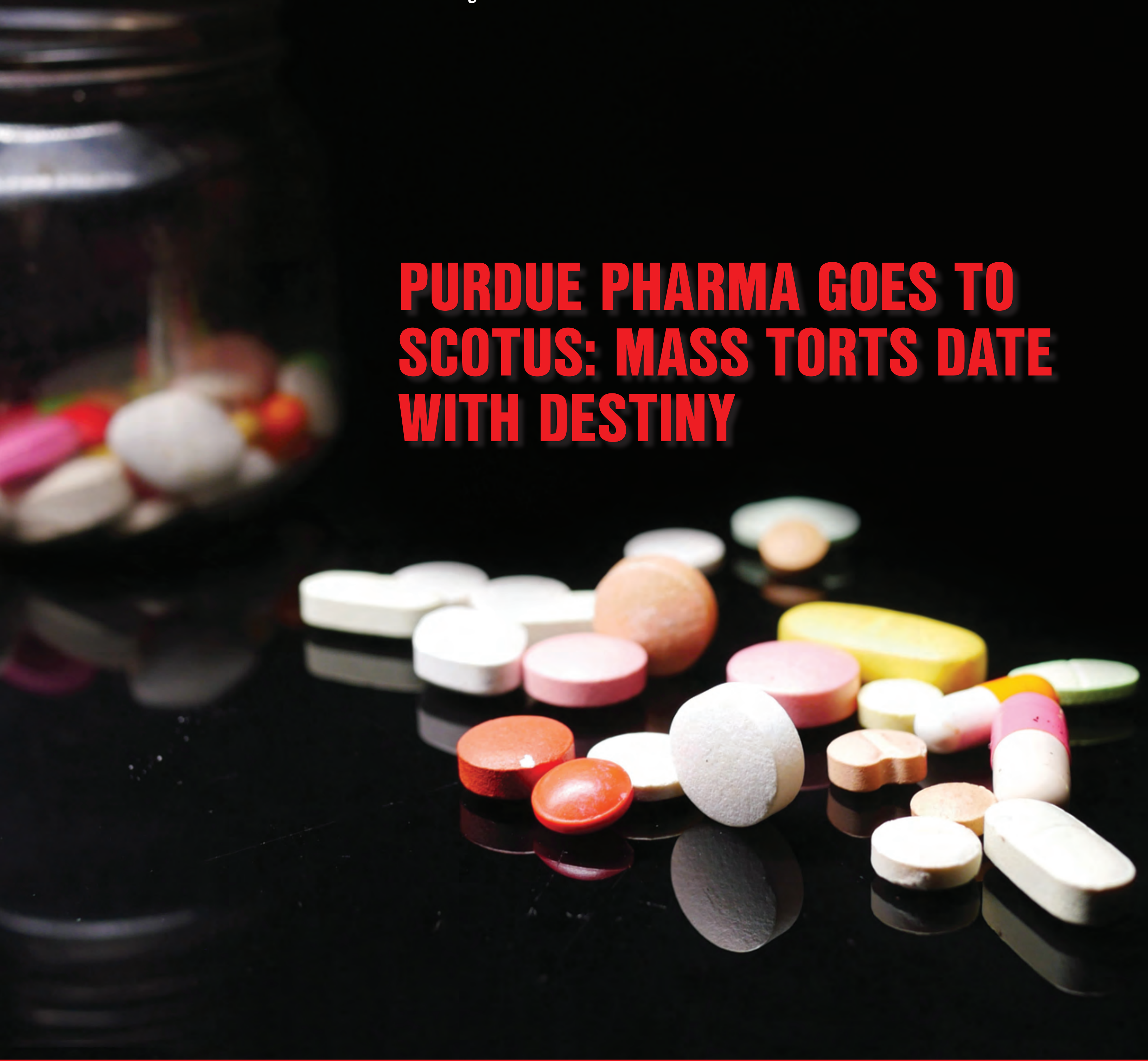
CLW
COMMERCIAL LAW WORLD MAGAZINE

JULY/AUGUST/SEPTEMBER 2023
VOL 37 / ISSUE 3

An Official Publication of the ***Commercial Law League of America***



PURDUE PHARMA GOES TO SCOTUS: MASS TORTS DATE WITH DESTINY

THE ANNUAL BANKRUPTCY ISSUE

FROM THE EDITOR

One of the reasons that I like working on the CLW is that it scratches an itch that I otherwise only occasionally get to scratch in my practice: the academic side of law. My practice is primarily creditors' commercial litigation; most days involve pleadings and discovery (and emails and zoom calls), but few days involve legal research into a new argument or novel legal theory. As a result, my day to day practice is a very long way away from what first got me interested in the law. It was not advocacy or argument, it was the opinions of the U.S. Supreme Court. Beginning with the seminal cases in constitutional law, I wasn't content to learn the summary of why *Marbury v. Madison* or Dred Scott was important, I liked reading the opinions. Concurrences and particularly dissents make for interesting reading as they highlight the ways in which these issues - which often seem cut-and-dried as initially written out by the majority - are not so clear-cut.

So I especially enjoy the Bankruptcy Issue of the CLW every year because it comes the closest to that academic interest, articles highlighting opinions that I've read and ones that I seek out and read once I see them mentioned. This issue features several such articles because it has been a banner year for important bankruptcy opinions. I am very fortunate to get to work with these writers, who are crafting the first draft of history.

The largest development is not an opinion yet, but the promise of one to come. For several years, we have been following the progression of mass tort cases through the bankruptcy system, and one of the largest is now headed to the Supreme Court. I have engaged in some spirited disagreements with my fellow bankruptcy practitioners about the legal propriety of the variety of procedural tactics pursued by the tort defendants - venue shopping, channeling injunctions, extending stay protection to non-debtor parties and non-consensual third party releases - and we will finally get to see whether the Court approves of wide-ranging use of Section 105, among other approaches.

My interest in these cases is primarily academic, but not exclusively so. Lawyers are, after all, prolific copycats; what proves effective in one case will get used in others. While the smaller cases that my creditor clients get dragged into seldom involve forum-shopping, the other tactics of the mass tort cases are coming for rest of us too. In the past couple of years, I have seen a motion to extend the stay in a Sub-V case to the principal of the debtor company, arguing that pursuit of collection on his guaranty of the business debt should be stayed because he should not be distracted by litigation from the apparently all-consuming task of running his company. Another business debtor attempted to engraft, onto an otherwise routine Chapter 11 plan, a general release of the principals of the company from "any and all obligations" related to the company, which presumably would have been argued to apply to guaranties, fraudulent transfers, malfeasance, deepening insolvency or any of the other theories under which corporate officers can be found liable for the debts of the companies they run into the ground. With *Purdue Pharma* on the docket for argument and decision in the current term, my academic interest could not be higher.

My guide along the twisting, halting yellow-brick road of mass tort bankruptcy cases has been Candice Kline, who has outdone herself with this issue's thorough review of how we got here and where mass tort bankruptcy may be going. Having read the decision in the first *LTL* case, I was interested to learn that LTL II had been rejected, and promptly pulled up the Order in that case to see what had changed (and more importantly for LTL, what had not).

Also of interest this year is the *Bartenwerfer* decision from the Supreme Court, holding that the fraud exception to dischargeability does not always require that the debtor be an active participant in the fraud. Discussed here by Ron Peterson and Breana K. Drozd, the *Bartenwerfer* decision has generated significant interest among creditors' attorneys. We shall soon be seeing multiple cases applying *Bartenwerfer,* which may turn out to be the most significant Chapter 7 case in years.

Finally, I would be remiss if I did not mention that Ron Peterson was awarded the President's Cup by the CLLA this last year, in recognition of his outstanding contributions to bankruptcy law and practice and our organization over the years. His annual case law updates are my favorite program during the League's National Conference, and the article we get to include here is merely the latest evidence that he is truly a worthy recipient of this honor. ■

Beau Hays
Co-Chair of the Board of Associate Editors

Beau

IN THIS ISSUE

JULY/AUGUST/SEPTEMBER 2023 | VOL 37 / ISSUE 3

LEAGUE VIEWS

INDUSTRY INFORMATION

FROM THE 2023-2024 PRESIDENT

THE POWER OF POSITIVE THINKING

As I begin my journey as the President of the CLLA, it occurs to me that, even though Jim Kozelek was a fantastically great President, as were Chris Young, Tim Wan, Lorna Walker and all the Presidents that preceded me, a new Presidential term is a time for reflecting on the future and the positive things that can come from that. For us, as lawyers and non-lawyers in the legal profession, however, thinking positively can be a difficult thing to do.

As many of us know, lawyers see the world a bit differently than other people do. I have spoken with CEOs, CFOs, venture capitalists, entrepreneurs, and many other business people outside of the legal profession, and many of them, if not most of them, tend to be very positive about their ideas and future plans, if not downright idealistic about them. Not us. No way. You see, we live our lives in the world of the 2%. No, not that 2%, a different 2%. I have always said, in the world, things go the way they are supposed to go 98% of the time. And 2% of the time, things go sideways. And those of us in the legal profession live 100% of our professional lives in that sideways 2%. OK, maybe those percentages are not exactly a scientific representation of the precise ratio, but you get my point. The constant exposure to the realization of the worst-case scenario skews our world view on how frequently that scenario actually comes to fruition. And that world view bleeds through to various aspects of our existence, manifesting itself as skepticism, negativity, cautiousness, doubt, pessimism, cynicism, or perhaps even as much as depression, despair, or melancholy.

Which is why we must consciously reject that negativity and think positively. Be creative. Be hopeful. Be idealistic. Look at things with a different eye. Life is good. This is such a good time to think about where we are, what we have, and what we can do in the future together. The Commercial Law League of America is the preeminent commercial law organization in the United States (dare I say even in the world). And we are fortunate to be a part of it. And the world, as they say, is our oyster.

Let's take stock in what the League provides for us: professional development, education, fellowship, networking, experience and so much more. And there is even more out there that we can cultivate. So, if you find yourself disengaged, uninvolved, bored, or even questioning your membership in the League, hit reset and remind yourself of all the things the League has to offer. Pick something to get involved with or re-engage with something new. Don't just think about what you can get from the League. Think about what you can give to it. Give a part of yourself – time, talent, or treasure – you choose.

Join a committee. There are several standing committees that you could be involved with – Education, Meetings, or Marketing and Membership. Or maybe Government Affairs is more your speed. Perhaps you could apply your advocacy skills to advocate for our League and our industry. Take part in Hill Day. Or if that is not your cup of tea, donate to the PAC fund to help others advocate for the League. Or come to a meeting, or a few meetings. You could check out a regional meeting or the National Conference. Or if you can't make it there in person, be a Sponsor, or a Champion.

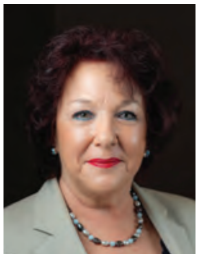
Or maybe you are interested in something new? Now is the time to think outside the box. During my term, I am creating a Diversification Task Force to look at new and different ways to engage with the community and legal profession at large. So, if you have ideas, or want to help explore new and different ways to grow the League, I encourage you to jump on in. The water is fine!

Embrace the positivity. Lean into the future and all of the excitement that comes with it. These are great times and getting greater. Each and every member in the League is an integral part of our collective success. We have the momentum. We have the energy. Let's seize the power of positive thinking and make it happen...together! ■

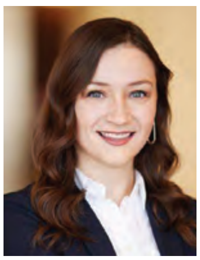
Bill Thrush, Esq.
2023-2024 CLLA President
Weinstock, Friedman & Friedman, P.A.

OUR TEAM 2023-2024

CONTRIBUTORS



Wanda Borges, Esq.
Principal Member
Borges and Associates, LLC
Wanda is the principal member of Borges & Associates, LLC, a law firm based in Syosset, NY. For more than 40 years, Ms. Borges has concentrated her practice on commercial litigation and creditors' rights in bankruptcy matters, representing corporate clients and creditors' committees throughout the United States in Chapter 11 proceedings, out-of-court settlements, commercial transactions and preference litigation. **borgeslawllc.com**



Breana Drozd
Associate
Jenner & Block, LLP
Breana Drozd helps debtors, creditors, and corporate entities navigate complex bankruptcy litigation. She also plays a key role in advising financially distressed clients in chapter 11 corporate restructuring matters. In addition to her bankruptcy work, Breana has experience in commercial litigation and other investigative matters. Breana brings a variety of civil litigation experience to her practice. As an intern for the Honorable James D. Peterson of the Western District of Wisconsin, she gained insight into the justice system from the perspective of a judge. As a member of her law school's Moot Court Board, Breana and her partner won the Best Brief award and were national semifinalists in the Chicago Bar Association's 2019 Moot Court Competition. She also received four awards for earning the top grade in her Administrative Law, Bankruptcy Law, Equal Employment Law, and Federal Jurisdiction courses. Breana serves as a member of the firm's Associates Committee. **jenner.com**

Peter M. Gannott
Attorney, *Gannott Law Group PLLC*
Peter M Gannott graduated with honors from the University of Illinois with degrees in History and Political Science and obtained his law degree from the Washington College of Law, American University, in Washington, D.C. His practice focuses on business and consumer bankruptcy, creditors' rights and commercial litigation and complex commercial, business and real estate litigation. He is licensed to practice in the state courts of Kentucky and Indiana, and admitted before ten district courts, three circuit courts and the U.S. Supreme Court. **gannottlaw.com**

Amy M. Kiser, Esq.
Partner, *Gilbert Garcia Group, P.A.*
Amy Kiser is admitted to the Florida Bar (2007), Middle District of Florida (2013), Northern District of Florida (2013), and Southern District of Florida (2013). She matriculated at the University of South Florida Honors College (B.A. Political Science, 2004), and Stetson University College of Law (J.D., 2007, Advocacy Board Member). Amy joined Gilbert Garcia Group in 2013, bringing years of experience representing clients in real estate and corporate transactions, probate, and estate planning. As partner, Amy's practice focuses on representing creditors in all aspects of bankruptcy proceedings, and lenders in all aspects of foreclosure matters. She is a regular contributor to industry publications, as well as the firm's newsletters and website. Amy is a passionate community advocate; she enjoys volunteering with local charities and providing pro bono legal services.
gilbertgrouplaw.com

