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CONFIRMATION ISSUES—SELECTED TOPICS

by

**Jay M. Goffman
Skadden, Arps, Slate, Meagher & Flom LLP
Four Times Square
New York, NY 10036
(212) 735-3000**

and

**Mark A. McDermott
Michael W. Perl
Skadden, Arps, Slate, Meagher & Flom LLP
333 West Wacker Drive
Chicago, IL 60606
(312) 407-0700**

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I. Introduction

This paper provides a general overview of several confirmation and related issues typically encountered in large chapter 11 bankruptcy cases. The topics covered in this paper include so-called "give-up" plans and the absolute priority rule; unfair discrimination; post-confirmation jurisdiction and litigation trusts; and bankruptcy appeals. These subjects are dealt with in a general manner. The paper is meant to provide an overview for practitioners rather than a detailed analysis of all pertinent legal issues. Some of the topics covered can only be dealt with in a cursory manner in a paper of this scope. This article does not provide legal advice and should not substitute for consultation with experienced bankruptcy counsel on these matters. Additionally, this article provides only a summary of selected confirmation items, and therefore should not be viewed as a comprehensive survey of all conceivable issues one may encounter in connection with plan confirmation proceedings.

II. Propriety of "Give Up" Plans

A. Introduction

In order for a chapter 11 plan of reorganization to be confirmed pursuant to § 1129(a) of the Bankruptcy Code, the plan must, among other things, be accepted by all impaired classes of creditors.¹ If this requirement is not met, the plan still may be confirmed pursuant to § 1129(b) of the Bankruptcy Code if it does not discriminate unfairly and is fair and equitable with respect to any class that does not accept the plan.² With respect to unsecured creditors and equity holders, a plan is fair and equitable if either (i) they are paid in full, on a present value basis, either in cash, notes, securities or other consideration, or (ii) no class of stakeholders junior to the dissenting class receives any recovery on account of their claims or interests.³ This fair and equitable standard frequently is referred to as the "absolute priority rule," and it generally mandates that creditors and other stakeholders be paid in the order of their priorities as established by non-bankruptcy law unless the class of which they are members agrees otherwise.

There are many long-standing issues, however, concerning the meaning and scope of this standard in application. For instance, one issue is whether there is a so-called "new value" exception or corollary to the absolute priority rule that allows equity holders to participate in a plan, even if creditors are not paid in full, so long as they contribute value to the reorganization in exchange for their participation interests.⁴ More recently, absolute priorities have been altered under plans involving so-called "give-ups," "gifts," "reverse cram-downs," or "distribution sharing" arrangements. Under such plans, distributions to stakeholders of lower priority are justified on the theory that stakeholders of higher priority have agreed to take less than what they are entitled to receive,

¹ See 11 U.S.C. § 1129(a)(8).

² See *id.* § 1129(b).

³ See *id.* § 1129(b)(2)(B) and (C).

⁴ See generally *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 444-46 (1999).

effectively "giving up" or "gifting" plan consideration to the lower priority stakeholders out of the higher priority stakeholders' own distributions.

The first major case involving a "give-up" was the First Circuit's decision in Official, Unsecured Creditors' Committee v. Stern (In re SPM Manufacturing Corp.),⁵ and plans that contain this provision frequently are referred to as "SPM plans." While the SPM case did not involve a chapter 11 plan, practitioners and courts sometimes point to the following statement from the First Circuit's opinion in support of the proposition that SPM plans are an appropriate means of compromising stakeholder claims: "[C]reditors are generally free to do whatever they wish with the bankruptcy dividends they receive, including to share them with other creditors."⁶ Accordingly, this principal has been relied upon by numerous courts in approving chapter 11 plans that contain give-up or other distribution sharing provisions.⁷

While some court decisions have limited In re SPM to its facts,⁸ the first major statement against so-called "SPM plans" was the Third Circuit's recent decision in In re Armstrong World Industries, Inc.⁹ In that case, the Third Circuit affirmed the District Court's decision denying confirmation of a plan that allowed plan consideration ostensibly payable to one class of creditors to be re-allocated, by agreement of those creditors, to holders of equity interests in the debtor. While the Third Circuit distinguished In re SPM, the Court's decision raised the broader question of whether "give up" or "gift" plans are, as a general matter, proper under the Bankruptcy Code. In order to assess this question, a more detailed analysis of the precise facts, holdings and reasoning of the courts that have considered the issue is required.

B. Overview of SPM and Its Progeny

Any review of this matter requires a complete understanding of what In re SPM involved and what it did *not* involve. Of particular significance to this discussion, the case did *not* involve a chapter 11 debtor and hence, no consideration of the absolute priority rule under § 1129 of the Bankruptcy Code. During the chapter 11 reorganization proceedings of the In re SPM debtor, the secured lender and the committee entered into a written agreement under which they agreed to divide between the lender and general unsecured creditors any proceeds payable to them upon disposition of the debtor's assets. The lender was owed \$9 million, but the ultimate sale of all the debtors' assets generated only \$5 million in proceeds. Upon consummation of the sale, the case was converted to a chapter 7 liquidation. The lender and the committee filed a motion with the Bankruptcy Court requesting distribution of the \$5 million in accordance with the parties' agreement.

⁵ 984 F.2d 1305 (1st Cir. 1993).

⁶ Id. at 1313.

⁷ See, e.g., In re WorldCom, Inc., No. 02-13533 (AJG), 2003 WL 23861928, at *61 (Bankr. S.D.N.Y. Oct. 31, 2003); In re Union Fin. Servs. Group, Inc., 303 B.R. 390 (Bankr. E.D. Mo. 2003); In re Genesis Health Ventures, Inc., 266 B.R. 591, 602 (Bankr. D. Del. 2001); In re MCorp Fin., Inc., 160 B.R. 941, 960 (S.D. Tex. 1993).

⁸ See, e.g., In re Snyders Drug Stores, Inc., 307 B.R. 889, 896 n. 11 (Bankr. N.D. Ohio 2004); In re CGE Shattuck, LLC, 254 B.R. 5, 10-11 (Bankr. D.N.H. 2000); In re Scott Cable Commc'ns, Inc., 227 B.R. 596, 603 (Bankr. D. Conn. 1998).

⁹ 432 F.3d 507, 514-15 (3d Cir. 2005).

The debtor and certain of its insiders objected to distribution of the proceeds in this fashion, arguing that it violated the priority scheme of the Code with respect to an outstanding, priority claim of the Internal Revenue Service (for which the insiders were also liable). The Bankruptcy Court entered an order finding that the lender had a secured claim of \$5 million (i.e., the amount of proceeds realized from the sale). However, it declined to approve the distribution scheme contemplated by the agreement entered into by the lender and the committee, ordering that any amount that otherwise would have been allocated to general unsecured creditors under the agreement should be paid by the lender to the chapter 7 trustee for distribution in accordance with the priority scheme of the Bankruptcy Code – including, presumably, the priority claim of the Internal Revenue Service. The District Court affirmed on appeal.

The First Circuit reversed. The issue on appeal was very narrow: whether the Bankruptcy Court had any power under § 105(a) of the Bankruptcy Code to reform the agreement between the lender and the committee, thereby compelling the lender to pay to the chapter 7 estate monies realized on account of its security interest that it otherwise would have been obligated to pay to the unsecured creditors pursuant to the terms of the agreement. The First Circuit held that the Bankruptcy Court had no such power. The Court was not persuaded by the debtor's argument that the agreement deviated from the priority scheme sanctioned by the Bankruptcy Code, reasoning that since there was no question that the lender was entitled to all of the proceeds of the sale, there was nothing otherwise payable to the estate.

More significantly, since the priority scheme of the Bankruptcy Code does not come into play unless there are assets in the estate after payment in full of all secured claims, the lender's agreement to pay to the general unsecured creditors a portion of the proceeds to which it was exclusively entitled did not violate the Code's priority rules. According to the Court, "[t]he Code does not govern the rights of creditors to transfer or receive nonestate property."¹⁰ It followed this statement with the declaration for which the opinion is best known: "[C]reditors are generally free to do whatever they wish with the bankruptcy dividends they receive, including to share them with other creditors."¹¹

A few months after the First Circuit's opinion in In re SPM, a court first had occasion to consider the applicability of the foregoing proposition in the chapter 11 context. In In re MCorp Financial, Inc., a debtor proposed a plan under which senior bondholders owed \$354 million agreed to reduce the distribution that they were entitled to receive to \$319 million in order to fund a \$33 million settlement with, and payment to, the FDIC in resolution of claims between the debtor and the FDIC.¹² The value of all assets available for creditors other than the senior bondholders, assuming the senior bondholders and other priority creditors were paid in full in accordance with the absolute priorities of the Code, was only about \$6 million.

The junior bondholders objected to the proposed settlement, arguing that

¹⁰ 984 F.2d at 1313.

¹¹ Id.

¹² 160 B.R. at 952-54.

because their claims were not junior to the claims of the FDIC, to pay the FDIC before the claims of the junior bondholders would be to violate the priorities of the Code. Relying on In re SPM, the Court overruled the objection, holding that the "senior [bondholders] may share their proceeds with creditors junior to the junior [bondholders], as long as the junior [bondholders] continue to receive as [sic] least as much as what they would without the sharing."¹³

Since In re MCorp, other courts have confirmed chapter 11 plans with similar provisions. For instance, in In re Genesis Health Ventures, Inc., holders of personal injury claims asserting punitive damages objected to a chapter 11 plan that provided that there would be no recovery on account of such claims.¹⁴ The holders asserted that they should have shared in the recovery being allocated to holders of general unsecured claims. In overruling the objection, the court held that there was insufficient value under the plan to pay in full the claims of the senior secured lenders. Thus, the lenders were entitled to all plan value. Consistent with In re SPM and In re MCorp, the Court held that the lenders could choose to surrender a portion of their recovery to holders of general unsecured claims, but not to holders of punitive damage claims.¹⁵

C. Limitations on In re SPM

In recent years, however, some courts have limited In re SPM to its specific context. For instance, the court in In re Scott Cable Communications, Inc. denied confirmation of a plan that was premised on the theory that undersecured creditors could choose to pay some administrative claimants, but not the Internal Revenue Service, from proceeds of the sale of their collateral.¹⁶ The court held that In re SPM simply was not applicable in the chapter 11 context, where the absolute priority rule applied.¹⁷

More significantly, courts have emphasized that for a give-up plan to be viable, the creditor who is purporting to surrender value to stakeholders of lower priority must in fact be giving up value in which it has a vested property interest. A creditor clearly cannot give away something that it does not own or in which it has no vested property right.¹⁸ While this may seem an obvious proposition, it can be difficult in

¹³ Id. at 960.

¹⁴ 266 B.R. 591, 600 (Bankr. D. Del. 2001). The creditors in Genesis did not argue that the plan violated the absolute priority rule, but rather that it "unfairly discriminated" among similarly-situated creditor groups in contravention of § 1129(b) of the Code.

