts should not be confused with the “case or controversy” requirement of constitutional mootness or the equitable mootness principle as it applies to general

⁹⁷ *Id.*

⁹⁸ 11 U.S.C. § 364(e); 11 U.S.C. § 363(m).

⁹⁹ *Id.*

¹⁰⁰ 11 U.S.C. § 364(e); 11 U.S.C. § 363(m).

¹⁰¹ *Cinicola*, 248 F.3d at 122. The Court states:

The reversal or modification on appeal of an authorization . . . of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, *whether or not such entity knew of the pendency of the appeal*, unless such authorization and such sale or lease were stayed pending appeal.

Id. (emphasis added); 11 U.S.C. § 363(m).

¹⁰² *In re Envirodyne Indus., Inc.*, 29 F.3d 301, 304 (7th Cir.1994) (defining the doctrine of equitable mootness as “merely an application of the age-old principle that in formulating equitable relief a court must consider the effects of the relief on innocent third parties”).

litigation cases.¹⁰³ Debtors-in-possession and trustees on one hand, and capital providers, be they buyers or lenders, on the other, should be prepared to adduce the necessary evidence to support a good faith finding under the totality of the circumstances to obtain the benefits afforded by Sections 363(m) or 364(e), i.e., finality.

¹⁰³ *In re Metromedia Fiber Network, Inc.*, 416 F.3d at 144 (“There is a big difference between inability to alter the outcome (real mootness) and unwillingness to alter the outcome (‘equitable mootness’).”) (citation and emphasis omitted).