Candice Kline, Esq.
Partner, *Saul Ewing LLP*
Candice advises clients on bankruptcy and corporate restructuring matters and related litigation. She represents debtors, trustees, official committees, investors and creditors in bankruptcy proceedings and out-of-court workouts. Her experience includes managing cases from $10 million to $13 billion, with key roles in large, complex Chapter 11 and 7 cases. She also handles Chapter 12 cases and has experience with cross-border insolvency Chapter 15 proceedings. **saul.com**

Ronald L. Peterson
Of Counsel
Jenner & Block, LLP
Ron Peterson is a prolific lecturer and writer on bankruptcy and commercial law issues. Rob served on the panel of the Chapter 7 Trustees for the Northern District of Illinois, Eastern Division, from 1989 to 2021. He is a member of INSOL and served on the Board of the National Association of Bankruptcy Trustees. He served as co-chair of the Avoidance Action Committee for the ABI's Commission on the Reform of Commercial Bankruptcy Law. Ron also recently completed a term on the Board of Governors of the Commercial Law League of America.
jenner.com

– Continued on page 6

WELCOME NEW MEMBERS | JULY/AUGUST/SEPTEMBER 2023

CALIFORNIA
Gary A. Bemis | Law Offices of Gary A. Bemis | Riverside, CA

FLORIDA
Scott Moore, Esq. | The Soto Law Group, P.A. | Fort Lauderdale, FL

ILLINOIS
Steve Victor | Development Specialists, Inc. | Chicago, IL

MARYLAND
Tom Gillespie | Access Receivables Management | Hunt Valley, MD
Emely Cruz, Esq. | Law Office of Emely Elizabeth, L.L.C. | Rockville, MD

NEBRASKA
Joseph Selde | BQ & Associates, P.C., L.L.O. | Omaha, NE

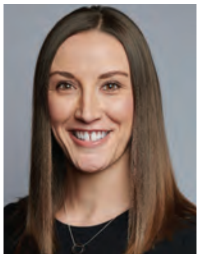
NEW JERSEY
Steven Mitnick, Esq. | S. Mitnick Law PC | Oldwick, NJ

NEW YORK
Sue Chin | Borges & Associates, LLC | Syosset, NY
Paul Vallario | BeeSeen Legal | Huntington, NY

PENNSYLVANIA
John Linarelli | University of Pittsburgh School of Law | Pittsburgh, PA
David Schlee | AG Commercial Law, LLC | Dickson City, PA

TEXAS
Liz Rios | Ryan & Jacobs | Plano, TX

 – *Continued from page 4*



Amy Pona
Director of Commercial Debt Collection, *Gurstel Law Firm P.C.*
Amy joined Gurstel's Consumer Collection Department in 2012, where she worked until 2015 when she transitioned to the Commercial Litigation Department (the "CLD") and was promoted to Director of that practice group in 2016. With Amy's stewardship, the CLD focuses on commercial civil litigation, pre-suit through post-judgment collection remedies. She also works closely with Gurstel's CEO and COO to develop new client relationships and enhance current client relationships, which include commercial collection agencies, local and national creditors, and other industry leaders. The aforementioned efforts have enabled Amy to expand the CLD into all of Gurstel's nine states of practice. **gurstel.com**

Emory Potter, Esq.
Partner, *Hays & Potter, LLP*
Emory Potter is a construction, commercial and civil litigation attorney with extensive trial experience. His specialties include materialmen's lien and construction bond work, creditor's rights, and commercial collections, handling a large volume of litigation from initiation of suit through post-judgment collection. **hpmlawatl.com**

Jack Rose
Partner, *The Law Offices of Jack J. Rose, PLLC*
Experienced leader with 30+ years advising top-level executives on critical issues. Extensive legal knowledge combined with strong business acumen developed over a 30-year career focused on distressed and special situations at large international law firms acting as lead counsel in significant international matters. A skilled collaborator, problem solver, and negotiator who can effectively communicate complex issues in a clear and concise manner, driving towards desired goals. Exceptionally skilled in risk assessment, leading complex restructuring transactions, negotiating settlements, and managing processes efficiently within budget and timeline. Proven leader who achieves outstanding results. All matters at the firm are personally overseen by Mr. Rose subject to the firm's standard staffing policies. **jackroselaw.com**

Timothy Wan, Esq.
Senior Partner and CEO
Smith Carroad Wan & Parikh
Timothy Wan, Esq. is Senior Partner and the Chief Executive Officer (CEO) of Smith Carroad Wan & Parikh. His areas of expertise include managing the creditor's rights and collection law practice, serving as General Counsel to various small businesses in the local business community and spearheading practice areas of entertainment law, music law, copyright and intellectual property. **smithcarroad.com**

CLW COMMERCIAL LAW WORLD MAGAZINE

An Official Publication of the Commercial Law League of America

Commercial Law World is published quarterly

CLLA COMMERCIAL LAW LEAGUE OF AMERICA
EXPERTISE • INSIGHT • RESULTS

TALES FROM THE FRONT, AT THE FRONT

PATIENCE FOR A TWELVEMONTH

I don't like to close out judgments as "uncollectible". Sure, sometimes the company is out of business, the owner/operator dies with no assets, and there is no successor company. That one can be closed. But if I have a judgment against an individual, I'll stay patient. A judgment in New York is valid for twenty years. Just because a judgment debtor appears to be judgment-proof at this time, they may not be forever. Think about where you were twenty years ago... Are you in the same financial position then as you are now?

A debtor, whom I shall refer to as "Fagin," was a miserly gentleman but one who acquired a great deal of wealth in the financial markets. Unfortunately, he fell victim to the financial crisis of 2008, Ponzi schemes, pick-pocketing, and losing his job. He couldn't pay the rent, and moved from his beautiful Gotham apartment (a two-bedroom apartment of the kind that sell for multiple seven-figures, and on which the monthly rent is more than some people's gross income for six months) to various hostels, one after another.

We were retained by the property owner, the Claridge, to sue on Fagin's rental arrears. We located him at the home of the Artful Dodger, commenced suit, served him personally in-hand, and obtained a judgment in 2009. We found no assets of any kind, but kept the matter in our inventory of cases, with our team checking for assets, or a viable address, every 180 days. And we did so, for 14 years.

In 2023, we located a bank account with over a hundred and sixty thousand dollars in it, and commenced the execution. Of course, Fagin brought an Order to Show Cause to vacate the judgment, on the basis of the inability to pay the rent, due entirely to the loss of his wages. Moreover, he admitted service, but said he had an inability to pay. Finally, he alleged that the amount was astronomically higher than the rent that he failed to pay.

Well, we had answers for all of those allegations. The loss of wages and inability to pay were not potentially meritorious defenses. And the higher amount was due to the compounding of 14 years of interest!

In response to our opposition papers, Fagin alleged that he was never served properly.

The Court's ruling was short and succinct. "Given the age of the case, Plaintiff would be at a grave disadvantage, and place an overwhelming burden of producing witnesses and evidence that are most likely no longer available... The Court would essentially be unfairly compensating Defendant for his abhorrent unexcused delay." The Court upheld our judgment and allowed us to execute.

Fagin had better go back to reviewing his situation ■

Timothy Wan, Esq.
Contributing Editor

FROM THE EXECUTIVE VICE PRESIDENT, CLLA

VIEWPOINT

Fall always ushers in a busy conference season for the League. We just wrapped up another successful Western Region Conference which was held in Anaheim, California on September 7 & 8, 2023. Robert Tyler, Law Offices of Gary A. Bemis, AC was elected as the new Chair of the Western Region and has set goals to increase both membership and membership participation in the regional conference next year. If you are in the Western Region look for a survey soon to begin planning for the 2024 conference.

Not to be outdone, the Eastern Region will hold its annual conference in New York City on November 8 & 9, 2023. The program will focus on the rise of artificial intelligence and its impact on both society and the practice of law and business. Cybersecurity will also be covered. We will be passing the gavel on to Chair Elect Joe Molinaro and will be honoring Wanda Borges as the recipient of the Warren Pinchuck Service Award. This award is bestowed upon a CLLA Eastern Region member in good standing based on their exemplary service and volunteerism to the CLLA.

We will also be honoring Judge Thomas Ambro at The Annual CLLA Luncheon & Hon. Frank Koger Memorial Educational Program at the NCBJ conference on Thursday, October 12th in Austin, TX. Judge Ambro will be receiving this year's Lawrence P. King Award. Each year, the Executive Council of the Commercial Law League's Bankruptcy Section presents the Lawrence P. King Award to recognize a lawyer, judge, teacher or legislator who exemplifies the best in scholarship, advocacy, judicial administration or legislative activities in the field of bankruptcy.

Finally, save the dates for the Southern Region Conference, February 9 & 10, 2024 at the Hotel Haya in Tampa, Florida and, of course, our 130th National Convention being held once again at the Swissotel in Chicago, Illinois on May 15 – 17. We look forward to seeing you at these events! ■

Phil Lattanzio
Executive Vice President

ABOUT US

Commercial Law World (ISSN 0888-8000) is published quarterly by the Commercial Law League of America®, 3005 Tollview Drive, Rolling Meadows, IL 60008, (312) 240-1400.

Please email your comments to the editor to editor@clla.org

ARE YOU ON SOCIAL MEDIA?

If not, follow CLLA to receive timely information on newsworthy topics, upcoming events, and now virtual meetings.

LIKE OR FOLLOW US ON

facebook.com/CommercialLawLeague/

twitter.com/CLLAInforms

linkedin.com/company/clla/

HEARD & OVERHEARD

The case of *Purdue Pharma* remains at the forefront of hot bankruptcy cases. The CLLA members are fortunate that we have among our ranks, several attorneys who have kept us abreast of all the activity in this case. Thank you to Candice Kline, Judge Judith Fitzgerald and Beverly Manne for your constant updates and educational programs. Most recently, these three members were joined by Professor Levitin of Georgetown University Law Center and Professor Organek of Baruch College to share differing views as to the real economic impact of nonconsensual third-party releases and whether the Supreme Court's decision will assure benefit or harm to mass tort victims and to the bankruptcy system overall. This issue of the CLW includes the latest article in the Purdue Pharma series by Candice. Since I live in Stamford, CT where Purdue Pharma is headquartered, articles addressing this case appear regularly in our local paper. And, Connecticut's Attorney General William Tong has become a strong advocate for the opioid victims pushing for more relief for the victims, reserving his rights to continue his opposition to third-party releases

Few CLLA members are involved directly with cases such as *Purdue Pharma*. Nevertheless, CLLA members are always willing to share information as to their involvement in cases across the country enabling our colleagues to use those cases in the matter in which they are involved. Just this week, I met with a fellow bankruptcy attorney in St. Louis. We are currently adversaries and had never met in person. Having the opportunity to do so, we spent over an hour discussing our pending case and other cases with which we are or were involved. His practice generally finds him representing consumer debtors or small business debtors. The case we are litigating involves the question of whether or not a default judgment based on fraud will hold up as collateral estoppel or res judicata in a chapter 13 proceeding. We will be seeking to bar the dischargeability of a debt. He will be seeking to pay our client as little as possible. While not entirely on point, our conversation on §523 discharges naturally led to a discussion of the recent SCOTUS decision in *Bartenwerfer*. Our case is pending in front of Bankruptcy Judge Kathy A. Surratt-States in the Eastern District of Missouri. Interestingly, her law clerk Kaila F. Spivey just published an article "After *Bartenwerfer*, What is an 'Honest Debtor'" in the ABI Journal, so there is no doubt that Judge Surratt-States' court is well-versed in dischargeability issues. Ron Peterson provides us with an insightful summary of the *Bartenwerfer* decision in his Supreme Court Case Review included in this issue of the CLW. It would have been nice to say that at the conclusion of our meeting, we shook hands on a settlement. Alas, that did not happen! Perhaps when our Missouri case is finalized, it will make for an interesting article in the CLW.

The St. Louis bankruptcy attorney had concluded a hearing that morning in which the Debtor had been jailed by the court for contempt. As we discussed his case, I informed him of bankruptcy cases [*Timothy McCallan* and *Allegro Law LLC*] in which I had been involved in the Middle District of Alabama in which Bankruptcy Judge William R. Sawyer had sent the Debtor to prison for over two years based on contempt of court. We discussed the similarities in our cases and my colleague had cited various of the McCallan decisions in his Missouri case. One of the values of CLLA membership is the ability to share personal case information with colleagues throughout the country. The legal issue you are dealing with in your case may already have been won (or lost) by a fellow CLLA member from whose experience you can gain perspective. ■

Wanda Borges, Esq.
Co-Chair of the Board of Associate Editors

Wanda Borges

CLLA IN ANAHEIM, CALIFORNIA

It was great to see the attendees at the Western Region Conference. It is a privilege to be elected as the new chair of the Region and I'm honored. It will be exciting to see how many new members we can add to the Western Region this year and I look forward to having as many of you as possible participate in helping us achieve this year's goals.

I have set as goals both an increase in membership and in participation in attending our next Western Region Conference. Information on locations and dates will be coming soon.

Robert Tyler

CLLA WESTERN REGION CONFERENCE

September 7-8, 2023

Westin Anaheim Resort

Candice L. Kline, Esq.
Partner
Saul Ewing LLP

PURDUE PHARMA GOES TO SCOTUS: MASS TORTS DATE WITH DESTINY

A handful of major mass tort bankruptcy cases are taking turns challenging the legal doctrines and practices that have made these cases possible under chapter 11. With *Purdue Pharma* now headed to the Supreme Court, and other cases on shaky ground, is the current practice of attempting to use bankruptcy to manage mass torts doomed? This sixth installment in our Mass Tort/Third-Party Releases Series discusses *Purdue Pharma* and recent developments in a few other mass tort cases.[1]

Taken together, mass tort reorganizations seem under threat, and the consequences could extend to other areas of practice currently viewed as routine such as exculpation clauses in chapter 11 plans, injunctions, and even asbestos cases permitted under Code section 524(g). With plaintiffs and the U.S. government pushing hard, courts are taking another look.

PURDUE PHARMA AND A NERVE – WRACKING TRIP TO SCOTUS

No other mass tort bankruptcy case has produced as much drama as *In re Purdue Pharma*, L.P. This opioid liability case involves millions of victims, billions in settlement funds, and deeply criticized third-party releases of the Sacker family that controlled *Purdue Pharma*. The Sacklers amassed an immense fortune while opioid victims, states, and municipalities have dealt with the negative impacts of the opioid crisis. Under the reorganization plan proposed by *Purdue Pharma*, the Sacklers and other nondebtors (many of whom paid nothing into the plan) would receive comprehensive releases of any potential opioid liabilities, among other liabilities, without ever having to file for bankruptcy protection themselves – in exchange for payment of several billion dollars. This reality has stirred enormous controversy.