¹⁵ See also In re Union Fin. Servs. Group, Inc., 303 B.R. 390, 421-23 (Bankr. E. D. Mo. 2003) (plan under which DIP and other secured lenders surrendered a portion of the value of their collateral to junior creditors did not "unfairly discriminate[]" against creditors who did not receive any such value).

¹⁶ 227 B.R. 596, 603-04 (Bankr. D. Conn. 1998).

¹⁷ See also In re CGE Shattuck, LLC, 254 B.R. 5, 11 (Bankr. D.N.H. 2000) (the decision in In re SPM "is not authority for the proposition that parties in a bankruptcy proceeding may avoid the requirements of the Bankruptcy Code by private agreement").

¹⁸ For instance, in In re Snyders Drug Stores, Inc., 307 B.R. 889, 894 (Bankr. N.D. Ohio 2004), a debtor and its secured lenders attempted to justify disparate treatment among classes of unsecured creditors by arguing that the favored classes were receiving a distribution by virtue of the secured lender's agreement to provide them value that it otherwise stood to receive on account of its secured claim. The Court disagreed, finding that the value being allocated to the favored classes

application, especially where there is a legitimate dispute about the value of the reorganization consideration that the surrendering creditor is to receive under a plan and hence, the value of such consideration that it ostensibly is giving away to others.

A recent example of the foregoing is afforded by the decision in In re Exide Technologies, Inc.¹⁹ In that case, under the debtor's proposed plan, senior secured lenders stood to receive substantially all the equity interests in the reorganized company in satisfaction of their secured claims. The debtor and the lenders believed that the enterprise value of the reorganized debtor was insufficient to pay the lenders in full. While unsecured creditors, under this theory, were not entitled to any recovery, the plan provided that the lenders nonetheless would provide a small amount of value for unsecured creditors, ostensibly out of the lenders' own collateral/recovery.

While this approach was clear in theory, it did not work in practice because the Bankruptcy Court found that the debtor had significantly undervalued the enterprise value of the reorganized company. In fact, it agreed with most of the points made by the valuation expert proffered by the creditors' committee, and found that the equity to be provided to the lenders in exchange for their claims under the plan afforded the lenders *more than a 100% recovery* on their claims. The lenders, therefore, were not giving up anything to which they were entitled. Indeed, they stood to receive *more* than they were entitled to receive under the plan, which violates a corollary to the absolute priority rule that no creditor can receive more than the amount of its claim.²⁰

The Court in In re Exide therefore denied confirmation of the plan, finding that it violated the absolute priority rule. The Court concluded that the First Circuit decision in In re SPM was wholly inapposite. In In re SPM, the secured creditor surrendered collateral value to junior creditors despite the fact that it would not be paid in full under the plan. Thus, the creditor was actually giving up real value to which it was exclusively entitled. The secured lenders in In re Exide, by contrast, stood to receive much more than they were owed. Their agreement to provide a so-called "tip" to unsecured creditors therefore did not come from the lenders' own pocket. Rather, it constituted value that should have gone to the unsecured creditors anyway.

The holding in In re Exide can be reduced to the following simple rule: if the value of the consideration that a secured creditor stands to receive under a plan, plus the value of any such consideration that the creditor purports to give up to other stakeholders, is equal to more than 100% of the amount of the creditor's secured claim, then there is no true "gift" by the secured creditor. The plan violates the absolute priority rule and should not be confirmed.

of unsecured creditors was not taken from the secured creditor's collateral. Indeed, such value was actually to be derived from certain estate avoidance actions.

¹⁹ 303 B.R. 48 (Bankr. D. Del. 2003).

²⁰ Id. at 61.

D. Armstrong World Industries

In late 2005, the Third Circuit issued its decision in In re Armstrong World Industries, Inc. The debtor in that case proposed a plan that placed general unsecured creditors in class 6 and asbestos claimants in class 7. Under the plan, neither class of creditors would be paid in full. In particular, members of class 6 stood to recover approximately \$982 million in the aggregate, or about 59.5% of their claims. Members of class 7 would be the beneficiaries of a trust funded with approximately \$1.8 billion, sufficient to afford them "an initial payment percentage" of 20% of their claims. The plan nonetheless provided warrants to class 12 equity interests, valued at between \$35 million and \$40 million, pursuant to the following mechanism: if class 6 accepted the plan, the warrants would be issued directly to class 12 equity interests; if, however, class 6 rejected the plan, the warrants would be granted to class 7, which would in turn be deemed to have transferred them to class 12. Either way, class 12 stood to receive the warrants.

Class 6 voted to reject the plan, and the unsecured creditors' committee objected to confirmation, arguing that the transfer of the warrants to class 12 equity interests violated the absolute priority rule. The Bankruptcy Court submitted proposed findings and conclusions to the District Court that recommended confirmation of the plan. However, the District Court denied confirmation, and the debtor appealed. The Third Circuit affirmed.

As an initial matter, the Third Circuit held that the case was governed by the absolute priority rule, which the Court believed was embodied in the plain language of § 1129(b) of the Code. Moreover, it held that the rule was violated in that case because a class of junior equity interests was receiving consideration under the plan on account of those interests while more senior creditors were not paid in full. It found each of In re SPM, In re MCorp and In re Genesis distinguishable. In particular, because SPM was a chapter 7 case, the First Circuit in that case had no occasion to consider applicability of the absolute priority rule.

Moreover, both SPM and Genesis Health involved property subject to senior lenders' liens, meaning that the property was not subject to distribution in accordance with the Code's priority scheme and hence, could be given up (in part) by the senior creditors to creditors of lower rank. Indeed, the distribution to more junior creditors in such cases effectively was a "carve-out" from the senior creditors' collateral. According to the Third Circuit, the foregoing cases, therefore, did "not stand for the unconditional proposition that creditors are generally free to do whatever they wish with the bankruptcy proceeds they receive."²¹

As is apparent from the foregoing, a key difference between Armstrong and In re SPM is that the former case entailed a so-called "give-up" of *estate* value by a class of unsecured creditors, whereas the latter case entailed a give-up of collateral value by a secured creditor. This raises the question whether a so-called SPM plan that

²¹ In re Armstrong World Indus. Inc., 432 F.3d 507, 514 (3d Cir. 2005).

involves a give-up or a carve-out by a secured creditor with respect to its collateral would be enforced by a court inclined to follow the Third Circuit's reasoning in Armstrong. While it may appear more likely – some courts have approved such plans²² – practitioners cannot forget the Court's emphasis on the importance of the absolute priority rule as well.

E. Legislative History and Supreme Court Precedent

In this regard, lessons may be gleaned from the legislative history of § 1129(b) and Supreme Court decisions that developed and later elaborated upon the fair and equitable standard. For instance, the Armstrong Court quoted statements of Congressional sponsors of the bill that ultimately became the Code: "a senior class *will not be able to give up value* to a junior class *over the dissent of an intervening class* unless the intervening class receives the full amount, as opposed to value, of its claims or interests."²³ Moreover, the legislative history provides that § 1129 "codifies the absolute priority rule from the dissenting class *on down*."²⁴ Section 1129, therefore, "is designed to *prevent a senior class from giving up consideration* to a junior class unless every intermediate class consents, is paid in full, or is unimpaired. This gives intermediate creditors a great deal of leverage in negotiating with senior or secured creditors who wish to have a plan that gives value to equity."²⁵

The plain language of § 1129 obviously does not afford the level of detail contemplated by the legislative history. However, an argument clearly can be made that, the language of the Code notwithstanding, give-up plans, even those involving give-ups by secured creditors, may not be warranted in light of the legislative history. In fact, the argument for give-up plans arguably becomes even more difficult if one examines older Supreme Court precedent that gave rise to the phrase "fair and equitable."²⁶ The Court's main case interpreting the phrase and effectively equating it with the modern notion of the absolute priority rule is Case v. Los Angeles Lumber Products Co., decided under the former Bankruptcy Act.²⁷

In that case, the debtor owned a business worth \$830,000. The debtor's assets were encumbered by secured bonds of approximately \$3.8 million. Thus, there was no equity in the enterprise. The debtor nonetheless proposed a plan of reorganization under which approximately 77% of the reorganization value would be allocated to the bondholders, and 23% of such value would be allocated to existing stockholders. The plan was overwhelmingly accepted by bondholders and shareholders. However, one bondholder objected to confirmation. The trial court nonetheless approved the plan. The Supreme Court reversed, holding that the plan was not "fair and equitable."²⁸ In defining

²² See e.g., In re Union Financial Servs. Group, Inc., 303 B.R. at 422-23.

²³ 432 F.3d at 513. (emphasis added) (citation omitted).

²⁴ H.R. Rep. No. 95-595, at 413 (1977) as reprinted in 1978 U.S.C.C.A.N 5963,6369 (emphasis added).

²⁵ Id. at 416 1978 U.S.C.C.A.N 6372 (emphasis added).

²⁶ The Court has held that § 1129 is to be construed in accordance with pre-Code case law. Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988).

²⁷ 308 U.S. 106, 108-09 (1939).

²⁸ Had these circumstances arisen under the Code, the plan would not have violated, or even implicated, the cramdown standard. Specifically, sufficient acceptances would have been received

this phrase, the Court looked to its own precedent for the "'familiar rule'" that "the 'stockholder's interest in the property [of a debtor] is subordinate to the rights of creditors.'"²⁹

Of particular importance to the present discussion, the Court quoted approvingly from its decision in Louisville Trust Co. v. Louisville N.A. & C. Ry. Co.:³⁰ "*any arrangement of the parties by which the subordinate rights and interests of the stockholders are attempted to be secured at the expense of the prior rights of either class of creditors [secured or unsecured] comes within judicial denunciation.*"³¹ Despite this precedent, the debtor in Case asserted that the plan should have been approved, arguing that "the stockholders' 'right of participation was secured by contract before, and as a condition precedent to, the institution of the [bankruptcy] proceedings.'"³² The Court dismissed this argument in the following language:

If the reorganization court were bound by such conventions of the parties, it would be effectively ousted of important duties which the Act places on it. Federal courts acting under [the Act] would be required to place their imprimatur on plans of reorganization which disposed of the assets of a company not in accord with the standards of 'fair and equitable' but in compliance with agreements which the required percentages of security holders had previously made. Such procedure would deprive scattered and unorganized security holders of the protection which the Congress had provided them under [the Act]. The scope of the duties and powers of the Court would be delimited by the bargain which reorganizers had been able to make with security holders . . . Minorities would have their fate decided not by the court in application of the law of the land as prescribed in [the Act], but by the forces utilized by reorganizers in prescribing the conditions precedent on which the benefits of the statute could be obtained. No conditions precedent to enjoyment of the benefits of [the Act] can be provided except by the Congress. To hold otherwise would be to allow reorganizers to rewrite it so as to best serve their own ends.³³

In short, the Court held that a class of secured creditors could not agree with out-of-the money stockholders to surrender to the stockholders a portion of the value that the creditors otherwise were entitled to receive. Under this rule, a court is not bound by any such agreement among stakeholders, and the fact that a plan embodying the agreement has been overwhelmingly accepted by the secured creditors will not serve to bind any dissenting creditor. These principles presumably may apply in situations where

²⁹ under § 1126 such that the class of bondholders would have been deemed to have accepted the plan. The one dissenting creditor would have been bound by the plan. See 11 U.S.C. § 1141. Id. at 116 quoting Louisville Trust Co. v. Louisville, N.A. & C. Ry. Co., 174 U.S. 674, 684, (1899).