To recap: the bankruptcy court approved *Purdue Pharma*'s first $4.5 billion settlement plan, which included nonconsensual third-party releases of the Sackler family, based on Second Circuit precedent and the practical result of a comprehensive settlement. Some dissenting parties appealed to the district court, which reversed the bankruptcy court's decision to confirm the plan.[2]

District Court Judge Colleen McMahon surprised most court watchers with her decision reversing the bankruptcy court (a somewhat rare appellate outcome) and her bold conclusion that nothing in the Bankruptcy Code permits the bankruptcy court to approve the third-party releases protecting the Sacklers.[3] She further concluded that the bankruptcy court lacked authority to issue a final order confirming the settlement plan under *Stern v. Marshall*, requiring a proposed findings of fact and conclusions of law to the district court for plan confirmation.[4]

Following that Order, *Purdue Pharma* and the Sacklers then quickly improved the settlement by agreeing to pay nearly $6 billion into the plan, garnering the support of the last appealing states and the District of Columbia (collectively called the "Nine") and again approved by the bankruptcy court.[5]

Connecticut's Attorney General William Tong captured his reluctant acceptance of the improved settlement: "This settlement is both significant and insufficient—constrained by the inadequacies of our federal bankruptcy code. But Connecticut cannot stall this process indefinitely as victims and our sister states await a resolution. This settlement resolves our claims against Purdue and the Sacklers, but we are not done fighting for justice against the addiction industry and against our broken bankruptcy code."[6]

The appeal resulted in the Sackler family improving the settlement offer, providing a better outcome than the original settlement approved by the bankruptcy court. The litigation process including appeals may better preserve creditor rights than the bankruptcy, even with its elaborate mediation rituals.

The bankruptcy court order approving the revised settlement was appealed and combined with an appeal of Judge McMahon's decision at the Second Circuit.[7] The most prominent of the appellees is the U.S. Trustee, the unit of the Department of Justice charged to oversee bankruptcy case administration as a "watchdog." Several pro se individual plaintiffs also oppose the plan and appealed.[8]

Court watchers waited anxiously for an opinion. When it finally dropped a year after oral argument, the Second Circuit reversed the district court and upheld plan confirmation. The industry exploded with

1 This article provides an overview of key issues and arguments and not an in-depth review of the voluminous filings and commentary in the cases discussed and the mass tort topic. Interested readers should stay tuned to further case developments through the CLLA's webinars and conferences, and subsequent articles in this long-running series.

2 See Candice Kline, *Are Nonconsensual Third Party Releases Headed to the Supreme Court?*, Commercial Law World (CLW) Magazine, Vol. 36, Issue 3 (2022).

3 Id.

4 Id.

5 The settling states that appealed and won an improved settlement were California, Connecticut, Delaware, Maryland, Oregon, Rhode Island, Vermont, and Washington. See Order Pursuant to 11 U.S.C. §§ 105 and 363(b) Authorizing and Approving Settlement Term Sheet, *In re Purdue Pharma L.P.,* Case No. 19-23649 (Bankr. S.D.N.Y. Mar. 10, 2022), Dkt. No. 4503. See also *In re Purdue Pharma, L.P.*, Case No. 22-110-bk (L) ("Purdue Op."), – F.4th – (2d. Cir. May 30, 2023), at 11-12, 38.

6 Press Release, at https://portal.ct.gov/AG/Press-Releases/2022-Press-Releases/AG-Tong-Compels-Purdue-and-Sacklers-to-Pay-Six-Billion-to-Victims-Survivors-and-States.

7 Purdue Op. at 12.

8 *Id.* at 12, 39. The pro se appellees are Ronald Bass, Ellen Isaacs, Maria Ecke, Richard Ecke, Andrew Ecke, the Estate of David Jonathan Ecke, and Peter Sottile. *Id.*

commentary and review. Some court observers cheered while others were critical and left wanting.[9]

SECOND CIRCUIT SPEAKS: THIRD-PARTY RELEASES PASS MUSTER

On May 30, 2023, the Second Circuit panel of Newman, Wesley, and Lee (writing for the court) reversed Judge McMahon and concluded that third-party releases of direct claims against nondebtors are allowed under Code sections 105 and 1123(b)(6), and case law precedent in the circuit.[10] The Court also relied on precedent and expanded its guidance to include a seven-factor test and applying the new test upheld the legality of nonconsensual third-party releases in chapter 11 plans.

The Second Circuit panel seemed persuaded by practical and equitable bankruptcy arguments that mass torts of this scale merit extraordinary remedies including third-party releases. Anything else will be costly, time-consuming, and ultimately harms victims.[11] The court acknowledged the serious harm caused by the opioid epidemic, propelled largely by *Purdue Pharma*'s OxyContin drug and its aggressive marketing activities.[12] Those activities made its owners, the Sacklers, multi-billionaires. The victims of the opioid epidemic, including states and municipalities burdened with the fallout, were left with litigation and the bankruptcy settlement on appeal.

The improved post-appeal settlement includes a grand bargain: $6 billion from the Sacklers to fund the settlement in exchange for a broad release of all direct claims related to *Purdue Pharma* and its conduct.[13] The deal releases most conceivable claims that parties would have against the Sacklers from opioid-related liabilities. The Sacklers get this release without ever having to seek bankruptcy protection themselves.

This outcome raises questions about a debtor's ability to buy a discharge even in situations involving wrongful conduct. It seems a remedy only available to the richest companies and individuals like the Sacklers. In a country with uniform bankruptcy laws,[14] this chapter 11 practice creates an appearance of endorsing a two-tier bankruptcy system, one for the biggest, most resourced cases and a second for everyone else. The bigger and more complex the case, the better the rewards. Courts have questioned an individual debtor's ability to "buy a discharge" in chapter 7 practice,[15] where exceptions to discharge include situations when the debtor incurred the debt through fraud.[16] Chapter 11 is different.

However, the Second Circuit has countered that third-party releases are legally supported and opined that its seven-factor test will make them rare, limited to only the most extraordinary circumstances, consistent with circuit precedent. Judge Wesley wrote a separate concurring opinion that raised eyebrows and signaled this fight wasn't, and shouldn't be, over. It was not. After the appellate back and forth, the decision is now at the Supreme Court, which granted certiorari.

BUT FIRST, ARE THIRD-PARTY RELEASES LEGAL?

The District Court had concluded that no statutory authority existed under the Bankruptcy Code to permit third-party releases of direct claims held by nondebtors[17] against other nondebtors. The district court determined Second Circuit precedent was ambiguous and unclear, and statutory authority "questionable."[18] This murkiness remained after a survey of Supreme Court and other circuit decisions.[19] The district court was skeptical of any "residual equitable authority" in the bankruptcy court to grant the releases, challenging a long-held view.[20] In bankruptcy appeals, the circuit court takes a fresh look at the bankruptcy court's decision. The legal standard of review is de novo on issues of law and clear error on issues of fact.[21] The Second Circuit reversed finding both legal support and no errors in the bankruptcy court's confirmation decision.

BUT WAIT, *STERN* STYMIES A BANKRUPTCY COURT (AGAIN)

The only limit to the bankruptcy court's power – a point on which the Second Circuit agreed with the District Court – is that third-party releases on nondebtor direct claims against nondebtors are Stern claims. In the continuing struggle to define bankruptcy court jurisdiction, the Supreme Court in *Stern v. Marshall*, held that bankruptcy courts (Article I courts) lacked the power to issue final judgment on claims about a non-bankruptcy public right – those rights arising from outside bankruptcy law.[22]

9 See CLLA Webinar, *Second Circuit Allows Controversial Nonconsensual Third-Party Releases in Purdue Pharma Chapter 11 Plan*, June 7, 2023, available at https://clla.org/clla-zoom-meetings/.

10 Purdue Op. at 3.

11 *Id.* at 26 (observing "an order against confirmation would not only destroy the entire settlement but would also result in a major escalation of costs and time") (citation omitted).

12 *Id.* at 10.

13 *Id.* at 11.

14 US CONST. Art. I, § 8.

15 *See* Terence L. Michael, & Michael R. Pacewicz, *Settling Objections to Discharge in Bankruptcy Cases: An Unsettling Look at Very Unsettled Law*, 37 Tulsa L. Rev. 637 (2013).

16 *See, e.g., Bartenwerfer v. Buckley*, 143 S. Ct. 665, 598 U.S. --- (Feb. 2, 2023).

17 Purdue Op. at 34-35 (citation omitted).

18 *Id.* at 35 (discussing Metromedia analysis).

19 *Id. at 36 (citation omitted).*

20 *Id. at 36 (citation omitted).*

21 *Id.* at 41-42 (citing *Morning Mist Holdings Ltd. v. Krys (In re Fairfield Sentry Ltd.)*, 714 F.3d 127, 132 (2d Cir. 2013)).

22 *Id.* at 39-40 (citation omitted); See also *Stern v. Marshall*, 564 U.S. 462 (2011).

Stern requires that, absent consent, the bankruptcy court can only issue proposed findings of facts and conclusions of law, reserving entry of the confirmation order by the Article III courts the District Court (and eventually) the Circuit Court. The import is to slow down the plan confirmation process in the Second Circuit. This extra step to plan confirmation, in the near term, may give the Third Circuit (which has not applied *Stern* to plan confirmations with third-party release) an edge in attracting cases premised on third-party releases, until the Supreme Court weighs in.

ARGUMENT: THIRD-PARTY RELEASES ARE STATUTORILY PERMITTED UNDER EQUITABLE PROVISIONS

The Second Circuit concluded that the Bankruptcy Code lets bankruptcy courts approve third-party releases under sections 105 and 1123(b)(6).[23] It also rejected other material objections to third-party releases premised on opposing statutory guidance in section 524 and on broader rights such as due process.[24]

Sections 105 and 1123(b)(6) are both broadly worded equitable provisions in the Code. Section 105 states that "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." But to grant relief under section 105(a), courts require a companion provision in the Code. Following the Seventh Circuit, and citing Supreme Court precedent,[25] the Second Circuit found that section 1123(b)(6) was a logical "companion" for the residual equitable authority to grant third-party releases. Section 1123(b)(6) provides a chapter 11 plan may "include any other appropriate provision not inconsistent with the applicable provisions of this title."[26]

Because third-party releases are not expressly *verboten* under the Code, in the Second Circuit's interpretation, they are "not inconsistent" with the Code and so are permissible. In adopting this view, the Second Circuit joined other circuits that rely on this provision for residual equity authority to grant third-party releases.[27]

SECOND CIRCUIT REJECTS VIEW RELEASES ARE IMPERMISSIBLE DISCHARGES

Code section 524(e) states that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt."[28] This section is relied on by the circuits that bar the releases as being akin to discharge, i.e., a permanent injunction.[29] The Second Circuit disagreed. It contended because the releases on appeal "neither offer umbrella protection against liability nor extinguish all claims" they stop short of a discharge on the non-debtor claims and thus the limitation presented by section 524(e).

For those circuits that bar third-party releases, only debtors submitting to the bankruptcy process may discharge their debts.[30] A simplified example is that discharge of the debtor does not also discharge a guarantor or co-obligor on the debt. Debt collection often relies on that additional security after default or bankruptcy. This view is not controversial.

According to the Second Circuit, however, a release is not a discharge when the release is narrow. The Second Circuit cited *MacArthur Co. v. Johns-Manville Corp. ("Manville I")*, 837 F.2d 89, 91 (2d Cir. 1988) to support its finding that lack of "umbrella protection" made these releases permissible and distinguishable from discharge. The court rejected an invitation from appellees to address section 524(g) which in effect codified *Manville* I in conferring this relief to asbestos cases. Section 524(g) permits channeling injunctions to a trust and related third-party releases only for asbestos liabilities, specifically limiting the remedy to "recovery for damages allegedly caused by the presence of, or exposure to, asbestos or asbestos-containing products."[31]

Proponents of chapter 11 settlements like in *Purdue Pharma* contend that section 524(g)'s grant of the injunction power is applicable to other mass tort liabilities. Opponents view the asbestos language as meaning what it says: only asbestos cases may benefit from section 524(g) solution. The Second Circuit sided with proponents of third-party releases who look beyond the plain language of the statute to the Bankruptcy Reform Act of 1994 that introduced it and

23 *Id.* at 11, 50-54.

24 *Id.* at 76-79.

25 *Id.* at 52 ("11 U.S.C. § 1123(b)(6) permits the inclusion of 'any other appropriate provision' in a plan so long as it is 'not inconsistent' with other sections of the Bankruptcy Code" (quoting *United States v. Energy Resources Co., Inc.*, 495 U.S. 545, 549 (1990))).

26 *Id.* at 50-54.

27 *Id.* To conclude section 1123(b)(6) is the statutory hook for the exercise of plenary equitable powers under section 105(a), the Second Circuit looks favorably on the Sixth and Seventh Circuit. *See Class Five Nev. Claimants (00-2516) v. Dow Corning Corp. (In re Dow Corning Corp.)*, 280 F.3d 648, 656-58 (6th Cir. 2002); *Airadigm Commc'ns, Inc. v. FEC (In re Airadigm Commc'ns, Inc.)*, 519 F.3d 640, 657 (7th Cir. 2008).

28 11 U.S.C. § 524(e).

29 Purdue Op. at 54 (citing cases relying on section 524(e) to bar third-party releases from the Fifth, Ninth, and Tenth Circuits).

30 Purdue Op.at 55.

31 11 U.S.C. § 524(g)(2)(B)(i)(I), which states "the injunction is to be implemented in connection with a trust that, pursuant to the plan of reorganization—

(I) is to assume the liabilities of a debtor which at the time of entry of the order for relief has been named as a defendant in personal injury, wrongful death, or property-damage actions seeking recovery for damages allegedly caused by the presence of, or exposure to, asbestos or asbestos-containing products;"

applied a rule of construction that nothing in the 1994 Act changes the court's authority to issue injunctions in plan confirmation orders.[32] For courts which see the power to grant third-party releases as valid and preexisting under the Code, the introduction of section 524(g) neither limits nor constrains that authority. However, under this view, if section 524 does not add to the existing authority of courts, to permit channeling injunctions and third-party releases to limit recovery of damages, then Congress has enacted mere surplus language into the Code.

This issue on discharge and permissive injunctions remains controversial. A decision against third-party releases under section 524(e) could affect section 524(g) at some point too. Although popular and viewed as successful, asbestos chapter 11 cases would become vulnerable to attack. The Supreme Court grant of certiorari here is based in part on the existing circuit court split on section 524 interpretation issues.[33]

SECOND CIRCUIT PRECEDENTS SUPPORT THIRD-PARTY RELEASES

Once the Second Circuit emerged from the statutory thicket, it found to its relief a welcome clearing in case law. "[T]his Court's precedents permit the imposition of nonconsensual third-party releases."[34] Rejecting appellee arguments to the contrary, the Second Circuit relied on its *Drexel* decision for authority that a bankruptcy court "may enjoin a creditor from suing a third party, provided the injunction plays an important part of the debtor's reorganization plan."[35] Likewise, the court's decisions in *Manville I*, discussed above, and *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005) (which cites *Manville I*) support the releases.[36] When third-parties release are necessary to the reorganization, and factually supported, precedent supports their use.

NEVER FEAR: A SEVEN-FACTOR TEST IS HERE!

The appeal also allowed the Second Circuit to endorse a factor-test as more specific guidance for plan proponents seeking approval of third-party releases. Appellees had challenged the Sackler releases on grounds they did not meet factors for approval identified in Second Circuit precedent, specifically in *Metromedia*.[37] Recognizing the potential for abuse, the Second Circuit adopted a seven-factor test, largely informed by *Dow Corning and Master Mortgage*, though it softens the seventh prong for a more permissive standard.[38]

The court held the seven factors for court consideration are:[39]

1. an identity of interests between the debtors and the released third parties, including indemnification relationships;
2. whether claims against the debtor and non-debtor are factually and legally intertwined, including whether the debtors and the released parties share common defenses, insurance coverage, or levels of culpability;
3. whether the scope of the releases is appropriate.... [A] release is proper in scope when its 'breadth' is 'necessary to the Plan;'
4. whether the releases are essential to the reorganization;
5. whether the non-debtor contributed substantial assets to the reorganization;
6. whether the impacted class of creditors 'overwhelmingly' voted in support of the plan with the releases.... [W]e consider [the 75% of voting creditors] threshold to be the bare minimum, and instead express approval for requiring overwhelming approval of the plan; and
7. whether the plan provides for the fair payment of enjoined claims.

This is an equitable test. Not all factors must be present. Bankruptcy courts must make specific factual findings on each factor, and plan proponents will have to present evidence to support such findings.

An important change by the Second Circuit diverges from the *Dow Corning* standard in the seventh prong. In *Dow Corning*, the Sixth Circuit allows third-party releases when the plan provides "for the full payment of all claims."[40] For example, plans with an opt out or other way to preserve a way to pursue them satisfy *Dow Corning*. The Sixth Circuit in *Dow Corning* rejected the third-party releases in the proposed plan because it did not give objecting claimants an ability to recover in full. The Second Circuit's sleight of hand – replacing "full payment" with "fair payment" occurs without explanation in the decision and appears to be a change mandated not by the Code but by a desire to create an

32 Purdue Op. at 59 (quoting Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 (1994)).

33 *See* note 61, supra; See also Candice Kline, *Nonconsensual Third-Party Releases in the Spotlight: Challenging the Limits of the Law and Drawing Congressional Scrutiny*, CLW, Vo. 34, Issue 3 (2021).

34 Purdue Op. at 56.

35 *Id.* at 57 (quoting *In re Drexel Burnham Lambert Group, Inc.*, 960 F.2d 285, 293 (2d Cir. 1992)).

36 *Id.* at 57-58.

37 *Id.* at 62-63.

38 *Id.* at 64 (citing *In re Dow Corning Corp.*, 280 F.3d 648, 658 (6th Cir. 2002) and *In re Master Mortgage Inv. Fund*, 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994)).

39 *Id.* at 64-67.

40 *Dow Corning*, 280 F.3d at 656.

COMMERCIAL LAW LEAGUE OF AMERICA
EXPERTISE • INSIGHT • RESULTS

2023 CLLA EVENTS AT THE NCBJ

THE ANNUAL CLLA LUNCHEON & FRANK KOGER MEMORIAL EDUCATIONAL PROGRAM

THURSDAY, OCTOBER 12, 2023

JW MARRIOTT AUSTIN, TX

exception which will allow *Purdue Pharma*'s plan to pass muster. It effectively gelds the Second Circuit's robust new test. No statutory basis for this test exists. The basis on which a court should decide what is "fair and equitable" comes with no guidance and seems conclusory: If you say so, it therefore is.

Applying these factors to *Purdue Pharma*, the Second Circuit readily approved the third-party releases under all seven factors.[41] The Second Circuit also weighed other non-monetary concessions by the Sacklers as favoring plan confirmation.[42] After rejecting all objections, including due process concerns about whether releasing claimants received adequate notice and an opportunity to be heard (despite reasonable questions about voting and implied consent without an ability to opt-out from nonvoting claimants),[43] the Second Circuit reversed the district court and held that the bankruptcy court acted properly when confirming the *Purdue Pharma* plan.[44]

THE CONCURRENCE THAT WANTS TO BE A DISSENT WHEN IT GROWS UP

Judge Wesley concurred in the Second Circuit's judgment but wrote a concurring opinion that expressed reluctance in joining the majority and lingering doubts about it. Reluctance because following precedent would mandate that the panel follow the *Drexel* decision, which it plainly does not do.[45] The concurrence is an exercise of restraint despite serious misgivings about the precedent and statutory authority.

Doubts linger based upon the uncertain statutory authority. Judge Wesley was "not convinced that statutory footing is up to the task."[46] Concerns remain around the use of the awesome power to extinguish (permanently enjoin and settle) nondebtor claims against nondebtors.[47] Judge Wesley calls this an "extraordinarily powerful tool" for "any court to wield."[48] Although he called upon Congress to take responsibility and provide clarity and statutory guidance, without lawmaker action, Judge Wesley endorsed uniformity through Supreme Court review.[49] Without uniformity though Congress or the Supreme Court Judge Wesley concludes whether third-party releases are proper "is a function of geography."[50] This does not seem like the American way.

On the plan and Sackler releases, Judge Wesley found the plan provides an overly broad release beyond what could occur in individual cases by the Sacklers. He found the "Shareholder Release" overly broad and providing no carveout for fraud, which would result in claims being barred that creditors could except from discharge under section 523.[51] He also raised concern that *Purdue Pharma*'s plan distributes no value for direct claims against the Sacklers released under the plan.[52] Would the releases that nondebtor direct claims against the Sacklers then fail for lack of consideration? Judge Wesley provided a hypothetical in footnote 3 suggesting the answer is obviously yes.

Taking together the various concerns, for Judge Wesley the Sackler releases provide "blanket immunity" and an impermissible discharge.[53] He observed that no part of the Sackler contribution, while substantial (though maybe not yet enough) goes to satisfying the released direct third-party claims.[54] His discussion signals a concern that questions about what "fair and equitable" means for claimants remain unanswered.

For Judge Wesley, the Code's silence on specifically granting extraordinary third-party releases was deafening. He questioned the authorities relied on by the majority in a dissenter's voice. In discussing the authority to grant third-party releases, he used the word "extraordinary" five times.

SCOTUS FOR THE LAST WORD

The Second Circuit rebuffed all attempts to reverse or stay its ruling. On July 24, 2023, it denied a petition for rehearing and rehearing en banc.[55] The next day it denied a motion to stay the mandate,[56] which would issue on August 1, 2023. The Second Circuit seemed unconcerned about the risk of allowing the plan to go forward pending appeal could result in dismissal on grounds of equitable mootness, another controversial bankruptcy practice to end plan appeals. Only a stay of the Second Circuit's decision would preserve status quo, and they elected not to maintain the status quo.

The U.S. Trustee's Office, through Solicitor General Elizabeth B. Prelogar, then sought a stay at the Supreme

41 Purdue Op. at 68-75.

42 Purdue Op. at 75 (citing "governance requirements, abatement trusts, the public document archive, and divestment of the Sacklers from the opioid business worldwide").

43 *See* note 58 supra, p. 9 ("Although the plan attracted overwhelming support from those creditors who voted, several States and more than 2,600 personal-injury claimants who voted opposed confirmation. And hundreds of thousands of claimants failed to vote at all; fewer than 20% of 618,194 claimants entities to vote - and fewer than 50% of the subset of claimants with personal-injury claims - ended up voting on the plan." (citations omitted)).

44 Purdue Op. at 79.

45 *Id.* (Concurring Op.) at 1.

46 *Id.* at 2.

47 *Id.*

48 *Id.*

49 *Id.* at 2-3.

50 Purdue Op. (Concurring Op.) at 14.

51 *Id.* at 4-5.

52 *Id.* at 5.

53 *Id.* at 7.

54 *Id.*

55 *In re Purdue Pharma L.P.*, No. 22-110 (July 24, 2023) (denying petition for rehearing and rehearing en banc).

56 *In re Purdue Pharma L.P.*, No. 22-110 (July 25, 2023) (denying motion for stay of mandate).

Court and certiorari review to stop *Purdue Pharma* from implementing its plan.[57] This effort proved more successful.

On July 28, 2023, Prelogar leveraged Judge Wesley's call for a nationwide resolution of the third-party releases issue.[58] The reasons for the stay were to avoid piecemeal and potentially wasteful implementation of the plan and to avoid an inevitable equitable mootness dispute.[59] She forcefully argued against the "sweeping nonconsensual releases" as an abusive bankruptcy practice.[60] Prelogar also laid bare the "entrenched" circuit court split inviting review.[61] Justice Sotomayor set a response date to the application of August 4, 2023.[62]

The City of Grande Prairie (for Canadian municipalities) filed a response supporting the U.S. Government's stay application.[63] The Canadian municipalities argued that the expansive third-party release is "the most abusive ever employed ... foisted upon opioid claimants without compensation and without consent."[64] Grande Prairie joined the government's concerns about equitable mootness and wasteful administrative complexities if *Purdue Pharma* began plan implementation.[65] Despite the funds being paid in connection with the releases, the Canadians receive "virtually nothing" under the plan, have no access to trust funds, and are treated as general unsecured creditors.[66]

Members of the Nine took no position on the stay, citing their settlement agreement with the debtors,[67] but as Connecticut's Attorney General Tong has announced an intent to do, may file amicus briefs opposing third-party releases despite agreeing to the improved settlement.[68]

Plan supporters that filed responses supporting the plan and third-party releases were the Ad Hoc Group of Individual Victims, the Creditor's Committee, the Debtors, the Multi-State Governmental Entities, and the Ad Hoc Committee of Governmental and Other Contingent Litigation Claimants.[69] They argued for the settlement's practical result: to release abatement funds to address the terrible opioid crisis, now.[70] According to *Purdue Pharma*, "victims emphatically and decisively reject[ ] such a protracted litigation battle in favor of their plan."[71] Further delay, went this argument, is inequitable and harms the victims, and ironically, helps the Sacklers.[72] Proponents argued the "balance of the equities" strongly favor rejecting the stay and denying certiorari.[73] A stay would cause avoidable deaths and suffering.[74]

On the legal arguments, plan proponents argued that the releases are "narrow" and the equities favor immediate plan implementation and no stay relief.[75] They also contended that the circuit court split is neither critical nor straightforward, and that *Purdue Pharma* is not the vehicle to resolve it.[76] Finally, they argued that decades of orders permitting third-party releases in at least some circuits cautions against any decision that would "upend[ ] the bankruptcy system."[77]

In their view, the legal basis for third-party releases is solid and withstands all arguments otherwise.[78] They call concerns about bankruptcy abuse stemming from third-party releases a "strawman" and a "hyperbolic concern."[79] With any challenge to third-party releases meritless, the Second Circuit's decision and status quo should remain untouched and unreviewed.

The U.S. Trustee's reply highlighted the risk of equitable mootness and wasteful use of estate resources implementing the plan without a stay.[80] Besides asserting rightful standing under Code section 307 (and leaning on the Canadian petitioners' standing), the U.S. Trustee contends that the balance of equities are in its favor to avoid waste and renegotiation.[81]

On whether a circuit court split exists and should be addressed, the U.S. Trustee had only to reference the Second Circuit's own opinions.[82] The Reply then went

57 *Harrington, U.S. Trustee, Region 2 v. Purdue Pharma, L.P.*, Case No. 23-124 ("UST Supreme Court Case"), Petition for a Writ of Certiorari, filed July 28, 2023.

58 UST Supreme Court Case, Solicitor General Stay Application, at 2.

59 *Id.* at 2, 5-6.

60 *Id.* at 3.

61 *Id.* at 14-16 (summarizing the circuit court split and decisions of the fifth, ninth, and tenth circuits that disallow then and the six circuits that permit them: third, fourth, sixth, seventh, and eleventh). *See* also note 33, infra.

62 UST Supreme Court Case, Response to Application requested by Justice Sotomayor by August 4, 2023, entered on July 28, 2023.

63 *Id.*

64 City of Grande Prairie Response, at 2.

65 *Id.* at 3.

66 *Id.* at 7-8.

67 California (States) Response, at 1.

68 Solicitor General Stay Application, at 10 (quoting Attorney General Tong Statement on Appeals Court Decision Enabling Purdue Settlement to Proceed (May 30, 2023), at https://perma.cc/52MQ-BM3D.)

69 UST Supreme Court Case, Responses, filed on August 4, 2023, generally.

70 Ad Hoc Group of Individual Victims Response, at 3-4.

71 Purdue Pharma Response, at 38.

72 UCC Response, at 2 ("Tragically, the only party that will benefit from the stay will be the Sacklers.").

73 Purdue Pharma Response, at 66-69.

74 Id. at 68-69.

75 UCC Response, at 6-7.

76 *Id.* at 19-20.

77 *Id.* at 24.

78 Purdue Pharma Response, at 50-59.

79 *Id.* at 59.

80 Solicitor General Reply, at 1-2.

81 *Id.* at 3-9.