³⁰ 174 U.S. 674, 684 (1899).

³¹ 308 U.S. at 116 (emphasis added).

³² Id. at 128.

³³ Id. at 128-29. While the Court criticized the treatment of minority creditor groups, as noted above in note 27, under the Code, minority creditors nonetheless can be bound by a plan so long as the requisite acceptances of the plan are obtained in accordance with § 1126 of the Code.

an intervening class of general unsecured creditors is denied recovery on account of the agreement between the senior creditors and stockholders. Indeed, the Louisville Trust case, quoted approvingly by the Court in Case, involved this very fact pattern.³⁴

Specifically, a railroad was sold at a foreclosure sale for an amount far less than the amount of the secured debt. Shareholders nonetheless received shares in the acquiring company -- by agreement of the secured debtholders -- whereas general unsecured creditors received nothing. The Supreme Court overturned a lower court order approving this arrangement. The Court clearly was concerned by facts suggesting collusion between the senior creditors and the stockholders designed to thwart the claims of general creditors. However, the Court made broad observations that could be construed to condemn any arrangement whereby a senior creditor gives up reorganization consideration to stakeholders of more junior rank:

It is one thing for a [secured] bondholder who has acquired absolute title by foreclosure to mortgaged property to thereafter *give* of his interest to others, and an entirely different thing whether such bondholder, to destroy the interest of all unsecured creditors, to secure a waiver of all objections on the part of the stockholder, and consummate speedily the foreclosure, may proffer to him an interest in the property after foreclosure. The former may be beyond the power of the courts to inquire into or condemn. The latter is something which on the face of it deserves the condemnation of every court, and should never be aided by any decree or order thereof.³⁵

This is strong language which has never been overruled. However, none of it is cited in any of the more recent opinions dealing with the propriety of give-up plans. Because these Supreme Court cases did not deal with § 1129 or current notions of give-up plans of reorganization, it is not clear whether a persuasive case can be made that they control a modern court's consideration of the propriety of this kind of plan mechanism. But the breadth of the Court's language in these cases may warrant more thorough consideration of the matter in the context of a give-up plan where a secured creditor purports to surrender a portion of its collateral value to junior stakeholders.

F. Conclusion

In sum, the current weight of authority appears to sanction the use of give-up plans where a secured creditor surrenders a portion of its collateral value to junior stakeholders. While the same analysis arguably should apply to gifts by classes of unsecured creditors, most recent case law is generally against a plan contemplating a give-up by unsecured creditors. Indeed, some courts have noted that unsecured creditors have no vested property rights that they can "give up." The Supreme Court's decisions in Case and Louisville Trust arguably can be distinguished on their facts; because they did not involve interpretations of § 1129; and because they did not arise under plans governed by the voting provisions of §§ 1126 and 1141 of the Code that serve to bind

³⁴ 174 U.S. 674 (1899).

³⁵ Id. at 688 (emphasis added).

dissenting creditors if the requisite acceptances are obtained. Practitioners nonetheless should be prepared to see these cases cited to them in support of objections to give-up plans, even those involving give-ups by secured creditors, where objectors may argue that such plans constitute nothing more than the same sort of collusive efforts of certain stakeholders, to the detriment of others, that the Supreme Court condemned in these earlier cases.

III. "Unfair Discrimination" Among Creditors

A. Introduction

Many of the published decisions dealing with give-up plans have considered the propriety of such plans not only under the "fair and equitable" standard, but also under the related cramdown standard which requires that a plan not "discriminate unfairly" among creditors and other stakeholders.³⁶ In fact, the "fair and equitable" and "unfair discrimination" standards are related conceptually. The fair and equitable standard is a "vertical" standard requiring respect for, and fairness among, stakeholders with different priorities.³⁷ The unfair discrimination standard, on the other hand, is a "horizontal" standard requiring fairness among stakeholders of equal rank.

While unfair discrimination issues only arise in the context of cramdown confirmation hearings, such issues frequently are accompanied by a related issue that may be raised in a non-cramdown context, i.e., whether a plan improperly places creditors of equal rank into different classes. Indeed, creditors of equal rank who are treated differently *must* be placed in separate classes.³⁸ A common example of a plan that separately classifies creditors of equal rank and treats each class differently is where a debtor places in one class claims held by unsecured trade creditors who are necessary to the reorganized debtor's future business prospect, whereas all other unsecured creditors, including holders of lease rejection claims and personal injury claims, are placed in a separate class. The go-forward trade creditors often are treated more favorably than the other creditors under the theory that they are necessary to the reorganization whereas the other creditors are not.³⁹

Plans of this sort frequently draw the objection that the two groups of creditors improperly were placed in the same class solely to ensure that at least one impaired class of creditors votes in favor of the plan as required by § 1129(a)(10) of the Code. They also frequently draw the objection that the treatment of the disfavored creditors constitutes unfair discrimination (an objection that is relevant only if the class of disfavored creditors votes against the plan). A final and related objection that sometimes

³⁶ See 11 U.S.C. § 1129(b)(1).

³⁷ See *In re Simmons*, 288 B.R. 737, 747 (Bankr. N.D. Tex. 2003) (chapter 13 case).

³⁸ See 11 U.S.C. § 1123(a)(4) (requiring all creditors in the same class to be treated the same unless a creditor specifically agrees to a less favorable treatment).

³⁹ See, e.g., *In re Am. HomePatient, Inc.*, 298 B.R. 152, 168 (Bankr. M.D. Tenn. 2003) (plan did not discriminate unfairly by paying trade creditors faster than other creditors; favorable treatment "is supported by the reasonable basis of continued good relations with the trade creditors"), *aff'd*, 420 F.3d 559 (6th Cir. 2005).

is made with respect to such plans is that they have not been proposed in good faith as required by § 1129(a)(3) of the Code. As a practical matter, there can be no complete discussion of the unfair discrimination standard without a discussion of the cases dealing with classification of claims. Indeed, the standards developed by courts with respect to each issue are strikingly similar.

B. Standards for Classification of Claims

Section 1122 of the Code governs the classification of claims in chapter 11 plans. Subsection (a) of that section states that "a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class." Note what the statute says and what it does not say. It says that claims or interests in a particular class must be substantially similar. It does *not* say, however, that *all* substantially similar claims *must* be placed in the same class. To the contrary, claims that are substantially similar may, in fact, be placed in different classes. Indeed, it is generally accepted that debtors have considerable discretion in determining how to structure the classes in their plans of reorganization.

There appear to be only two limitations on this flexibility. First, courts uniformly have held that a debtor may not classify similar claims differently in order to gerrymander an affirmative vote on its plan.⁴⁰ Second, a debtor's classification scheme will be sustained so long as it can articulate some "legitimate business reason" for doing so.⁴¹ A debtor can satisfy this requirement if it provides evidence that its business would be adversely affected if it were precluded from treating separate classes of creditors differently. A classic example of a legitimate business reason for separately classifying creditors of equal rank is that outlined above, i.e., where a debtor separately classifies go-forward trade creditors and provides them better treatment than other unsecured creditors because the go-forward creditors are essential to the debtor's restructuring.

C. Standards for Unfair Discrimination

The phrase "unfair discrimination" is defined nowhere in the Code, and the legislative history is of very limited use in any attempt to discern its meaning. As a general matter, courts therefore have adopted a multi-factor test designed to take into account the facts and circumstances of each case and that considers notions of reasonableness and good faith. This multi-factor test is premised on one clear aspect of the statute: it does not prohibit all discrimination, but only that which is "unfair."⁴² Thus, if the discrimination proposed in a plan comports with general notions of fairness, it will be sustained.

Most courts consider four factors (or their variants) in determining

⁴⁰ See, e.g., In re Greystone III Joint Venture, 995 F.2d 1274, 1279 (5th Cir. 1991); John Hancock Mut. Life Ins. Co. v. Route 37 Bus. Park Assocs., 987 F.2d 154, 159 (3d Cir. 1993).

⁴¹ See, e.g., Aetna Cas. & Sur. Co. v. Clerk, U.S. Bankr. Ct., N.Y., N.Y. (In re Chateaugay Corp.), 89 F.3d 942, 951 (2d Cir. 1996); Teamsters Nat'l Freight Indus. Negotiating Comm. V. U.S. Truck Co., 800 F.2d 581, 589-90 (6th Cir. 1986).

⁴² In re Union Fin. Servs. Group, Inc., 303 B.R. 390, 421 (Bankr. E.D. Mo. 2003).

whether a plan's discrimination among creditors of equal rank is fair: (i) whether there is a reasonable basis for the discrimination; (ii) whether the discrimination is necessary to the reorganization; (iii) whether the discrimination is proposed in good faith; and (iv) whether the degree of discrimination is directly proportional to its rationale.⁴³ There are obvious parallels between these factors and the requirement that separate classification of similar creditors be justified by a legitimate or reasonable business purpose. For instance, the "reasonable basis" prong of this four-part inquiry essentially is indistinguishable from the "reasonable business purpose" required for separate classification of creditors of equal rank.

Moreover, the second prong, which focuses on whether the discrimination is "necessary to the reorganization," presumably would be supported by evidence that separate classification (and more favorable treatment) of certain creditors is necessary to the debtor's go-forward business prospects. The good faith prong of the unfair discrimination test is, in many respects, redundant of § 1129(a)(3) of the Code, which requires that plans be proposed in good faith, i.e., with an honest purpose to reorganize; that they be consistent with the objectives and purposes of the Code; and that they not be proposed by any means forbidden by law.⁴⁴ It also dovetails with the requirement that stakeholders of equal rank not be separately classified solely for the improper purpose of manipulating voting on a plan.

The fourth and final prong of the undue discrimination standard – that the degree of the discrimination be directly proportional to its rationale – has no parallel in the classification cases. It appears to be based on the notion that if there is not some nexus between the incremental value being afforded to favored creditors and the value to be derived by the reorganizing debtor with respect to its rehabilitative prospects, then the discrimination will be deemed unfair. Indeed, there is a strong parallel between this requirement and a requirement imposed in recent court decisions dealing with debtors' requests to pay the prepetition claims of so-called "critical vendors" prior to confirmation of a plan. In particular, an increasing number of courts have stated that vendors may not be favored in this fashion unless a debtor can establish that its estate and all creditors will be better off with the payments than without them.⁴⁵ Critical vendor payments also must be "necessary" to the debtor's rehabilitative prospects, similar to the requirement that discrimination under a plan that favors certain creditors must be "necessary to the reorganization."