82 *Id.* at 9.

further to address the effort by plan proponents to diminish the appearance of a stark circuit split,[83] a split that most practitioners, courts, and treatises have also recognized. Solicitor General Prelogar observed that the improved $6 billion settlement to resolve the Nine's appeals – resulting in an additional $1.675 billion – "demonstrates that requiring consent is important leverage that can lead to better outcomes."[84] Justice Sotomayor then denied *Purdue Pharma*'s request to file a Sur-Reply.[85]

On August 10, 2023, Justice Sotomayor referred the application to the entire court, which granted the stay and further granted the Application as a petition for writ of certiorari. In its Order, the Supreme Court framed the question for review: "Whether the Bankruptcy Code authorizes a court to approve, as part of a plan of reorganization under Chapter 11 of the Bankruptcy Code, a release that extinguishes claims held by nondebtors against nondebtor third parties, without the claimants' consent."[86] The Court scheduled argument for this December and will decide the case in its October Term 2023-2024.[87]

The U.S. Trustee's Office, the bankruptcy system's watchdog, has been vigorously criticized by *Purdue Pharma* and commentators.[88] The main criticism uses words of confrontation: waging a "(nearly) solo campaign ... not content to advance its own agenda" and "put a stop to the U.S. Trustee's campaign."[89] *Purdue Pharma* argued the "Trustee's attack on third-party releases is also deeply unfair to bankruptcy practice and at odds with real-world experience."[90] The Debtors claim "the Trustee has hijacked the case."[91] In their opposition to the stay and certiorari, the Debtors argued that bankruptcy is for debtors and creditors and anyone else without an economic interest – or any "concrete interest (economic or otherwise)"[92] including the bankruptcy watchdog, should go home.[93] The Debtors further contend that the U.S. Trustee is "in no way aggrieved by the third-party releases in the Debtors' plan," and as such the U.S. Trustee lacks Article III standing.[94]

For anyone who has represented the public interest in bankruptcy, this position, and threats to challenge standing, as the plan proponents did against the U.S. Trustee,[95] are nothing new. Instead of advocacy, the arguments against public interest regulation reflect an unfortunate breakdown in civility and respect for the role of public interest stakeholders in our bankruptcy system. The adult in the room, the Supreme Court, will now settle the question.

THIRD-PARTY RELEASES IN MASS TORTS: AN ISSUE FOR OUR TIME

The weight of *Purdue Pharma* on the bankruptcy system is significant. Professor Adam Levitin has described the case as "the most socially important bankruptcy case in Chapter 11 history."[96] The case and controversy has generated tremendous attention from bench and bar and academics. The CLLA itself has this now six-part article series and recently produced two webinars besides conference programming. The mass torts practice is reaching a zenith in the courts and commentary.

THE BEST OF THE REST: AEARO TECHNOLOGIES, MALLINCKRODT AND LTL MANAGEMENT

With the dark cloud of uncertainty hovering over mass tort bankruptcies, debtors continue to try their luck in the courts. These three cases each test a part of mass tort bankruptcy practice, which together with third-party releases inform the typical case playbook: (1) file the bankruptcy case in a circuit that permits third-party releases; (2) leverage the automatic stay and companion injunction to also stay litigation against third-party plan proponents; (3) propose a global settlement releasing third-party plan proponents in exchange for substantial contribution to the plan (i.e., a large settlement payment and mediation to achieve buy-in); and (4) confirm a plan over any remaining objections.

Although these cases, with *Purdue Pharma*, deal with different challenges to mass tort bankruptcy strategy, they collectively suggest a closing door. Yet more mass

83 *Id.* at 9-16.

84 *Id.* at 28.

85 Denying Motion to Direct the Clerk to File a Sur-Reply, entered on August 9, 2023.

86 Mandate Granting Stay and Writ of Certiorari, entered on August 10, 2023.

87 Briefing Schedule, entered on August 21, 2023.

88 See John Kruzel and Andrew Chung, "US Supreme Court halts Purdue Pharma bankruptcy settlement pending review, Reuters, August 11, 2023 ("In a statement, Purdue said it was disappointed that the U.S. Trustee, the Justice Department's bankruptcy watchdog that filed the challenge at the Supreme Court, has been able to 'single-handedly delay billions of dollars in value that should be put to use for victim compensation, opioid crisis abatement for communities across the country and overdose rescue medicines.'"); See also Thomas Salerno's Op-Ed, "*When Will the Fool's Errand End? The U.S. Trustee's Continued Pursuit of the Destruction of Third Party Releases in Purdue Pharma*" and LinkedIn post: "When I see a government agency so disconnected from economic reality that it takes positions that affirmatively harm the creditors of the case, I am speechless (although obviously not wordless)," available at https://www.linkedin.com/posts/thomassalernoattorney_fools-errand-article-activity-7088180812105338880-PmAB.

89 Ad Hoc Group of Individual Victims Response, at 2, 4.

90 Purdue Pharma Response, at 61.

91 *Id.* at 33.

92 UCC Response, at 3; Purdue Pharma Response, at 32-37.

93 Ad Hoc Group of Individual Victims Response, at 2 (noting "no ties to the opioid crisis" and "no economic stake in the outcome").

94 Purdue Pharma Response, at 34.

95 UCC Response, at 20-22, arguing without a financial interest, U.S. Trustee lacks standing to petition the Court.

96 *See* Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter 11's Checks and Balances*, 100 Tex. L. Rev. 102, 103 (2022).

tort cases may still be filed. For example, as of the publication deadline, Rite Aid has announced its intent to file bankruptcy to resolve its opioid liabilities and address its major debt and performance challenges.

AEARO TECHNOLOGIES: ARE WE DONE YET? TRYING SETTLEMENT OUTSIDE BANKRUPTCY

After experiencing headwinds with its bankruptcy strategy to resolve massive defective earplug litigation, 3M's subsidiary Aearo Technologies is trying a new tactic: An old-fashioned settlement without bankruptcy. First denied preliminary injunctive relief to protect parent 3M then having the chapter 11 case dismissed on bad faith grounds (both on appeal to the Seventh Circuit), Aearo clearly received the cold shoulder in bankruptcy.[97] The federal district court judge, overseeing the multi-district litigation (MDL) that combines thousands of earplug lawsuits into one forum, criticized the bankruptcy tactic.[98]

Aearo and its parent 3M have apparently moved on and have now offered to settle for $6 billion to settle 260,000 earplug lawsuits – outside of bankruptcy court.[99] For some mass tort defendants, bankruptcy is not the shiny new object anymore. What might appeal more is moving on. Global peace may exist outside bankruptcy too.

MALLINCKRODT: CHAPTER 22, A MORE FEASIBLE, FEASIBLE PLAN, AND SMALLER SETTLEMENT FOR OPIOID VICTIMS

Providing a lesson on plan feasibility, on August 23, 2023, Mallinckrodt filed its second chapter 11 case, labelled a "chapter 22," within two years of confirming its first chapter 11 plan. The bankruptcy judge had approved Mallinckrodt's plan as "feasible" under Code section 1129(a)(11) and found the company unlikely to file again.[100] That plan included a negotiated $1.7 billion settlement with opioid victims.[101]

It did not work out. Citing "significant unanticipated business developments, adverse economic conditions, and a market environment that the Company anticipates may prevent it from timely refinancing $817 million of upcoming debt maturities in 2025," Mallinckrodt required a new plan.[102] Mallinckrodt did, however, pay opioid claimants a final settlement payment of $250 million before filing.[103]

Mallinckrodt's pre-pack plan is supported by its major creditors and opioid claimants, including 88% of its first lien funded debt and 86% of its second lien funded debt, and the master opioid disbursement trust.[104] Under the new plan, opioid settlement obligations are reduced to $250 million from $1.275 billion, and Mallinckrodt made the final payment prepetition.[105] Mallinckrodt's insolvency and business prospects require less debt. This is a consensual plan. If actually feasible, Mallinckrodt may exit bankruptcy this year.

LTL MANAGEMENT: STUCK ON (LACK OF) FINANCIAL DISTRESS AND TWICE DISMISSED

In a prior article in this series,[106] we discussed *In re LTL Management's* dismissal after the Third Circuit determined that the debtor could not show financial distress.[107] Within hours of dismissal, LTL Management filed a second bankruptcy case with different terms hoping to scale that hurdle.[108] It again failed.[109] The bankruptcy court, applying the same financial distress factors and analysis established in the Third Circuit's opinion and decision dismissing the first bankruptcy case, dismissed the second case.[110] Using an analogy of a burning house, Judge Kaplan explained, "as it stands now, in gauging financial distress, observing smoke may not be enough—one must see flames."[111] On August 25, 2023, LTL Management appealed the bankruptcy court's dismissal decision to the district court.[112] The

---

97 *In re Aearo Techs. LLC*, No. 22-02890-JJG-11, 2023 WL 3938436, at *22 (Bankr. S.D. Ind. June 9, 2023) (similarly dismissing Chapter 11 cases filed to manage mass tort liability arising from 3M's manufacture and sale of hearing protection devices).

98 See Brendan Pierson, *Florida Judge Sharply Questions 3M Bankruptcy Strategy*, Reuters (Aug. 11, 2022).

99 *See also* Emily R. Siegel, "3M Lawsuit Investors Ordered to Be Unmasked Amid $6 Billion Deal," Bloomberg Law, Aug. 30, 2023.

100 *In re Mallinckrodt PLC*, Case No. 20-12522, Revised Opinion, Dkt. No. 6378, at 75 (Bankr. D. Del. Feb. 8, 2022) (Dorsey, J.).

101 *See* Dietrich Knauth, *Drugmaker Mallinckrodt Files for Second Bankruptcy in US*, Reuters (Aug. 28, 2023).

102 *In re Mallinckrodt PLC*, Case No. 23-11258, Goodson Declaration, Dkt. No. 16, at 4 (Bankr. D. Del. Aug. 28, 2023).

103 *Id.* at 5.

104 *Id.* at 3-4.

105 *Id.* at 5 & n.4 ("The Debtors have paid $700 million to date on account of their opioid settlement obligations.").

106 *See* Candice Kline, *LTL Management and the Pursuit of Liberty: Third Circuit's Requirement of Financial Distress for Good Faith Filings Thwarts Mass Torts Maneuvers (Maybe)*, CLW, Vol. 37, Issue 1 (2023).

107 *LTL Management, LLC. v. Official Committee of Talc Claimants, et al. (In re LTL Management, LLC)*, 58 F.4th 73, Case. No. 22-2003 (3d Cir. Jan. 30, 2023).

108 *In re LTL Management, LLC,* Case No. 23-12825, Voluntary Petition, Dkt. No. 1 (Bankr. D.N.J. Apr. 4, 2023); *See also* Kim Declaration, Dkt. No. 4 (Bankr. D.N.J. Apr. 4, 2023).

109 *In re LTL Management, LLC*, Case No. 23-12825, Dismissal Order, Dkt. 1211 (Bankr. D.N.J. Aug. 11, 2023). *See also* Memorandum Opinion, Dkt. No. 1127 (Bankr. D.N.J. July 28, 2023) (Kaplan, J.).

110 *In re LTL Management, LLC*, Case No. 23-12825, Memorandum Opinion, Dkt. No. 1127, p. 3, 39. "[T]he evidentiary record fixed at trial does not establish sufficient "imminent" or "immediate" financial distress to satisfy the criteria enunciated by the Third Circuit in I*n re LTL Mgmt., LLC*, 64 F.4th 84 at 102, 108 (3d Cir. 2023)." *Id.* at 3.

111 *Id.* at 17.

112 *In re LTL Management, LLC*, Case No. 23-12825, Notice of Appeal Transmittal to District Court, filed on Aug. 24, 2023.

district court will hear the appeal and issued a stay pending appeal.[113]

Recently, a 24-year-old talc plaintiff, who was allowed by the bankruptcy court to continue his litigation because he was near death, won a jury award of nearly $19 million.[114] J&J denies any liability and announced plans to appeal. J&J has spent $4.5 billion on talc litigation, including legal fees.[115]

The mass tort bankruptcy settlement approach is intended to resolve all such cases in a global settlement. J&J and LTL Management keep pushing the bankruptcy solution though their prospects for success seem increasingly remote. It may be time for J&J to explore the 3M and Aearo Technologies approach of settling without the leverage sought in bankruptcy.

CONCLUSION

A few years ago, mass torts in bankruptcy seemed like a solid strategy. The playbook established, debtors and stakeholders counting on third-party releases could seek welcome shelter in bankruptcy. Injunctions would bind parties to the bargaining table, mediation would protect stakeholders from public disclosures and support the plan confirmation process, and bankruptcy would deal with any nonconsenting creditors. But the risks and expenses (professional fees are in the hundreds of millions of dollars) in a handful of ongoing mass tort bankruptcy cases coupled with major legal uncertainty suggest parties may seek alternatives.[116] ■

113 *In re LTL Management, LLC*, Letter Order Granting Stay Pending Appeal, entered on Sept. 1, 2023.

114 Brendan Pierson, *J&J Must Pay $18.8 million to California Cancer Patient in Baby Powder Suit*, Reuters (July 18, 2023).

115 *Id.*

116 *See, e.g.*, Robert Bruan, *Governor Josh Green Detailing Economic Options for Lahaina Fire Victims*, KITV 4 (Sept. 8, 2023) (proposing a damages settlement fund to provide “a settlement right away” that would avoid attorney fees and get more money to fire victims).

Ed. Note – CLLA and Third-Party Releases

The CLLA continues to track developments on mass torts and third-party releases and provides timely updates and analysis to its members. The CLLA has produced two live online seminars on mass torts and third-party releases in Purdue Pharma. The League also has a dedicated sub-committee of its Bankruptcy Section evaluating legislation and policy and continues to advocate where appropriate through its amicus committee. Interested in becoming a member and joining the League’s efforts? Please contact the League at www.clla.org.

The Lawrence P. King Award

ABOUT THE AWARD

Each year, the Executive Council of the Commercial Law League's Bankruptcy Section presents the Lawrence P. King Award to recognize a lawyer, judge, teacher or legislator who exemplifies the best in scholarship, advocacy, judicial administration or legislative activities in the field of bankruptcy. The award is designed to recognize the lifetime achievements of Professor King, which include contributing to the practice of bankruptcy law through teaching, by working to elevate the profession and through bankruptcy-related legislative activities.