Courts have applied the foregoing factors or similar considerations in numerous cases, sustaining plans that discriminate among stakeholders of equal rank in a

⁴³ See, e.g., Liberty Nat'l Enters. v. Ambanc La Mesa Ltd. P'ship, 115 F.3d 650, 656 (9th Cir. 1997); In re Hoffinger Indus., Inc., 321 B.R. 498, 505 (Bankr. E.D. Ark. 2005); In re Snyder's Drug Stores, Inc., 307 B.R. 889, 894-95 (Bankr. N.D. Ohio 2004); In re Union Fin. Servs. Group, Inc., 303 B.R. at 421; In re Lernout & Hauspie Speech Prods., N.V., 301 B.R. 651 (Bankr. D. Del. 2003), aff'd, 308 B.R. 672 (D. Del. 2004); In re Am. HomePatient, Inc., 298 B.R. at 168; In re Simmons, 288 B.R. at 750; In re WorldCom, Inc., No. 02-13533 (AJG), 2003 WL 23861928 at *59 (Bankr. S.D.N.Y. Oct. 31, 2003).

⁴⁴ See, e.g., In re Rivers End Apartments, Ltd., 167 B.R. 470, 476 (Bankr. S.D. Ohio 1994).

⁴⁵ See, e.g., In re Kmart Corp., 359 F.3d 866 (7th Cir. 2004).

very broad array of circumstances involving exceptionally disparate treatment. For instance, in Creekstone Apartments Associates, L.P. v. Resolution Trust Corp., a debtor proposed a 10% distribution on the secured lender's unsecured deficiency claim and a 100% distribution on all other general unsecured claims.⁴⁶ The court sustained this treatment, agreeing with the debtor that the favorable treatment for the general unsecured creditors was necessary to the reorganized debtor's ability to obtain trade credit from vendors whose services and products were essential to the debtor's operations.⁴⁷

Similarly in In re Kliegl Bros. Universal Electric Stage Lighting Co., the bankruptcy court held that a debtor's plan properly could propose to pay a 75% distribution on union member wage claims, while paying only 15% to holders of other unsecured claims.⁴⁸ The court reasoned that there was a possibility that the union members may strike if they were not paid, and that the debtor's critical need to continue to utilize the labor provided by unionized workers was sufficient to justify the large distribution to them. The court held as it did while acknowledging that there was "no testimony to support such a finding."⁴⁹

Cases involving tort claims provide especially tempting opportunities for disparate treatment under the business purpose rationale. In one case, the debtor proposed to pay the holder of a \$35 million tort claim an amount equal to 0.14% of its claim.⁵⁰ Trade creditors, however, stood to receive a 50% distribution. The court confirmed the plan, even though testimony at the confirmation hearing suggested that many trade creditors would not do business with the reorganized debtor in any event. A much more recent case, however, declined to approve discrimination of this magnitude, holding that a debtor could not propose to pay trade creditors a 30% distribution while limiting tort claimants to recoveries under insurance policies that appeared to have questionable, if any, value.⁵¹

D. A Tightening of the Standards?

While the foregoing standards for determining whether a plan unfairly discriminates against a group of creditors fulfills one of the key policies underlying the Code – flexibility – it arguably conflicts with another one of the key aims of the Code – equality of treatment of similarly-situated creditors. Moreover, there are at least two other

⁴⁶ 168 B.R. 639 (Bankr. M.D. Tenn. 1994).

⁴⁷ See In re Simmons, 288 B.R. at 752 (" [I]f discrimination serves to enhance going concern value it may not be unfair . . .") see also In re Graphic Commc'ns, 200 B.R. 143, 148 (Bankr. E.D. Mich. 1996) ("A plan may reasonably discriminate if the 'proposed discrimination protect[s] a relationship with specific creditors that the debtor need[s] to reorganize successfully.") (citation omitted).

⁴⁸ 149 B.R. 306 (Bankr. E.D.N.Y. 1992); In re Richard Buick, Inc., 126 B.R. 840, 851-52 (Bankr. E.D. Pa. 1991) (allowing separate classification of trade claims from other unsecured claims and payment in full of the former with payment of only 5% to the latter).

⁴⁹ Kliegl Bros., 149 B.R. at 309; see also Aetna Cas. and Sur. Co., 89 F.3d at 949 (allowing separate classification of unpaid workers' compensation claims and payment in full, whereas other unsecured creditors would not be paid in full).

⁵⁰ In re Rochem, Ltd., 58 B.R. 641 (Bankr. D.N.J. 1985).

⁵¹ In re Hoffinger Indus., Inc., 321 B.R. at 511.

potential drawbacks to the standard. First, being premised on nothing more than a court's determination of "reasonableness," it arguably is vague, leading to unpredictable and inconsistent results in application. Second, it may create incentives for trade or other creditors considered "critical" or "necessary" to the reorganization to exert undue leverage over the reorganization process. For this reason, some courts have adopted a more stringent standard based on a test formulated by Professor Bruce Markell.⁵² Prior to the 2005 amendments to the Code, the Committee on Bankruptcy and Corporate Reorganization of the Association of the Bar of the City of New York (the "New York Reorganization Committee") advocated an even tougher standard.⁵³

The so-called "Markell Proposal" suggests that there should be a rebuttable presumption of unfair discrimination under a plan where there is (i) a dissenting class; (ii) another class of the same rank; and (iii) a difference in the plans treatment of the two classes that results in either (a) a materially lower percentage recovery for the dissenting class, measured in terms of net present value, or (b) regardless of percentage recovery, an allocation under the plan of materially greater risk to the dissenting class in connection with its proposed distribution. This presumption could be rebutted by a showing that either (i) the greater recovery is consistent with what would occur outside bankruptcy or is offset by contributions from the favored class or (ii) greater risk is consistent with prebankruptcy expectations.

As indicated above, several courts have explicitly adopted the Markell Proposal.⁵⁴ In applying it, most of them sustained the proposed discrimination, although one court declined to approve a plan that proposed to pay one group of unsecured creditors in full while paying another group of unsecured creditors only 1% of their claims.⁵⁵ The New York Reorganization Committee's proposal, which has not yet been adopted in any published decision, endorsed the Markell Proposal relating to the rebuttable presumption. However, it recommended that this presumption may be overcome only by a showing that any material discrimination in recovery or allocation of risk be justified by evidence that the favored class is making a "specific contribution in money or money's worth reasonably equivalent to the amount by which it is favored."⁵⁶ This proposal is derived from the "new value" corollary to the absolute priority rule, which states that stakeholders of lower priority may participate in a reorganization even if stakeholders of higher priority are not paid in full only if they contribute "new value" to

⁵² Bruce A. Markell, A New Perspective on Unfair Discrimination in Chapter 11, 72 Am. Bankr. L. J. 227 (1998).

⁵³ Making the Test for Unfair Discrimination More "Fair": A Proposal, 58 Bus. Law. 83 (2002) ("New York Reorganization Committee Proposal").

⁵⁴ E.g., In re Dow Corning Corp., 244 B.R. 696 (Bankr. E.D. Mich. 1999); In re Greate Bay Hotel & Casino, Inc., 251 B.R. 213 (Bankr. D. N.J. 2000); see also In re Lernout & Hauspie Speech Prods., N.V., 301 B.R. 651, 661 (Bankr. D. Del. 2003) (quoting standard), aff'd, 308 B.R. 672 (D. Del. 2004).

⁵⁵ In re Sentry Operating Co., 264 B.R. 850, 864 (Bankr. S.D. Tex. 2001) ("a 99% payout differential is not justified").

⁵⁶ New York Reorganization Committee Proposal, supra note 53, at 106-07.

the reorganization in the form of money or money's worth.⁵⁷

The claims of necessary, go-forward trade vendors may warrant favorable treatment under the Markell Proposal. Specifically, under the Proposal, a debtor may rebut the presumption of unfair discrimination if the greater recovery to be afforded a particular group of creditors is consistent with the parties' expectations outside of bankruptcy. Outside bankruptcy, trade vendors typically receive payment according to 30, 45 or 60 days terms. Such expectations therefore may warrant greater, or at least quicker, payments to trade creditors under a plan.⁵⁸ Moreover, under the Proposal, greater recovery may be warranted if it is offset by contributions to the favored class. Trade vendors provide such contributions in the form of trade support for the reorganized company.⁵⁹

It is not entirely clear whether this rationale holds up, however, if trade claims are purchased by claims traders.⁶⁰ It is far less likely that critical trade vendors would warrant favorable treatment under the proposal by the New York Reorganization Committee absent a commitment to fund the reorganization. It remains to be seen whether more courts will adopt the Markell Proposal or the proposal of the New York Reorganization Committee and, if so, how these proposals will be applied in practice.

Moreover, these proposals may be part of a larger trend away from practices that result in some creditors receiving more favorable treatment, and towards practices that ensure greater equality among creditors of equal rank. There are two recent case law developments where this trend can be seen. The first relates to the propriety of critical vendor payments. Older decisions in this area granted debtor requests to pay the prepetition claims of critical vendors outside the context of a plan if such vendors were "critical," "necessary" or "indispensable" to the reorganization.⁶¹ The more recent trend, however, is to impose more exacting standards, including a requirement of evidentiary proof that all creditors will be better off with the payments than without them.⁶²

An example of a recent application of this tougher standard is afforded by the opinion of the Bankruptcy Court for the Eastern District of Virginia in In re United American, Inc.⁶³ In that case, a chapter 11 contractor was unable to complete a construction project, and thereby receive a significant payment from the owner, because it was precluded from paying the prepetition claims of two of its sub-contractors. It

⁵⁷ See Case v. L. A. Lumber Prods. Co., 308 U.S. 106, 117-19 (1939) (discussing application of absolute priority rule).

⁵⁸ See New York Reorganization Committee Proposal, supra note 53, at 97.

⁵⁹ See, e.g., In re Rivers End Apartments, Ltd., 167 B.R. 470, 488 (Bankr. S.D. Ohio 1994) (quicker plan payments to trade creditors justified by the fact that they "anticipate payment on a short-term basis").

⁶⁰ See New York Reorganization Committee Proposal, supra note 53, at 100.

⁶¹ See, e.g., In re Payless Cashways, Inc., 268 B.R. 543 (Bankr. W.D. Mo. 2001); In re Just for Feet, Inc., 242 B.R. 821 (D. Del. 1999).

⁶² See, e.g., In re Kmart Corp., 359 F.3d 866, 872-73 (7th Cir. 2004); In re Tropical Sportswear Int'l Corp., 320 B.R. 15, 20 (Bankr. M.D. Fla. 2005); In re Mirant Corp., 296 B.R. 427 (Bankr. N.D. Tex. 2003); In re CoServ, LLC, 273 B.R. 487, 498-99 (Bankr. N.D. Tex. 2002).

⁶³ 327 B.R. 776 (Bankr. E.D. Va. 2005).

therefore sought authority to pay them, but the court ruled that the contractor failed to satisfy the tests for payment of prepetition claims outside the context of a plan. With respect to one sub-contractor in particular, the court was unpersuaded by the fact that a successor sub-contractor would have to undertake significant work at "perhaps significant expense" to the estate, and that the sub-contractor had no obligation to turn over necessary shop drawings that had already been approved by government agencies and that a successor would have to re-create. In denying the requested payments, the Court pointedly noted that the Code prohibits unfair discrimination among creditors of equal rank.⁶⁴

The second recent development is the Supreme Court's 2006 ruling in Howard Delivery Service, Inc. v. Zurich American Insurance Co.⁶⁵ The Court held in Zurich American that an insurer's prepetition claim against a debtor for unpaid workers' compensation premiums did not constitute an unpaid contribution to an employee benefit plan under § 507(a)(5) of the Bankruptcy Code.⁶⁶ Section 507(a) of the Code affords priority status to several specific classes of prepetition claims, including claims for wages, salaries, commissions and related items. In other words, the statute sanctions certain types of discrimination among creditors. While Zurich American had nothing to do with unfair discrimination under § 1129(b), the Court clearly took a dim view of the broader notion of affording preferential treatment to some creditors, but not others, absent explicit sanction in the Bankruptcy Code.

Specifically, in construing the wording of § 507(a)(5) to exclude from its scope the claim asserted by the insurance carrier, the Court said that it was guided by the "principle that provisions [of the Bankruptcy Code] allowing preferences *must be tightly construed*."⁶⁷ Indeed, to "'give priority to a claimant not clearly entitled thereto is not only inconsistent with the policy of equality of distribution; it dilutes the value of the priority for those creditors Congress intended to prefer.'" According to the Court, to the extent there is any doubt about the proper way to interpret a provision of the Code according a certain class of claims priority, the doubt "is best resolved in accord with the Bankruptcy Code's *equal distribution aim*."⁶⁸

E. Conclusion

In sum, reorganizing debtors have considerable discretion in creating separate classes of creditors and proposing disparate treatment for those creditors most necessary for their go-forward prospects. There clearly are some recent trends in other areas of reorganization law that are restricting debtors' ability to favor some creditors over others, most notably in the critical vendor context. However, absent a major change in approach by the courts through adoption of the Markell Proposal, the New York Reorganization Committee Proposal, or other stringent standards, reorganizing debtors

⁶⁴ Id. at 782-84.

⁶⁵ 126 S. Ct. 2015 (2006).

⁶⁶ Id. at 2116.

⁶⁷ Id. (emphasis added).

⁶⁸ Id. (citation omitted) (emphasis added); see also United States v. Noland, 517 U.S. 535 (1996) (policy choices regarding priorities should be left to Congress).

should be free to structure their plans primarily in accordance with their own particular business needs and restructuring goals consistent with the Code's aim of affording chapter 11 businesses the flexibility they need to maximize their prospects of a successful turnaround.

IV. Post Confirmation Jurisdiction and Liquidating Trusts

A. Post Confirmation Jurisdiction In General

The subject matter jurisdiction of bankruptcy courts is governed by statute. The two relevant jurisdictional statutes are 28 U.S.C. § 1334 and § 157. Specifically, 28 U.S.C. § 1334 provides that "the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11."⁶⁹ Additionally, 28 U.S.C. § 157 provides that "Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11"⁷⁰

Proceedings "arising under title 11" and "arising in" bankruptcy cases are generally referred to as "core proceedings."⁷¹ A "core proceeding" is one that invokes a substantive right under title 11, or could only arise in the context of a bankruptcy case.⁷² Bankruptcy courts also have jurisdiction of a much broader group of cases, namely, "non-core" proceedings that are merely "related to" a case under title 11. Under what has become known as the "*Pacor* test," followed in most jurisdictions, a bankruptcy court has "related to" jurisdiction if "the outcome of the proceeding could conceivably have any effect on the estate being administered in bankruptcy."⁷³

The extent of a bankruptcy court's post-confirmation "related to" jurisdiction is not clear. In fact, the Bankruptcy Court for the Southern District of New York recently stated that "all courts that have addressed the question have ruled that once confirmation occurs, the bankruptcy court's jurisdiction shrinks."⁷⁴ Numerous other courts have endorsed this principle,⁷⁵ although courts are split on the precise scope of a bankruptcy court's post-confirmation jurisdiction.⁷⁶ In determining whether a bankruptcy

⁶⁹ 28 U.S.C. § 1334(b).

⁷⁰ *Id.* § 157(b)(1).

⁷¹ *Montana v. Goldin* (In re Pegasus Gold Corp.), 394 F.3d 1189, 1193 (9th Cir. 2005).

⁷² *Penthouse Media Group v. Guccione* (In re Gen. Media, Inc.), 335 B.R. 66, 72 (Bankr. S.D.N.Y. 2005).

⁷³ *In re Pegasus Gold Corp.*, 394 F.3d at 1193 (quoting *Pacor, Inc. v. Higgins*, 743 F.2d 984, 994 (3d Cir. 1984)); see also *Resorts Int'l Fin., Inc. v. Price Waterhouse & Co.* (In re Resorts Int'l, Inc.), 372 F.3d 154, 164 (3d Cir. 2004).

⁷⁴ *In re Gen. Media, Inc.*, 335 B.R. at 73.

⁷⁵ See *Premium of Am., LLC v. Sanchez* (In re Premium Escrow Servs., Inc.), 342 B.R. 390, 396 (Bankr. D.D.C. 2006) (quoting *In re Gen. Media, Inc.*, 335 B.R. at 73; see also *In re Pegasus Gold Corp.*, 394 F.3d at 1194 (citing *In re Resorts Int'l, Inc.*, 372 F.3d at 166-67) ("We agree that post-confirmation bankruptcy court jurisdiction is necessarily more limited than pre-confirmation jurisdiction, and that the *Pacor* formulation may be somewhat overbroad in the post-confirmation context.").

⁷⁶ For a discussion of courts' differing views on the matter, see Harold S. Novikoff, et al., Chapter 11 Business Reorganizations – Post-Confirmation Issues: Ascertaining the Effective Date; Post-

court retains jurisdiction post confirmation, the Third Circuit in Resorts International recently adopted what has been coined the "close nexus" test. As the court stated, "[t]hough courts have varied the standard they apply post-confirmation, the essential inquiry appears to be whether there is a *close nexus* to the bankruptcy plan or proceeding sufficient to uphold bankruptcy court jurisdiction over the matter."⁷⁷

The court further explained that the "close nexus" test means that "when a matter affects the interpretation, implementation, consummation, execution, or administration of a confirmed plan or incorporated litigation trust agreement, retention of post-confirmation bankruptcy court jurisdiction is normally appropriate."⁷⁸ Numerous other courts have followed the "close nexus" or similar tests.⁷⁹ The rationale behind the close nexus test is that extending jurisdiction beyond matters that have a close nexus to the bankruptcy plan or proceeding "open[s] the specter [for] unending jurisdiction."⁸⁰ Without limiting a bankruptcy court's post confirmation jurisdiction, "related to" jurisdiction in the post confirmation setting therefore could be boundless.⁸¹

Satisfaction of the close nexus test, while necessary for post-confirmation jurisdiction, may not be sufficient by itself. Many courts have held that the plan of reorganization itself must specifically provide for retention of jurisdiction over the dispute for the bankruptcy court to have post-confirmation jurisdiction over the matter.⁸² However, "[a] bankruptcy court may not create its own jurisdiction over a matter through a plan of reorganization."⁸³ "Thus, "[i]f there is no jurisdiction under 28 U.S.C. § 1334 or

Confirmation Jurisdiction; Serial Filing; Post-Confirmation Litigation Vehicles, 631, 639-45 (2005), available at SK092 ALI-ABA 631 (Westlaw) ("Post-Confirmation Issues").

⁷⁷ In re Resorts Int'l, Inc., 372 F.3d at 166-67 (emphasis added).

⁷⁸ Id. at 168-69.

⁷⁹ See In re Pegasus Gold Corp., 394 F.3d at 1194 (adopting Third Circuit's formulation); In re Premium Escrow Servs., Inc., 342 B.R. at 397 (quoting Kassover v. Prism Venture Partners, LLC (In re Kassover), 336 B.R. 74, 79 (Bankr. S.D.N.Y. 2006)) (applying close nexus text); U.S. Brass Corp. v. Travelers Ins. Group, Inc. (In re U.S. Brass Corp.), 301 F.3d 296 (5th Cir. 2002) (quoting Bank of La. v. Craig's Stores of Texas, Inc. (In re Craig's Stores of Texas, Inc.), 266 F.3d 388, 390 (5th Cir. 2001) ("After a debtor's reorganization plan has been confirmed, the debtor's estate, and thus bankruptcy jurisdiction, ceases to exist, other than for matters pertaining to the implementation or execution of the plan.")); Guttman v. Martin (In re Railworks Corp.), 325 B.R. 709, 723 (Bankr. D. Md. 2005) (citing In re Resorts Int'l, Inc., 372 F.3d at 166-67); Ernst & Young LLP v. Cohen (In re Friedman's Inc), Nos. 406CV024, 406CV086, slip op. at 6 (S.D. Ga. June 21, 2006) ("[O]nly those matters with a 'close nexus' to the bankruptcy plan shall fall under the bankruptcy court's jurisdiction.").

⁸⁰ In re Railworks Corp., 325 B.R. at 723.

⁸¹ But see In re General Media, Inc., 335 B.R. at 73 n.7 (citing Boston Regional Med. Ctr. v. Reynolds (In re Boston Regional Med. Ctr.), 410 F.3d 100 (1st Cir. 2005) (explaining that post-confirmation jurisdiction in a liquidating chapter 11 case is greater because the debtor is winding up and there is no chance of endless jurisdiction)).

⁸² In re General Media, Inc., 335 B.R. at 73-74 (citing Hosp. and Univ. Prop. Damage Claimants v. Johns Manville Corp. (In re Johns Manville Corp.), 7 F.3d 32, 34 (2d Cir. 1993)). Some courts have held, however, that the absence of a plan provision retaining jurisdiction in a confirmed plan does not deprive a bankruptcy court of post-confirmation jurisdiction. See, e.g., United States Trustee v. Gryphon at the Stone Mansion, Inc., 216 B.R. 764, 769 (W.D. Pa. 1997), aff'd, 166 F.3d 552 (3d Cir. 1999).