CONGRATULATIONS
JUDGE **THOMAS L. AMBRO**

Thomas L. Ambro is a Judge on the United States Court of Appeals for the Third Circuit. Prior to becoming a Judge in 2000, he was a member of the law firm of Richards, Layton & Finger, Wilmington, Delaware, where he was the head of its Bankruptcy Group and involved in many of the most significant reorganizations in the 1990s. Judge Ambro joined the firm in 1976 after a judicial clerkship with Delaware Supreme Court Chief Justice Daniel L. Herrmann. On the Third Circuit Judge Ambro has authored over 1,000 opinions, many of which relate to bankruptcy and commercial issues.

Judge Ambro is a past Chair of the Section of Business Law of the American Bar Association and past Editor of The Business Lawyer. He is also a past member of the Board of Trustees of the American Inns of Court Foundation, and in Delaware he is a past President of the Richard S. Rodney Inn of Court and a former Co-Chair of the Collins J. Seitz Bankruptcy Inn of Court. Within the Delaware State Bar Association, Judge Ambro is a former Chair of the Commercial Law Section and chaired for 20 years that Section's Committee on the Uniform Commercial Code. He currently is a member of the American Law Institute, the American College of Bankruptcy, and the National Bankruptcy Conference (where he served on its Executive Committee).

Judge Ambro has authored numerous articles and CLE materials, and has lectured frequently throughout the country, including on various bankruptcy and commercial matters. In 2017, Judge Ambro gave the inaugural King-Seligson Lecture on Bankruptcy and Corporate Reorganization, named after two renowned NYU law scholars—Professor Lawrence King, the former Editor-in-Chief of Collier on Bankruptcy, and Professor Charles Seligson, a preeminent academic of his era on bankruptcy and creditors' rights.

From mid-2017 until early 2022, Judge Ambro was a member of the mediation team involved with debt-restructuring proceedings of the Commonwealth of Puerto Rico and affiliated entities under the federal Puerto Rico Oversight, Management and Economic Stability Act.

Judge Ambro graduated from Georgetown University's College in 1971 (Class of '72) and from the Georgetown University Law Center in 1975.

COMMERCIAL COLLECTION CLLA CERTIFIED IACC AGENCY

Certified by CLLA
Endorsed by IACC

WANT TO EARN A $500 CREDIT?

You can!

Contact Dawn Federico today about our NEW Agency-Get-A-Certified-Agency referral program.

REFER an agency for certification and your agency will receive a $500 credit* when that agency becomes certified. Your $500 credit can be used for a CLLA or IACC event. There are plenty of excellent events coming so be sure to be a part of this exciting offer!

Dawn Federico
Director
312.240.1400
dawn.federico@clla.org

CLLA
Commercial Law League of America
Expertise • Insight • Results

International Association of Commercial Collectors
Est. 1970
IACC

*To qualify for the $500 credit, the referring member agency must contact the prospective member agency. The referring agency must also contact Dawn Federico and provide their contact information for follow up to the prospect agency.

PROCEED WITH CAUTION: JUDGES ISSUING STANDING ORDERS REGARDING THE USE OF ARTIFICIAL INTELLIGENCE IN THE COURTROOM, PLEADINGS AND LEGAL RESEARCH

Wanda Borges, Esq.
Principal Member
Borges and Associates, LLC

&

Amy L. Pona
Director of Commercial Debt Collection
Gurstel Law Firm P.C.

Both federal court and bankruptcy judges around the country are issuing standing orders at increasing frequency regarding the use of ChatGPT and other artificial intelligence ("AI") in the courtroom and in parties' legal pleadings. As of late, the standing orders coming out vary from completely banning the use of AI in court or in pleadings, to requiring disclosure if AI was used in the "preparation of any pleading, motion or other paper filed with the Court".[1]

Many judges who have issued orders regarding the use of AI in their courtrooms or proceedings are requiring litigants to attest when filing pleadings that "no portion of any filing [was] drafted by generative artificial intelligence (such as ChatGPT, Harvey.AI, or Google Bard)" and that "any language drafted by generative artificial intelligence [has been] checked for accuracy."[2] One judge issuing such an Order, U.S. District Court Judge Brantley Starr of the Northern District of Texas, was the first to require attorneys before his court to make this AI certification and noted that concerns over bias were driving his order. He reasoned that, "[t]hese platforms in their current states are prone to hallucinations and bias. . . Another issue is reliability or bias. While attorneys swear an oath to set aside their personal prejudices, biases, and beliefs to faithfully uphold the law and represent their clients, generative artificial intelligence is the product of programming devised by humans who did not have to swear such oath".[3] Judge Starr goes on to state that unlike attorneys, "generative artificial intelligence ... hold[s] no allegiance to any client, the rule of law, or the laws."[4]

Similarly, Magistrate Judge Gabriel Fuentes in the Northern District of Illinois is not only requiring litigants to disclose the use of AI in pleadings, but also in legal research.[5] A similar order in a Texas Bankruptcy court requires litigants to verify that any information contained in pleadings or other papers that was generated by AI has been checked for accuracy against traditional legal databases or other reliable means.[6] This Judge notes in her Order that, "Artificial intelligence systems hold no allegiance to any client, the rule of law, or the laws and Constitution of the United States and are likewise not factually or legally trustworthy sources without human verification". This is a good reminder to all of us as we enter into a new chapter of our practices in the digital era.

While Judge Starr and others were concerned about the unreliability and bias of the technology, other judges have noted their additional concerns with the safeguarding of privileged information. Judge Stephen Alexander Vaden on the US Court of International Trade, for example, requires in his standing Order that the party provide a certification that the use of any AI program did not result in the disclosure of any confidential or business proprietary information to any unauthorized third party.[7] Judge Vaden notes that generative artificial intelligence programs that supply natural language answers to user prompts create "novel risks to the security of confidential information".[8] Users having conversations with these programs may include confidential information in their prompts, which may result in the program retaining access to confidential information.[9]

While there are legitimate ways to leverage and use AI tools in the legal profession, judges around the country are taking a clear stance that legal briefing and research is not one of them. Recently a Colorado Springs attorney practicing for less than two years learned this lesson the hard way after using ChatGPT to conduct legal "research" and cite those cases in a civil motion to set aside that was filed with the Court. The cases that were included in the ChatGPT materials were cases that did not exist. The attorney claims that he filed the motion without knowing he cited fake cases. On the day of the hearing, he realized his mistake when he began to review and try to locate the cases in a legitimate legal research platform. The judge overseeing the hearing couldn't find the cases either and denied the motion due to the false citations. He then threatened to file a complaint against the attorney. The attorney, in turn, filed an affidavit with the Court apologizing for his mistake. He states in his affidavit that there "were several inquiries and prompts given to ChatGPT that proved accurate based on my existing knowledge of the law and what I confirmed through research, such that I made the imprudent leap in assuming that the tool would be generally accurate. . . The initial confirmatory searches emboldened my confidence in the technology and I imprudently accepted the case law research that followed without investigation into each case citation's accuracy."[10]

While technology can certainly be a powerful tool in our law practices, artificial intelligence is not an acceptable alternative to true lawyering. As these AI programs become more popular, it will be prudent to be cognizant of your jurisdiction's ethical requirements, local rules and court specific requirements regarding the use of AI technology, and adhere to the standing orders and expected decorum of the court. ■

1 Hon. Michael M. Bayslon, "Standing Order RE: Artificial Intelligence ("AI") in Cases Assigned to Judge Bayslon (E.D. PA)

2 Hon. Brantley Starr, "Mandatory Certification Regarding Generative Artificial Intelligence Standing Order" (N.D. Tex)

3 *Id.*

4 *Id.*

5 Hon. Gabriel Fuentes, "Standing Order For Civil Cases Before Magistrate Judge Fuentes (N.D. Ill).

6 Hon. Stacy G. C. Jernigan, "In Re: Pleadings using Generative Artificial Intelligence" (N.D. Tex)

7 Hon. Stephen Alexander Vaden, "Order on: Artificial Intelligence (U.S. Court of International Trade)

8 *Id.*

9 *Id.*

10 https://reason.com/volokh/2023/06/16/lawyers-affidavit-in-the-colorado-ai-hallucinated-precedent-case/?utm_source=ground.news&utm_medium=referral

THE U.S. SUPREME COURT IN REVIEW: BANKRUPTCY EDITION

Ronald L. Peterson
Of Counsel
Jenner & Block, LLP

Breana K. Drozd
Associate
Jenner & Block, LLP

In re Bartenwerfer, 598 U.S. 69, 143 S. Ct. 665, 214 L. Ed. 2d 434 (2023)

Kate Bartenwerfer thought she was the ideal innocent spouse under the law, but she had no idea what fate awaited her.

Kate and her then-partner, David (hereinafter, **"Mrs. Bartenwerfer"** and **"Mr. Bartenwerfer"**) purchased and renovated a house. After the renovations were completed, the Bartenwerfers sold the house to Kieran Buckley (**"Mr. Buckley"**). At the time of the sale, the Bartenwerfers attested to Mr. Buckley that they had disclosed all known defects in the house. However, Mr. Bartenwerfer failed to tell Mrs. Bartenwerfer and Mr. Buckley about the house's leaky roof, defective windows, missing fire escape, and permit problems.

Upon learning of the defects, Mr. Buckley sued both of the Bartenwerfers for, as relevant here, fraudulent misrepresentation. At trial, the parties, contractors, and real estate agents all testified that Mr. Bartenwerfer—but not Mrs. Bartenwerfer—had hid the defects. The suit resulted in a $200,000 verdict against both the Bartenwerfers. However, the Bartenwerfers were unable to pay the judgment or their other creditors (of which there were many) and consequently filed for relief under chapter 7 of the Bankruptcy Code.

But Mr. Buckley said not so fast—he commenced an adversary proceeding objecting to the Bartenwerfers' discharge, arguing that section 523(a)(2)(A) prohibited the discharge of debts that are obtained through fraud. Mr. Buckley's suit resulted in the bankruptcy court denying not only Mr. Bartenwerfer's discharge, but Mrs. Bartenwerfer's discharge as well. The bankruptcy court reasoned that Mr. Bartenwerfer's fraud was imputed to Mrs. Bartenwerfer because they were in a marital partnership, and under California law, were therefore jointly and severally liable.

The Bankruptcy Appellate Panel (the **"Panel"**) reversed the bankruptcy court as to Mrs. Bartenwerfer only. Adopting the "knew or should have known" standard from *Walker v. Citizens State Bank*, 726 F.2d 452 (8th Cir. 1984), the Panel remanded the case to the bankruptcy court with instructions to determine whether Mrs. Bartenwerfer "knew or should have known" of Mr. Bartenwerfer's fraudulent misrepresentation to Mr. Buckley. On remand, the bankruptcy court determined that Mrs. Bartenwerfer did not know of Mr. Bartenwerfer's fraud—*i.e.*, that she was an innocent spouse that had not engaged in fraud—and therefore that Mr. Bartenwerfer's fraud could not be imputed to her. The Panel affirmed on appeal.

Thereafter, Mr. Buckley appealed to the Court of Appeals for the Ninth Circuit, which reversed the bankruptcy court's decision. Applying "basic partnership principles" from the U.S. Supreme Court's decision in *Strang v. Bradner*, 114 U.S. 555, 561 (1885), which held that both partners in a partnership are liable for the fraudulent conduct of one partner, the Ninth Circuit held that "Mrs. Bartenwerfer's debt is nondischargeable regardless of her knowledge of [Mr. Bartenwerfer's] fraud." *Bartenwerfer*, 860 Fed. Appx. at 546-47. Following this decision, the U.S. Supreme Court granted certiorari to resolve the dispute among lower courts regarding the meaning of section 523(a)(2)(A) of the Bankruptcy Code.

Section 523(a)(2)(A) excepts from discharge "any debt . . . for money [or] property, . . . obtained by false pretenses, a false representation, or actual fraud[.]" 11 U.S.C. § 523(a)(2)(A). Before the U.S. Supreme Court, Mrs. Bartenwerfer argued that section 523(a)(2)(A) only prohibited the discharge of debts obtained by a fraudulent misrepresentation *of her own making or with her knowledge*. She argued that it was *Mr. Bartenwerfer* that had committed fraud—not she—and that she had no knowledge of the fraud. Mrs. Bartenwerfer lamented that the passive voice of the statue hides the relevant actor, Mr. Bartenwerfer, in "plain sight." Bartenwerfer, 143 S.Ct. 665, 671-72 (2023).

The U.S. Supreme Court disagreed, reasoning that Congress' use of the passive voice "pulls the actor"—in this case, Mr. Bartenwerfer—"off the stage." *Id.* at 672. The Supreme Court reasoned that Congress framed section 523(a)(2)(A) on the *event*, not the *actor*, and "without respect to any actor's intent or culpability." *Id.* Liability for common law fraud is not limited to the wrongdoer; rather, the principal may be liable for the acts of the principal's agent. Accordingly, under common law, individual partners are often liable for the fraudulent conduct of their fellow partners. Notably, the Bankruptcy Act of 1867 only excepted from discharge debts that were obtained by the fraudulent actions of the debtor. However, the Act of 1898 and the Bankruptcy Code of 1978 eliminated the requirement that the debtor is the fraudulent actor—instead, a debtor's debts could be excepted from discharge even if they were not the fraudulent actor. In drafting new legislation, the U.S. Supreme Court said, Congress is aware of existing law, and in the case of section 523(a)(2)(A) specifically elected to use the passive voice rather than the active voice in drafting the legislation. *See id.* at 674-75. Accordingly, Congress must have intended section 523(a)(2)(A) to cover debtors in Mrs. Bartenwerfer's position.

In line with these principles, the U.S. Supreme Court concluded that Mrs. Bartenwerfer's debts were nondischargeable as a result of Mr. Bartenwerfer's fraudulent conduct. *See id.* Unfortunately for Mrs. Bartenwerfer, she was not so "innocent" under the law after all.

There are several important takeaways from this case. First, when preparing an argument, be sure to review older U.S. Supreme Court cases for insight, as these cases are precedential. Second, in applying the rules of statutory construction, one must revisit Ms. Crabtree's fourth grade grammar class and consider voice, tense, and case in interpreting statutes. For a higher degree of diligence, I suggest Justice Scalia's and Bruce Garner's treatise *Reading Law: The Interpretation of Legal Texts* (Thompson West 2012). Third, depending on state law, many debts may be considered joint debts between two partners under the law and therefore non-exempt under tenancy by the entirety principles, or alternatively entitle the trustee to sue the non-debtor spouse for contribution for such debts. Fourth, there has been a robust debate as to whether corporations in Subchapter V cases have an absolute right to a discharge under section 1192 of the Bankruptcy Code. The defenders of the absolute right to discharge argue that section 523 must be read as requiring that the debtor be the fraudulent actor, while other courts argue that the agent is irrelevant because of the presence of the passive voice; it is not *who* committed the forbidden act, these latter courts argue, but the *act itself*. However, that is the case for another day.