⁸³ In re Railworks Corp., 325 B.R. at 722 (citing In re Resorts Int'l, Inc., 372 F.3d at 161).

28 U.S.C. § 157, retention of jurisdiction provisions in a plan of reorganization or trust agreements are fundamentally irrelevant."⁸⁴ In short, for a bankruptcy court to retain post confirmation jurisdiction, the bankruptcy court must have subject matter jurisdiction (i.e., there must be a "close nexus") *and* the plan of reorganization must specifically provide for retention of jurisdiction.

B. Liquidating/Litigation Trusts

One area where issues of post-confirmation jurisdiction are particularly important is in the context of liquidating trusts or litigation trusts established under plans of reorganization. As the Third Circuit noted: "Whether a matter has a close nexus to a bankruptcy plan or proceeding is particularly relevant to situations involving continuing trusts, like litigation trusts, where the plan has been confirmed, but former creditors are relegated to the trust res for payment on account of their claims."⁸⁵ Plans of reorganization often establish separate legal entities such as liquidating or litigation trusts. This often occurs to expedite the reorganization process by moving certain claims or causes of action held by the debtor to a trust for the trust to pursue on behalf of claimants.⁸⁶ If a trust is involved, a trustee is appointed to administer the trust and pursue the causes of actions and legal rights of the trust.

Whether a bankruptcy court has post-confirmation "related to" jurisdiction over a liquidating trust established under a plan of reorganization will depend on whether the "close nexus" test has been satisfied. Additionally, in order for a bankruptcy court to exercise post-confirmation jurisdiction over a litigation trust, the plan must specifically provide, as contemplated by § 1123(b)(3) of the Bankruptcy Code, for "the retention and enforcement by the debtor, the trustee, or by a representative of the estate appointed for such purpose, of any such claim or interest."⁸⁷ There are three general requirements under this section. First, "the plan must retain the claims to be asserted."⁸⁸ Courts are divided over how specifically a claim or cause of action must be described in order for the claim or cause of action to be retained.⁸⁹

Some courts require that a plan must "specifically and unequivocally" retain and describe the action,⁹⁰ while other courts permit reserving certain types or

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Id.

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In re Resorts Int'l, Inc., 372 F.3d at 167.

⁸⁶

See, e.g., In re Premium Escrow Servs., Inc., 342 B.R. at 394-95 (causes of action turned over); In re Railworks Corp., 325 B.R. at 713 (causes of action turned over); In re Friedman's Inc., Case No. 05-40129 (Bankr. S.D. Ga. 2005) (Davis, J.) (establishing creditor's trust whereby certain causes of action were turned over to a trust for the benefit of unsecured creditors).
11 U.S.C. § 1123(b)(3)(B).

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In re Premium Escrow Services, 342 B.R. at 400 (quoting In re Railworks Corp., 325 B.R. at 715).
⁸⁸ See Kmart Corp. v. Intercraft Co. (In re Kmart Corp.), 310 B.R. 107, 120 (Bankr. N.D. Ill. 2004);
⁸⁹ See also In re Railworks Corp., 325 B.R. at 716 (citing Fleet Nat'l Bank v. Gray (In re Bankvest), 375 F.3d 51 (1st Cir. 2004) (discussing various court decisions and the level of specificity required to retain certain actions)); see also Post-Confirmation Issues, supra note 76, at 641-42 (collecting cases)).

⁹⁰

In re Kmart Corp., 310 B.R. at 120 (quoting Harstad v. First Am. Bank (In re Harstad), 155 B.R. 500, 509 (Bankr. D. Minn. 1993), aff'd, No. 3-93-512, 1994 WL 526013 (D. Minn. Jan. 20), aff'd,

categories of claims.⁹¹ At a minimum, however, the plan must "clearly evince the debtor's intent to reserve claims," and not just be a "mere blanket reservation[]." ⁹² Failure of a debtor to properly reserve claims under a plan of reorganization may preclude the liquidating trustee from recovering on such claims post confirmation.⁹³ For instance, a litigation trustee in one case was precluded from pursuing breach of fiduciary duty claims because the plan, by its terms, transferred to the trust only bankruptcy avoidance claims.⁹⁴ Identification of the potential targets of estate claims in the plan also is important. Indeed, one court held that a trustee had no standing to pursue malpractice claims against the debtor's pre-petition auditor because the plan reserved to the trustee only claims against the debtor's "current or former directors and officers."⁹⁵

The second requirement under § 1123(b)(3) is that, "if the person seeking to enforce the claim is a stranger to the estate, the person must be appointed and be a representative of the estate."⁹⁶ Whether a person is a proper "representative of the estate" is determined using a "case-by-case analysis,"⁹⁷ but the "primary concern is whether a successful recovery by the appointed representative would benefit the debtor's estate and particularly...the debtor's unsecured creditors."⁹⁸ The third and most obvious requirement of § 1123(b)(3) is that the "[t]he claims that are being reserved by the plan for later enforcement and adjudication must belong to the estate of the debtor' because 'the plan may only preserve those claims that a trustee in bankruptcy, or a debtor in possession, could have asserted prior to confirmation."⁹⁹

Indeed, in In re Premium Escrow Services, Inc., the court emphasized the importance of the distinction between estate and non-estate claims with respect to bankruptcy jurisdiction. "If a litigation trust prosecutes a cause of action that did not belong to the debtor or the debtor's estate prior to confirmation, that cause of action

⁹¹ 39 F.3d 898 (8th Cir. 1994); Paramount Plastics, Inc. v. Polymerland, Inc. (In re Paramount Plastics, Inc), 172 B.R. 331, 335 (Bankr. W.D. Wash. 1994)).

⁹² In re Kmart Corp., 310 B.R. at 121 (citing In re USN Commc'ns, Inc., 280 B.R. 573, 591, 593 (Bankr. D. Del. 2002) (upholding general reservation with respect to claims transferred to a liquidating trust); In re Ampace Corp., 279 B.R. 145, 156-62 (Bankr. D. Del. 2002)).

⁹³ In re Kmart Corp., 310 B.R. at 124. Plan provisions that identify causes of action by type or category are not mere blanket reservations. See id. (citing D.A. Bergner & Co v. Bank One, Milwaukee, N.A. (In re Bergner & Co.), 140 F.3d 1111 (7th Cir. 1998)).

⁹⁴ See, e.g., Astropower Liquidating Trust v. Xantrex Tech., Inc., 335 B.R. 309, 323-24 (Bankr. D. Del. 2005).

⁹⁵ Zahn v. Yucaipa Capital Fund (In re Almac's, Inc.), 202 B.R. 648 (D.R.I. 1996).

⁹⁶ Rahl v. Bande, 328 B.R. 387, 399 (S.D.N.Y. 2005).

⁹⁷ In re Premium Escrow Services, 342 B.R. at 400 (citation omitted).

⁹⁸ Id. (quoting McFarland v. Leyh (In re Tex. Gen. Petroleum Corp.), 52 F.3d 1330, 1335 (5th Cir. 1995)).

⁹⁹ Id. (quoting Citicorp Acceptance Co. v. Robinson (In re Sweetwater), 884 F.2d 1323, 1327 (10th Cir. 1989)). There has been uncertainty whether a creditors § committee may be afforded standing to prosecute estate claims pre-confirmation. See, e.g., In re Cybergenics Corp., 330 F.3d 548 (3d Cir.) (en banc), cert. denied, 124 S.Ct. 530 (2003). There appears to be less ambiguity with respect to the standing of litigation trustees in light of the explicit statutory authorization of post-confirmation estate representatives provided by § 1123(b)(3). But see Robert M. Quinn, Not So Fast, Mr. Liquidating Trustee, 22-APR Am. Bankr. Inst. J. 28 (2003).

belongs to the litigation trust personally rather than in its capacity as representative of the debtor's estate. As a personal cause of action rather than a cause of action wielded on behalf of the estate, such a claim is not subject to a court's jurisdiction under 28 U.S.C. § 1334."¹⁰⁰

There are several courts that have considered these and related jurisdictional matters in the context of liquidating plans. For example, in In re Railworks Corp., the plan of reorganization provided for a litigation trust to be established for the benefit of a class of unsecured creditors. The claimants were to receive shares of stock in the reorganized company and a pro rata share of the proceeds from the litigation trust. The debtor turned over to the litigation trust the rights to pursue certain causes of action. The trustee of the trust filed various causes of action under § 544 and various state fraudulent conveyance statutes. The defendants claimed, however, that the trustee did not have standing and that the bankruptcy court did not have post confirmation jurisdiction over the claims.¹⁰¹

In holding that the bankruptcy court had post-confirmation jurisdiction over the litigation trust claims, the court found that the payment to unsecured creditors from the proceeds of the litigation trust "falls squarely in the realm of limited jurisdiction that a bankruptcy court may hear. In addition, this type of proceeding, avoidance of a fraudulent transfer, is deemed a core proceeding under the Bankruptcy Code."¹⁰² However, the court noted that even if it were not a core proceeding, the bankruptcy court would have had jurisdiction. Adopting the Third Circuit's approach, "[t]he essential inquiry appears to be whether there is a close nexus to the bankruptcy plan or proceeding sufficient to uphold bankruptcy court jurisdiction over the matter."¹⁰³

In holding that the bankruptcy court had post-confirmation jurisdiction, the court distinguished its case from Resorts International. In Resorts International, the plan of reorganization established a litigation trust whereby the debtor turned over certain litigation claims to the trust. Pursuant to the trust agreement, the trust was permitted to hire an accounting firm to conduct an audit and provide certain tax related services. The trustee of the trust later alleged that the accounting firm committed malpractice in connection with the services it had provided to the trust.

The trustee therefore brought an adversary proceeding in the bankruptcy court against the accounting firm. The accounting firm moved to dismiss, claiming that the bankruptcy court did not have jurisdiction. Applying the "close nexus" test, the court found that "this proceeding lacks a close nexus to the bankruptcy plan or proceeding and affects only matters collateral to the bankruptcy process."¹⁰⁴ In particular, the court explained that the malpractice claims will have no effect on the estate, "will have only incidental effect on the reorganized debtor," and "will not interfere with the

¹⁰⁰ Id. at 399.

¹⁰¹ In re Railworks Corp., 325 B.R. at 394-95.

¹⁰² Id. at 723.

¹⁰³ Id. (quoting In re Resorts Int'l, Inc., 372 F.3d at 166-67).