Tyler v. Hennepin County, 143 S.Ct. 1369 (2023)

Is a State's retention of excess proceeds from a tax foreclosure sale a "taking" within the meaning of the Fifth Amendment? Under Minnesota law, the U.S. Supreme Court says yes. In this case, plaintiff Geraline Tyler (**"Ms. Tyler"**), a 94-year-old widow and owner of a one-bedroom condominium in Hennepin County, Minneapolis (the **"County"**), lived alone in the condominium for more than a decade until she moved into a senior community. In Ms. Tyler's absence, the condominium accumulated approximately $15,000 in unpaid taxes, along with interest and penalties. Pursuant to Minnesota state forfeiture laws, the County seized and sold the condominium for $40,000 to satisfy the delinquent taxes. The County kept the remaining $25,000 in sale proceeds for its own use.

Ms. Tyler subsequently filed a putative class action against the County, alleging claims under the Takings Clause of the Fifth Amendment and the Excessive Fines Clause of the Eighth Amendment. The district court dismissed the suit for failure to state a claim. The Court of Appeals for the Eighth Circuit affirmed. Specifically, the Eighth Circuit held that Minnesota law did not recognize a property interest in surplus proceeds from a tax foreclosure sale conducted after adequate notice had been given to the property owner, and therefore that the County's retention of the $25,000 was not a "taking" within the meaning of the Fifth Amendment. The Eighth Circuit also held that the $25,000 forfeiture was not a "fine" within the meaning of the Eighth Amendment because it was intended to remedy the State's tax losses–not to punish Ms. Tyler.

The U.S. Supreme Court granted *certiorari* to explore the question of whether the County's retention of the excess $25,000 in sale proceeds from the tax foreclosure sale constituted a taking without just compensation as prohibited by the Fifth Amendment. The Court held that Ms. Tyler had plausibly alleged that the County's retention of the $25,000 in excess sale proceeds constituted a taking without just compensation. *Tyler*, 143 S.Ct. at 1380-81. The Takings Clause of the Fifth Amendment, made applicable to the States through the Fourteenth Amendment, provides that "private property [shall not] be taken for public use, without just compensation." U.S. Const. Amend. 5. The principle that one's government may not take more from an individual than what she owes is deeply rooted in English law, wherein the English Crown retained the power to sell a taxpayer's property to recover delinquent tax debts but was required to return any surplus from the sale to the taxpayer. *Tyler*, 143 S.Ct. at 1376. In line with this principle, Minnesota law recognizes a property right in a homeowner's financial interest in property, such as home equity. Additionally, the Court stated that Minnesota law also historically recognized that a homeowner whose property had been sold to satisfy outstanding property taxes had an interest in the excess proceeds recovered above the amount of the tax debt owed. *Id.* at 1375-79.

Since the Court found that Ms. Tyler had plausibly alleged a taking under the Fifth Amendment, the Court did not decide whether she had alleged an excessive fine under the Eighth Amendment. However, Justice Gorsuch, joined by Justice Jackson, writing in concurrence, stated that Minnesota's tax forfeiture scheme also violated the Excessive Fines Clause of the Eighth Amendment because it served in part to punish the delinquent taxpayer. "It matters not whether the scheme has a remedial purpose, even a predominantly remedial purpose" Justice Gorsuch wrote, "[s]o long as the law 'cannot fairly be said *solely* to serve a remedial purpose,' the Excessive Fines Clause applies." *Id.* at 1381 (internal citations omitted).

This decision provides an additional arrow in the quiver of bankruptcy trustees to avoid tax forfeiture sales of the debtor's property. However, a trustee must still look closely at state law and statutes of limitation before bringing forth such arguments.

Lac Du Flambeau Band of Lake Superior Chippewa Indians vs. Coughlin, 143 S. Ct. 1689 (2023)

In Lac Du Flambeau Band of Lake Superior Chippewa Indians vs. Coughlin, the U.S. Supreme Court considered the issue of tribal sovereign immunity, and specifically, whether a federally recognized Indian tribe may be subject to suit under the Bankruptcy Code. It is settled law that a recognized tribal nation retains its historic sovereign authority and therefore possesses common law immunity from suit traditionally enjoyed by sovereign powers. *Kiowa Tribe of Okla. Manuf. Techs, Inc.*, 523 U.S. 751, 756 (1998). But did Congress waive the sovereign immunity of federally recognized Indian tribes in bankruptcy cases through section 106 of the Bankruptcy Code? *See* 11 U.S.C. § 106(a)(1).

In this case, the Lac du Flambeau Band of Lake Superior Chippewa Indians, a federally recognized Indian tribe (the **"Tribe"**), operated several businesses that generate revenue for the Tribe. One of those businesses, Lendgreen—a wholly owned subsidiary of the Tribe—provided small loan, short-term, high interest financing to consumers.

Lendgreen provided a $1,100 loan to Brian Coughlin (**"Mr. Coughlin"**). Later that year, Mr. Coughlin filed a petition for relief under chapter 13 of the Bankruptcy Code. Despite the pendency of Mr. Coughlin's bankruptcy case, Lendgreen continued its efforts to collect on its loan, in violation of the automatic stay. In response to Lendgreen's collection activities, Mr. Coughlin filed a motion to enforce the automatic stay, and sought damages for emotional distress, along with costs and attorneys' fees. The Tribe filed a motion to dismiss for lack of subject matter jurisdiction, asserting tribal sovereign immunity.

The bankruptcy court dismissed the proceeding because of the Tribe's sovereign immunity. The bankruptcy court held that section 106 of the Bankruptcy Code abrogates sovereign immunity as to a "governmental unit", which, according to the bankruptcy court, the Tribe was not. "Governmental unit" is defined in the Bankruptcy Code as:

> United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States [. . .], a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government.

11 U.S.C. § 101(27). In reaching its conclusion, the bankruptcy court considered whether the phrase in section 101(27) "other foreign or domestic government" encompassed a recognized Indian tribe. Following the holding in In re Greektown Holdings LLC, 917 F.3d 451, 460 (6th Cir. 2019), which held that the phrase "other foreign or domestic government" was not explicit enough to cover Indian tribes, the bankruptcy court held that the Tribe had immunity against Mr. Coughlin's lawsuit.

The Court of Appeals for the First Circuit, in a split decision, reversed and followed the Ninth Circuit's decision in *Krystal Energy Co.*, 357 F.3d 1055 (9th Cir. 2004). The First Circuit held that the term "domestic government" included recognized Indian tribes. The First Circuit relied on Webster's Dictionary to bolster its conclusion: a tribe is a "government," and second, it is a *domestic* and not *foreign* government, as those terms are defined in Webster's Dictionary. Since the Tribe is a domestic government, the First Circuit concluded, it is a governmental unit within the meaning of section 101(27) and is therefore subject to suit under section 106 of the Bankruptcy Code. *See* 11 U.S.C. § 106(a)(1).

The U,S. Supreme Court granted *certiorari* to resolve a deep split among the circuits on the issue of tribal sovereign immunity. The Court held that the definition of "governmental unit" was comprehensive and extended to federally recognized Indian tribe, thereby abrogating their sovereign immunity and exposing them to suit under the Bankruptcy Code. Congress may only abrogate sovereign immunity by expressing its "unmistakably clear" intent to do so in the language of the applicable statute. *Coughlin*, 143 S.Ct. 1695. The Court stated that no "magic [] words" were required for Congress to abrogate sovereign immunity, but "if 'there is a plausible interpretation of the statute' that preserves sovereign immunity, Congress has not unambiguously expressed the requisite intent" to abrogate that immunity. *Id.* Applying this principle to section 106, the Court held that "the Bankruptcy Code unequivocally abrogates the sovereign immunity of any and every government that possesses the power to assert such immunity. Federally recognized tribes undeniably fit that description; therefore, the Code's abrogation provision plainly applies to them as well." *Id.* at 1696. Accordingly, the Court held that the Tribe was not immune from Mr. Coughlin's lawsuit, thereby also abrogating *In re Greektown Holdings LLC*, 917 F.3d 451 (6th Cir. 2019). Following this case, federally recognized Indian tribes do not enjoy the protections of sovereign immunity in bankruptcy cases.

Justice Gorsuch, writing in dissent, argued that Indian tribes "enjoy a unique status" under the law, and stated that Congress did not clearly and unequivocally express its intent to abrogate tribal immunity in the language of section 106 of the Bankruptcy Code. *Id.* at 1704. "A 'necessary corollary to [] Indian sovereignty" is immunity from private suit,'" he stated. *Id.* Because, in Justice Gorsuch's eyes, Congress failed to "supply a clear statement" that tribes are "governmental units" for which sovereign immunity is abrogated under section 106, Justice Gorsuch declined to join the majority's opinion.

MOAC Mall Holdings LLC v. Transform Holdco LLC, 143 S.Ct. 927 (2023)

In MOAC Mall Holdings LLC v. Transform Holdco LLC, the U.S. Supreme Court considered whether section 363(m) of the Bankruptcy Code is a jurisdictional provision. Section 363(m) provides:

> [t]he reversal or modification on appeal of an authorization under subsection (b) or (c) of this section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or

> not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

In this case, Sears, Roebuck and Co. (**"Sears"**) filed for chapter 11 bankruptcy and self-administered its case as a debtor in possession. In its capacity as debtor in possession, Sears exercised its statutory power to sell most of its assets to Transform Holdco LLC (**"Transform"**), an entity controlled by Edward Leppert, a former insider of Sears. The bankruptcy court entered an order approving the sale (the **"Sale Order"**).

As part of the sale, Transform acquired the right to designate an assignee to any lease between Sears and its landlords. One such lease eligible for assignment was Sears' lease with MOAC Mall Holdings LLC (**"MOAC"**), which leased space to Sears at the Minnesota Mall of America (the **"MOAC Lease"**).

As relevant to this case, section 365 of the Bankruptcy Code prohibits the assignment of an unexpired lease without "adequate assurance of future performance by the assignee." 11 U.S.C. § 365(f)(2)(B). That statute also sets forth special adequate assurance criteria specific to "shopping center[s]" like the Mall of America.

Transform designated the MOAC Lease to its wholly owned subsidiary. MOAC objected to the assignment on the basis that Sears had failed to provide adequate assurance of future performance by the assignee. The bankruptcy court, however, approved the assignment over MOAC's objections (the **"Assignment Order"**).

MOAC sought to appeal the Assignment Order, but feared that the restrictions of section 363(m) would limit or bar its appeal. Accordingly, MOAC sought to foreclose any such argument by Transform by seeking a stay of the Assignment Order. Before the bankruptcy court, Transform argued that section 363(m) did not apply to the Assignment Order, and ensured MOAC that it would not raise the issue on appeal. Based upon those representations, the bankruptcy court denied MOAC's stay motion

Following the denial of MOAC's stay motion, the Assignment Order became effective. MOAC subsequently appealed the Assignment Order to the district court, which initially vacated the Assignment Order "to the extent it approved" the assignment of the MOAC Lease to Transform. *In re Sears Holdings Corp.*, 613 B.R. 51, 79 (S.D.N.Y. 2020). Apparently forgetting what it represented to the bankruptcy court, Transform sought rehearing on the basis that section 363(m) deprived the district court of jurisdiction to consider MOAC's requested relief. The district court—although "appalled" by Transform's change in position—determined that Second Circuit law required the district court to treat section 363(m) as jurisdictional, and therefore "not subject to waiver [or] judicial estoppel." *See Contrarian Funds LLC v. Aretex LLC*, 600 F.3d 231 (2d Cir. 2010). MOAC appealed to the Court of Appeals for the Second Circuit.

The Second Circuit reaffirmed its prior precedent, stating that section 363(m) applied to orders that were not entered pursuant to section 363(a) or (b) if the ancillary order subject of the appeal is integral to the protected transaction. The Second Circuit concluded that Transform's assignment designation rights granted to Transform were integral to the entire transaction under the Sale Order and the Assignment Order, and were therefore valid and protected under 363(m). *See Sears*, 2021 WL 5986997, at *2 (2d Cir. 2021).

The U.S. Supreme Court granted *certiorari* to resolve a substantial circuit split as to whether section 363(m) operates as a jurisdictional provision—*i.e.*, one that must be rigidly raised and enforced. Following Transform's belated raising of section 363(m), the district court stated that "if ever there were an appropriate situation for the application of judicial estoppel, this would be it." *Sears*, 616 B.R. at 627. But if section 363(m) truly is a jurisdictional provision, then "not even such egregious conduct [by Transform] could permit the application of judicial estoppel" against it. *Sears*, 143 S.Ct. at 936.

The U.S. Supreme Court, however, held that section 363(m) is not a jurisdictional provision, thereby reversing the Second Circuit. *Id.* at 936-37. The Court highlighted the distinction between a court's statutory authority and subject matter jurisdiction, stating that section 363(m) "reads like a 'statutory limitation,' . . . that is tied in some instances to the need for a party to take 'certain procedural steps at certain specified times[,]" not a provision that must be rigidly applied by the court. *See id.* at 937. Furthermore, section 363(m) is separated from Bankruptcy Code provisions providing for federal courts' jurisdiction over bankruptcy matters. Accordingly, the Court determined that Congress had not "clearly stated" that section 363(m) "is a limit on judicial power, rather than a mere restriction on the effects of a valid exercise of that power[.]" *Id.* at 939. Because the Second Circuit's opinion was based on its erroneous decision that section 363(m) was jurisdictional, the Court vacated the judgment and remanded to the Second Circuit for further proceedings. *Id.* at 940. The Court also suggested that the doctrine of judicial estoppel barred Transform from raising its section 363(m) argument again before the district court. ■

COMMERCIAL LAW LEAGUE HAS PARTNERED WITH LORMAN EDUCATION FOR CONTINUING EDUCATION

The Commercial Law League is dedicated to providing cost-effective training opportunities that meet the needs of our members and enhance your skills, knowledge, and competencies. The Commercial Law League has partnered with Lorman Education Services to provide continuing education in a variety of topic areas.