¹⁰⁴ In re Resorts Int'l, Inc., 372 F.3d at 169.

implementation of the Reorganization Plan."¹⁰⁵

In Railworks Corp., by contrast, the fraudulent conveyance actions that the trustee was pursuing were pre-petition claims that originally were part of the bankruptcy estate. Thus, these claims were part of the bankruptcy court's core jurisdiction and they affect the "implementation, execution or administration of a confirmed plan."¹⁰⁶ The claims at issue in Resorts International, on the other hand, only arose post-confirmation from conduct between the accounting firm and the trust. These were not claims that were originally held by the debtor pre-petition. Thus, permitting post-confirmation jurisdiction over such claims could "open[] the specter of unending jurisdiction."¹⁰⁷

Another important consideration in the context of litigation trusts is what tools the trustee may use to investigate and pursue estate claims. For instance, can it use Rule 2004, even though litigation is contemplated pursuant to which only the traditional discovery tactics may be used? In a decision that may constitute the high water mark in this area, the District Court for Southern District of Georgia in In re Friedman's recently held that a creditors trust may pursue Rule 2004 subpoenas originally issued by the debtor pre-confirmation.¹⁰⁸ Although Rule 2004 examinations are primarily used in pre-confirmation discovery, the Court explained that "it is also true that courts often authorize Rule 2004 examinations *post*-confirmation."¹⁰⁹

Indeed, the confirmation order specifically authorized the trustee of the creditors' trust to enforce Rule 2004 subpoenas previously issued by the debtor. The Court concluded that the enforcement of such subpoenas was "critical to compliance with, and execution of, the plan."¹¹⁰ Thus, the Court concluded that it had post-confirmation jurisdiction over the 2004 subpoenas because such subpoenas had a "close nexus" to the implementation of the plan. This ruling recently was appealed to the Eleventh Circuit, where the matter remains pending.

C. Enforcement of Arbitration Clauses

Another particularly important issue respecting litigation trusts is whether post-confirmation jurisdiction may be asserted over trust claims that arose out of prepetition agreements requiring any such claims to be arbitrated. The issue of whether arbitration agreements are enforceable in bankruptcy is not new or novel,¹¹¹ although there are very few decisions addressing the matter in the context of litigation trusts. The general rule is that when a bankruptcy court is faced with a "non core" proceeding pre-

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Id.

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In re Railworks Corp., 325 B.R. at 723.

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Id.

¹⁰⁸

See Ernst & Young LLP v. Cohen (In re Friedman's Inc), No. 406CV024, slip op. at 6-7 (S.D. Ga. June 21, 2006).

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Id. at 7 (citing In re Daisytek, Inc., 323 B.R. 180, 185-86 (N.D. Tex. 2005); In re Express One Int'l, Inc., 217 B.R. 215 (Bankr. E.D. Tex. 1998)).

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Id. at 6.

¹¹¹

For one of the earliest, comprehensive discussions of the issue and pertinent case law, see Fred Neufeld, Enforcement of Contractual Arbitration Agreements Under the Bankruptcy Code, 65 Am. Bankr. L.J. 525 (1991).

confirmation that is governed by an arbitration agreement, the court must enforce the arbitration clause and not decide the matter itself. However, in a "core" proceeding, the bankruptcy court must determine whether enforcement of the provision would undermine a substantial purpose of the bankruptcy code.¹¹²

The matter can become confusing in the post-confirmation context, especially if a trust pursues both core and non-core claims. For instance, in In re Astropower Liquidating Trust, the liquidating trust brought various fraudulent transfer claims as well as breach of contract and breach of fiduciary duty claims arising from certain pre-petition stock transfers.¹¹³ Certain defendant's moved to dismiss based upon an arbitration clause in the underlying shareholder agreement. Explaining that the fraudulent transfer actions "are creatures of statute, available in bankruptcy only for the benefit of creditors of the debtor," the court held that "this Court may not require fraudulent conveyance actions . . . to be submitted to arbitration."¹¹⁴ However, the other "non core" cause of action were subject to the arbitration provision because "enforcement of arbitration provisions as to non-core claims is mandatory, not discretionary."¹¹⁵ The trust, therefore, had no choice but to pursue its claims in two separate proceedings.

In In re Friedman's, the plan and disclosure statement described the claims that were transferred to the trust, including possible malpractice claims against the debtor's pre-petition auditor. When the auditor sought to quash Rule 2004 subpoenas that were being pursued by the litigation trustee, it argued that any such claims were subject to mandatory arbitration pursuant to an arbitration clause contained in the auditor's pre-petition engagement agreement with the debtor. The Bankruptcy Court denied that auditor's motion to quash, and the District Court affirmed on appeal, reasoning that since no formal claims had yet been asserted by the trustee, there was no way to know what specific types of claims may be at issue and, hence, whether they were arbitrable.¹¹⁶ The District Court noted that this was a novel issue, i.e., whether a bankruptcy court can refuse to enforce a pre-petition arbitration provision if "'there is no way to determine' the nature of the underlying proceeding."¹¹⁷ As noted above, this "novel" issue is now on appeal to the Eleventh Circuit.

D. Conclusion

In sum, many courts agree that bankruptcy jurisdiction contracts once a plan is confirmed and a debtor emerges from chapter 11. A court nonetheless will exercise continuing jurisdiction over any matter that has a "close nexus" to the bankruptcy proceedings. Such a nexus should be found with respect to liquidating trusts,

¹¹² See generally In re U.S. Lines Inc., 197 F.3d 631, 641 (2d Cir. 1999); Ins. Co. of N. Am. v. NGC Settlement Trust & Asbestos Claims Mgmt. Corp. (In re Nat'l Gypsum Co.), 118 F.3d 1056 (5th Cir. 1997).

¹¹³ Astropower Liquidating Trust v. Xantrex Tech., Inc., 335 B.R. 309 (Bankr. D. Del. 2005).

¹¹⁴ Id. at 326 (citing Hays & Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 885 F.2d 1149, 1154 (3d Cir. 1989)).

¹¹⁵ Id.

¹¹⁶ See In re Friedman's, slip op. at 8.

¹¹⁷ Id. at 9 (citation omitted).

but so long as they are established in conformity with § 1123(b)(3) of the Code. Practitioners must take care to describe with reasonable specificity the causes of action transferred to the trust in order to avoid later litigation regarding whether they were properly reserved. And notwithstanding efforts to retain bankruptcy jurisdiction over all estate claims, courts likely will enforce arbitration agreements with respect to state law, non-core claims. Litigation trustees, therefore, must consider the potential ramifications of proceeding in bankruptcy court versus arbitration and the possibility that core and non-core claims may have to be pursued in separate forums.

V. Appeals of Confirmation Orders

Bankruptcy appeals are governed by a complex web of statutes, rules and court rulings (many of which conflict). The discussion of bankruptcy appeals in this paper, therefore, provides a very brief overview that focuses only on three discrete issues that are especially relevant to chapter 11 plan confirmation and related proceedings: (i) recent statutory changes concerning the circumstances under which appeals may be had to the Courts of Appeals; (ii) determinations of which orders are final and hence, may be appealed as of right; and (iii) stays of confirmation orders and the circumstances under which appeals of such orders may be rendered moot.

A. Appeals to the Courts of Appeals

A party appealing from an order of a Bankruptcy Court may appeal as of right either to the District Court or any Bankruptcy Appellate Panel organized for the Circuit in which the Bankruptcy Court sits.¹¹⁸ Further appeals from either the District Court or Bankruptcy Appellate Panel, as applicable, may be taken to the appropriate Court of Appeals.¹¹⁹ Of course, there may be circumstances under which a District Court exercises original jurisdiction over plan confirmation proceedings, in which case any appeal from the District Court's ruling must be directly to the Court of Appeals. However, since the great majority of plan confirmation hearings are conducted by Bankruptcy Courts in the first instance, there are two levels of appeal as of right as outlined above.

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "BAPCPA") provides a mechanism whereby Bankruptcy Court orders may be appealed directly to the Court of Appeals, thereby skipping intermediate appellate review by the District Court or any Bankruptcy Appellate Panel. Direct appeals to the Court of Appeals may be pursued in this fashion only upon certification either of (i) the lower court or (ii) all appellants and appellees that (a) the order "involves a question of law as to which there is no controlling decision of the court of appeals for the circuit or of the Supreme Court of the United States, or involves a matter of public importance"; (b) the order "involves a question of law requiring resolution of conflicting decisions"; or (c) immediate appeal to the Court of Appeals "may materially advance the progress of the

¹¹⁸ See 28 U.S.C. § 158(a).

¹¹⁹ See *id.* § 1291.

case or proceeding in which the appeal is taken."¹²⁰

The new statute requires that any request for certification be made not later than 60 days after the entry of the judgment, order, or decree. There is nothing in the statute to suggest, however, that the normal rules relating to the deadlines for appeals have been altered. Since appeals from Bankruptcy Court orders must be filed within 10 days of entry of the judgment,¹²¹ practitioners considering requesting certification should file a timely notice of appeal to preserve their appellate rights pending any court consideration of their certification request.

B. Finality of Orders

A party may appeal as of right only from a final order of a Bankruptcy Court.¹²² Non-final, interlocutory orders may be appealed only with permission of the appellate court if there is a controlling question of law, exceptional circumstances, or a disputed standard of review.¹²³ Courts agree, however, that the standard of "finality" is more relaxed in bankruptcy proceedings, with the result that a Bankruptcy Court may enter numerous "final" orders throughout the course of a chapter 11 case, long before it considers confirmation of any plan.¹²⁴ As a general matter, a bankruptcy order is final if it completely disposes of a parties' dispute, leaving nothing left for further consideration by the court.¹²⁵

Some courts, however, determine whether a Bankruptcy Court order is final by consideration of several factors, including the extent to which the order leaves the Bankruptcy Court with nothing to do but execute the order; the extent to which delay in obtaining review of the order would prevent an aggrieved party from obtaining effective relief; and the extent to which later reversal of the issue would require recommencement of the entire proceeding.¹²⁶ Other courts consider the impact of the order on the bankruptcy estate; the need for further fact-finding on remand; the preclusive effect of a decision on the merits; and the interests of judicial economy.¹²⁷

It is likely because of multi-factor tests such as these that some courts have commented that in the bankruptcy context, finality determinations are "far from straightforward."¹²⁸ Fortunately for practitioners, there seems to be little dispute that an order confirming a chapter 11 plan of reorganization is final and hence may be appealed

¹²⁰ See *id.* § 158(d)(2).

¹²¹ See Fed. R. Bankr. P. 8002.

¹²² See 28 U.S.C. § 158(a)(1).

¹²³ See *id.* § 158(a); *In re WorldCom, Inc.*, No. M-47 HB, 2003 WL 21498904, *10 (S.D.N.Y. June 30, 2003).

¹²⁴ See, e.g., *Computer Learning Ctrs., Inc. v. Guberman*, 407 F.3d 656 (4th Cir. 2005); *In re Marvel Entm't Group, Inc.*, 140 F.3d 463, 470 (3d Cir. 1998); *Tex. Extrusion Corp. v. Lockheed Corp.*, 844 F.2d 1142, 1155-56 (5th Cir. 1988).

¹²⁵ See, e.g., *Faragalla v. Access Receivable Mgmt.*, 422 F.3d 1208, 1210 (10th Cir. 2005) (citation omitted).

¹²⁶ See, e.g., *In re Farmland Indus., Inc.*, 397 F.3d 647, 650 (8th Cir. 2005).

¹²⁷ See, e.g., *In re Armstrong World Indus., Inc.*, 432 F.3d 507, 511 (3d Cir. 2005).

¹²⁸ *Knupfer v. Lindblade* (*In re Dyer*), 322 F.3d 1178, 1186 (9th Cir. 2003).

by an aggrieved party as of right.¹²⁹ On the other hand, most courts have held that orders denying confirmation are not final unless the chapter 11 case also is either converted to chapter 7 or dismissed.¹³⁰ The theory is that absent conversion or dismissal, further efforts may be taken before the Bankruptcy Court to develop a confirmable plan, and that appellate consideration of orders denying confirmation will only interrupt these efforts and will not advance the underlying case.¹³¹

However, it is not unheard of for an appellate court to determine that an order denying confirmation is a final order that may be appealed as of right. The Third Circuit in the Armstrong decision held that the District Court's order denying confirmation of the give-up plan was final, primarily because the issue on appeal was relatively discrete and would provide significant guidance to the parties in pursuing efforts to construct a viable plan.¹³²

Of course, there are other orders that a Bankruptcy Court may need to enter in anticipation of plan confirmation proceedings. At a minimum, there must be an order approving a disclosure statement.¹³³ Courts generally hold, however, that an order denying approval of a disclosure statement is not a final order that may be appealed as of right.¹³⁴ But other orders, such as orders approving substantive consolidation of multiple estates antecedent to court consideration of a reorganization plan for all the estates, have been held to be final that may be appealed.¹³⁵

C. Stays and Mootness

A confirmation order is not final, and execution of the plan is stayed, until 10 days after entry of the order on the Bankruptcy Court's docket.¹³⁶ This automatic 10-day stay, however, may be waived by order of the Court. Thereafter, a debtor is free to implement the plan. A party may obtain an additional stay of implementation of the plan only upon motion to the Bankruptcy Court in the first instance, and only if the Court finds that a stay is warranted in light of the likelihood of success on appeal, the relative harms to the parties, and the public interest, and only if the appellant posts a bond or if

¹²⁹ See, e.g., In re Adelpia Commc'ns Corp., 333 B.R. 649, 656 (S.D.N.Y. 2005); Kham & Nate's Shoes No. 2, Inc. v. First Bank of Whiting, 908 F.2d 1351, 1354-55 (7th Cir. 1990); see also Fed. R. Bankr. P. 8002(c)(1)(F).

¹³⁰ See, e.g., Lievsay v. W. Fin. Sav. Bank, 118 F.3d 661 (9th Cir. 1997); Flor v. BOT Fin. Corp., 79 F.3d 281, 283 (2d Cir. 1996); WCI Steel, Inc. v. Wilmington Trust Co., 338 B.R. 1 (N.D. Ohio 2005) (citing cases).

¹³¹ Pleasant Woods Assoc. Ltd. P'ship v. Simmons First Nat'l Bank, 2 F.3d 837 (8th Cir. 1993); WCI Steel, 338 B.R. at 9.
¹³² 432 F.3d at 511.

¹³³ See 11 U.S.C. § 1125(b).

¹³⁴ See, e.g., Adams v. First Fin. Dev. Corp., 960 F.2d 23, 26 (5th Cir. 1992); Tex. Extrusion Corp. v. Lockheed Corp., 844 F.2d 1142, 1156 (5th Cir. 1988); In re Adelpia Commc'ns Corp., 333 B.R. 649, 657 (S.D.N.Y. 2005); In re WorldCom, Inc., No. M-47 HB, 2003 WL 21498904 (S.D.N.Y. 2003) (providing extended discussion and analysis of cases). But see In re Pac. Gas & Elec. Co., 280 B.R. 506, 509-10 (N.D. Cal. 2002) (certifying appeal from order denying adequacy of disclosure statement in light of importance of issue raised by plan of preemption of state laws).

¹³⁵ See In re Owens Corning, 419 F.3d 195 (3d Cir. 2005) (substantive consolidation).

¹³⁶ See Fed. R. Bankr. P. 3020(e).

there is other protection afforded the non-appealing parties on account of the delay occasioned by the appeal.¹³⁷ Generally, it is exceptionally difficult to obtain a stay.

An appeal from an unstayed confirmation order may be rendered moot and hence, dismissed, if the plan is carried into effect by the debtor. This rule is rooted in a strong public policy favoring "finality of bankruptcy confirmation orders."¹³⁸ In accord with this policy, a confirmation order, "once implemented, should be disturbed only for compelling reasons."¹³⁹ Despite this policy, courts typically consider whether an appeal from a confirmation is moot by examining a series of equitable factors, with the result that the determination of mootness is not as predictable as it should be for reorganizing debtors, their lenders and other stakeholders who frequently have millions of dollars and jobs at stake.

For instance, some courts have determined whether an appeal from a confirmation order is moot by examining whether a stay has been obtained; whether the plan has been "substantially consummated"; and "whether the relief requested would affect either the rights of parties not before the court or the success of the plan."¹⁴⁰ Other courts consider these factors, plus whether the relief requested would affect the success of the plan and the public policy of giving finality to bankruptcy judgments.¹⁴¹ The "substantial consummation" consideration is drawn from the definition of the term contained in § 1101(2) of the Code 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 distribution under the plan."¹⁴²

It is not always clear which of these factors, if any of them, takes precedence.¹⁴³ Indeed, some courts seem to suggest that the failure of an appellant to obtain a stay could be fatal, stating that an appellant must "make every effort" to obtain a stay or else the appeal runs the risk of being dismissed as moot.¹⁴⁴ Others have clearly said, however, that the failure to obtain a stay is not, in and of itself, determinative.¹⁴⁵ Moreover, others have held that substantial consummation of the plan will not necessarily

¹³⁷ See Fed. R. Bankr. P. 8005.

¹³⁸ In re Continental Airlines, 91 F.3d 553, 565 (3d Cir. 1996); see also Manges v. Seattle-First National Bank, 29 F.3d 1034, 1039 (5th Cir. 1994) (citing First Union Real Estate Equity and Mort. Inv. v. Club Assoc., 956 F.2d 1065, 1069 (11th Cir. 1992)).

¹³⁹ In re UNR Indus., Inc., 20 F.3d 766, 769 (7th Cir. 1994) (citing various cases supporting this proposition).

¹⁴⁰ Bank of Montreal v. Official Comm. of Unsecured Creditors (In re Am. Homepatient, Inc.), 420 F.3d 559, 563 (6th Cir. 2005) (quoting Manges, 29 F.3d at 563).

¹⁴¹ In re Continental Airlines, Inc., 91 F.3d at 560.

¹⁴² 11 U.S.C. § 1101(2).

¹⁴³ See, e.g., MAC Panel Co. v. Va. Panel Corp., 283 F.3d 622, 625 (4th Cir. 2002); Nordhoff Invs., Inc. v. Zenith Elecs. Corp., 258 F.3d 180, 185 (3d Cir. 2001); In re Continental Airlines, Inc., 91 F.3d at 560 In re Club Associates, 956 F.2d 1065, 1069 (11th Cir. 1992).

¹⁴⁴ Nordhoff Invs., Inc., 258 F.3d at 187 (citing various cases).

¹⁴⁵ In re Am. Homepatient, Inc., 420 F.3d at 563 (quoting City of Covington v. Covington Landing Ltd. P'ship, 71 F.3d 1221, 1225 (6th Cir. 1995) (citing Manges v. Seattle-First Nat'l Bank, 29 F.3d 1034, 1039 (5th Cir. 1994))).

render an appeal moot; indeed, some courts have said that whether the plan has been consummated is "the foremost consideration,"¹⁴⁶ while other courts have said that whether the relief requested would affect the rights of parties not before the court was the "most important factor."¹⁴⁷

Notwithstanding these various tests and considerations, the main factor that influences courts' determinations of mootness appears to be the relative complexity of the reorganization transactions being appealed from, and whether they feasibly can be undone once they have been implemented.¹⁴⁸ Related to this point is the extent to which third parties not before the court have relied on implementation of plan transactions and the potential unfairness to them of a ruling that abrogates their expectations.¹⁴⁹ Thus, an appellate court likely will conclude that it is incapable of granting "effective relief" if it is faced with a complex restructuring involving hundreds or thousands of stakeholders that has long-since been implemented.¹⁵⁰ In such cases, courts typically find that it is "no longer prudent to upset the plan of reorganization."¹⁵¹

In sum, "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."¹⁵² As one court noted, when granting an appeal of a confirmation order "would require the bankruptcy court to traverse a totally impractical, perhaps impossible, course — one that might be as daunting as the reconstruction of Humpty Dumpty," the appeal will likely be denied.¹⁵³

¹⁴⁶ In re Continental Airlines, Inc., 91 F.3d at 560.

¹⁴⁷ In re Am. Homepatient, 420 F.3d at 564.

¹⁴⁸ In re Cont'l Airlines, Inc., 91 F.3d at 560-61 ("where the reorganization involves intricate transactions or where outside investors have relied on the confirmation of the plan" (citations omitted)); see also MAC Panel Co. v. Virginia Panel Corp., 283 F.3d 622, 625 (4th Cir. 2002).

¹⁴⁹ See In re Cont'l Airlines, 91 F.3d at 560-61.

¹⁵⁰ Compare Nordhoff Invs. Inc. v. Zenith Elecs. Corp., 258 F.3d 180, 185 (3d Cir. 2001) (appeal of confirmation order moot where plan would be difficult to unravel and had been relied on by various parties), with Platinum Capital, Inc. v. Sylmar Plaza, L.P. (In re Sylmar Plaza, L.P.), 314 F.3d 1070, 1074 (9th Cir. 2002) (appeal not moot, despite failure to obtain stay pending appeal and substantial consummation, where there was no "comprehensive change" in circumstances), and In re PWS Holding Corp., 228 F.3d 224, 236 (3d Cir. 2000) (appeal from confirmation order not moot where contested plan releases could be stricken without unraveling entire plan), and Lowenschuss v. Selnick, 170 F.3d 923, 933 (9th Cir. 1999) (plan did not contain complex transactions that would be difficult to unwind).

¹⁵¹ Bank of Montreal v. Official Comm. of Unsecured Creditors (In re Am. Homepatient, Inc.), 420 F.3d 559, 563 (6th Cir. 2005) (citing Guardian Sav. & Loan Ass'n v. Arbors of Houston Assocs. Ltd. P'shp., No. 97-2099, 1999 WL 17649, at *2 (6th Cir. Jan. 4, 1999)).

¹⁵² MAC Panel Co. v. Va. Panel Corp., 283 F.3d 622, 625 (4th Cir. 2002) (emphasis in original).

¹⁵³ Id. at 627.