ACCESS TO CONTINUING LEGAL EDUCATION (CLE) AND CONTINUING EDUCATION (CEU) UNITS

Each time you attend a course with Lorman Education Services, you will have the opportunity to request approved CLE's/CEU's prior to the program. Upon completion of the course, you will be provided a certificate of completion reflecting the CLE's/CEU's you requested. If CLE's/CEU's are not requested, you will be provided a general certificate of completion for each course. If you would like to find a specific credit you can search from Lorman's main Training page and if you have additional credit questions, please reach out to creditinfo@lorman.com.

CREATE A FREE ACCOUNT AND RECEIVE A COMMERCIAL LAW LEAGUE MEMBER DISCOUNT

Members receive a 20% discount on all orders. You first must register for a free account. Register online at http://www.lorman.com/training/CLLA or call Lorman at 866-352-9539. Please use Priority Code 19295 and Discount Code H9587528 when registering.

FOR MORE INFO, PLEASE VISIT
www.lorman.com/training/CLLA

Jack Rose
Partner
The Law Offices of Jack J. Rose, PLLC
CEO
JR2G LLC

HOW FAST IS TOO FAST? A CLOSER LOOK AT 24-HOUR BANKRUPTCIES

In our fast-paced world, speed is everything. From social media platforms like TicToc, to the convenience of online shopping and same-day delivery. But when it comes to matters of legal rights and due process, should speed be the governing principal?

In the realm of bankruptcy, it seems like we may be heading down a dangerous path. There is a growing trend of cases that wrap up within 24 hours – an alarming speed for complex matters. Companies like Full Beauty and Belk have become members of what we call the "24-hour club." In certain cases this may be necessary to prevent a debtor from suffering irreparable harm to its reputation or financial arrangements that substantially reduce the likelihood of a successful restructuring. In cases where a "True Balance Sheet" restructuring occurs, with those in higher positions in the Cap Stack agreeing to take a haircut while creditors lower down sail through the cases not only unimpaired but without impact, a 24-hour case may be appropriate. However, there is a slippery slope in the bankruptcy world, where smart lawyers and financial advisors push the envelope.

Judges like Marvin Isgur and Robert Drain have taken great care in their orders to assure that proper notice was given before the filing of the case and the right to object was reserved after confirmation. They also have looked to the effects of these cases.

The Bloomberg Practical Guide states,

> It is important to note that a 1-Day Prepack is not a viable mechanism for a case seeking to reject burdensome leases and contracts, sell assets, or compromise litigation claims. A 1-Day Prepack may also be inappropriate for a publicly held company seeking to wipe-out publicly-held equity. None of the aforementioned 1-Day Prepacks involved publicly held equity, and it is unclear how a court would handle this type of a case in such a short timeframe.
>
> In the context of the *Sungard* confirmation, Judge Drain of the Bankruptcy Court for the Southern District of New York indicated that a 1-Day Prepack might not be appropriate where there were creditor objections and a contested confirmation hearing. As such, the 1-Day Prepack mechanic lends itself to completely consensual restructuring situations without impaired objectors.

1-Day Prepackaged Bankruptcy, Bloomberg Practical Guidance, Sarah Borders and Stephen Blank, August, 2021.

However, bankruptcy lawyers and financial advisors love to push the envelope. Let's take a closer look at a specific scenario that could be the next case in the "24-hour club." Imagine a debtor rejecting multiple leases on Day-1 (the only day of the case). We know there have been warnings against lease rejections in a 24-hour case --- **keep reading, the landlord creditors are unimpaired!!!** And, the debtor provides for payment in full of all lease rejection damages under the Plan. Thus, the landlords are unimpaired creditors. **See what we mean – they are unimpaired!!!**

What harm could there be? The debtor maintains its business operations, the landlords receive full payment for their claims, and they have ample opportunity to voice any objections after the effective date. The debtor is relieved of burdensome leases, and the case is concluded within 24 hours, before all but the fastest of landlords could even appear in court.

At first glance, everything appears to be in line with the Bankruptcy Code. However, there are a few points that should be examined – the lack of a Creditor's Committee seems to stand out; no one aside from those directly involved in the negotiations had the chance to review any of the relevant documents in the case, including the Disclosure Statement, Plan, or financing documents and additionally, very few creditors were even aware of the case before it concluded. While this hypothetical case is one example that we hope never materializes, there is a lingering concern that it might.

Isn't bankruptcy supposed to be an open and transparent process? How open can a process be that adjusts hundreds of millions of dollars in debt in less than 24 hours? There may be limited situations where "24-hour cases" are justified, but judges need to be diligent like Judges Drain and Isgur to insure that such cases remain the exception to the rule rather than becoming the new "normal" for Chapter 11 cases. ■

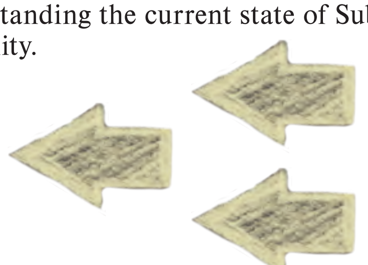
Peter M. Gannott
Attorney
Gannott Law Group PLLC

SUBCHAPTER V BUSINESS BANKRUPTCY ELIGIBILITY: UNDERSTANDING THE CONFLICTING DECISIONS

The Small Business Reorganization Act (SBRA), codified as 11 U.S.C. §§ 1181-1195, created a new Subchapter V, which applies only to a subset of Chapter 11 debtors. This law broadened the relief available to small businesses and streamlined the existing reorganization processes to improve the ability of small businesses to reorganize. Since its addition to the Bankruptcy Code in 2020, courts have provided conflicting decisions on the eligibility requirements under Subchapter V.

To proceed under Subchapter V, the bankrupt party must meet the definition of a debtor under § 1182(1) and must elect its application under§ 103(i). An eligible Subchapter V debtor must be a "person": (1) engaged in commercial or business activities; (2) with aggregate noncontingent, liquidated secured and unsecured debts not exceeding the debt limit of $7.5 million; (3) with at least 50% of the debts arising from the debtor's commercial or business activities.[1] The term "person" generally includes individuals, partnerships, and corporations.[2] Hence, Subchapter V applies to actions which can be performed by either individuals or businesses (both incorporated or unincorporated). On the other hand, an eligible debtor does not include: (1) a member of a group of affiliated debtors with aggregate noncontingent, liquidated secured and unsecured debts exceeding $7.5 million; (2) a debtor that is subject to reporting requirements under the Securities Exchange Act of 1934; or (3) a debtor whose primary activity is the business of owning single-asset real estate (SARE).[3]

Understanding the conflicting decisions relating to a debtor's Subchapter V eligibility is important, since avoiding a traditional Chapter 11 filing will frequently alter the procedural and substantive results of the bankruptcy. Key Subchapter V eligibility issues include: (1) which party has the burden of proving the debtor meets the requirements of the Subchapter; (2) what does being "engaged in" commercial or business activities mean; (3) what constitutes "commercial or business activity"; (4) which debts count toward the $7.5 million threshold; and (5) what is required to prove over 50% of the debts arise from commercial or business activities. Becoming acquainted with the conflicting decisions on these issues is important for understanding the current state of Subchapter V eligibility.



1. WHICH PARTY HAS THE BURDEN OF PROVING DEBTOR'S SUBCHAPTER V ELIGIBILITY?

Resolving who has the burden of proof is an important first step in determining whether a debtor can proceed under Subchapter V. A majority of courts have concluded that Subchapter V offers many advantages over a traditional Chapter 11 case and placed the burden of proof on the debtor.[4] The Ninth Circuit Bankruptcy Appellate Panel ("BAP") in *In re NetJets Aviation*[5] reasoned that the debtor has the burden for establishing Subchapter V eligibility since the burden lies with a Chapter 12 debtor, which contains the analogous requirement that a "family farmer" be "engaged in a farming operation." Additionally, *NetJets Aviation* held that placing the burden on debtor was justified because it is in the best position to prove it is qualified to be in Subchapter V.[6]

Several other courts have come to the opposite conclusion, holding that the objecting party has the burden to prove debtor is not eligible to proceed in Subchapter V. They hold that the movant normally has the burden of persuasion, so a party challenging Subchapter V status must prove debtor is ineligible.[7] Likewise, a movant filing an objection to a Subchapter V election on the ground that debtor is a Single Asset Real Estate Entity ("SARE") under §101 (51B)[8], may have the burden of proof consistent with prior SARE decisions.[9] Without more decisions placing the burden of persuasion on the movants, it seems likely that debtors will need to be prepared to prove they meet the Subchapter V qualifications.

2. WHAT IS REQUIRED TO PROVE DEBTOR IS "ENGAGED IN" COMMERCIAL OR BUSINESS ACTIVITY?

Courts are divided when interpreting what is required to prove a debtor is "engaged in" commercial or business activity. Two bankruptcy courts have held in unpublished decisions that debtor need not currently be "engaged in" commercial or business activities to qualify for Subchapter V, so long as it was

1 11 U.S.C.§ 1181(1)(a); *In re Ikalowych,* 629 B.R 261, 275-276 (Bankr. D. Colo 2021).

2 11 U.S.C. § 101 (41); *In re Quadruple D Trust*, 639 B.R. 204, 236-237 (Bankr. D. Colo. 2022) (The trust was not authorized to proceed as a Subchapter V debtor, since it was not a "business trust" as defined under 11 U.S.C. § 101.).

3 11 U.S.C. § 1182(1).

4 E.g., *In re Evergreen Site Holdings, Inc.*, 2023 Bankr. LEXIS 1649 (Bank. S.D. Oh. 6/21/23) (citing cases).

5 *NetJets Aviation, Inc. v. RS. Air, LLC* (In re RS Air, LLC), 638 B.R. 403 (B.A.P. 9th Cir. 2022).

6 *Id*., at 413-414.

7 *In re Body Transit, Inc.*, 613 B.R. 400, 409 n. 15 (Bankr. E.D. Pa. 2020) (The objecting party is the de facto movant and, absent a contrary provision in the Bankruptcy Code or Rules, the movant bears the burden of proof when requesting relief from the court.); *Hall L.A. WTS, LLC v. Serendipity Labs, Inc. (In re Serendipity Labs, Inc.)*, 620 B.R. 679, 679 n.3 (Bankr. N.D. Ga. 2020) (same).

8 11 U.S.C. §101 (51B).

9 *In re 218 Jackson LLC*, 2021 Bankr. LEXIS 2284 (Bankr. M.D. Fla. 6/3/21) (The movant challenging debtor's Subchapter V status on the ground that it is a SARE bears the burden of proof.).

engaged in such activities at some point in the past.[10] More recently, courts reviewing Subchapter V eligibility have found "engaged in" requires proof that debtor is currently – as opposed to formerly – engaged in commercial or business activities.[11] These courts hold the "engaged in" inquiry is a contemporary focus instead of retrospective, requiring assessment of the debtor's current status as of the filing of the bankruptcy petition.

Virtually all courts have applied a broad and encompassing construction of the "engaged in commercial or business activities" phrase based on a totality of the circumstances. This approach was followed by the Ninth Circuit BAP in *NetJets Aviation*[12] which is the first appellate panel to rule on this issue. In this case, RS Air, LLC (RS Air) was formed to provide aircraft transportation services, acquire, and sell interests in aircraft, and provide depreciation tax benefits for its sole owner and manager, Stephen Perlman. RS Air had agreements with NetJets Aviation, Inc. ("NetJets") to purchase fractional interests in private jets. RS Air and NetJets had a falling out resulting in a state court lawsuit where NetJets alleged breach of contract and RS Air counterclaimed for breach of contract and fraud. As a result of these disputes, RS Air ceased normal flight operations and filed a Subchapter V bankruptcy, with NetJets holding 98% of the non-insider debt.

The BAP affirmed the bankruptcy court's decision finding debtor was authorized for Subchapter V eligibility based on: (1) its litigation with NetJets; (2) staying in good standing; (3) keeping current on tax obligations and registry fees; and (4) having the intent to reengage in buying and selling fractionalized aircraft interests in the future.[13] The BAP concluded that debtor "need not be maintaining its core or historical operations on the petition date, but it must be 'presently' engaged in some type of commercial or business activities to satisfy§ 1182(1)(A)."[14] The BAP's decision demonstrates the breadth of what it means to engage in commercial or business activities.

Applying this broad construction, courts have recognized a variety of wind-down functions are sufficient to meet the requirement that debtor is engaged in commercial or business activities. The debtor was permitted to proceed under Subchapter V in *In re Offer Space*[15] during its wind down process, because it maintained a bank account, held accounts receivable, explored claims against a third party, and was taking reasonable steps to pay its creditors and realize value for its assets. The same result was reached in *In re Port Arthur Steam Energy, L.P.*[16] where debtor satisfied the eligibility requirement because it was actively pursuing litigation against a third-party, seeking to collect accounts receivable and selling assets, and oversaw an independent contractor maintaining its facility. More recently, the court in *In re Hillman*[17] held that an individual qualified for Subchapter V relief because she was being sued in state court on her personal guaranty of debt incurred by her defunct business. In short, the liberal interpretation of Subchapter V allows a debtor to proceed under this Subchapter if it will engage in some minimal amount of future activities related to its pre-petition operation.

3. WHAT IS REQUIRED TO PROVE DEBTOR'S "COMMERCIAL OR BUSINESS ACTIVITY"??

There is no statutory definition of what constitutes "commercial or business activities" under Subchapter V, so courts turn to the plain language of the statute to determine the meaning of the phrase.[18] By using this approach, two early decisions construed the "commercial or business activities" phrase as requiring that the Subchapter V debtor must be "participating in purchasing or selling goods or services for a profit."[19] Since then, the case law has developed so that a "profit motive" is no longer required. The Ninth Circuit BAP in *NetJets Aviation*[20] stated that "we conclude that no profit motive is required for a debtor to qualify for Subchapter V relief. To hold otherwise would wrongfully exclude nonprofits and other persons that lack such a motive." In *In re Ellingsworth*[21] the court expressly held that a non-profit business could file for bankruptcy under Subchapter V. The unsecured creditor in this case argued that the debtor — a nonprofit homeowners association — was not eligible for Subchapter V because, as a nonprofit, it did not "engage in commercial or business activities." The bankruptcy court disagreed and found that no profit motive is required by the statute.[22] The court held that the many of the activities the nonprofit debtor engaged in fit the "broad" category of commercial or business activities (i.e., contracting for goods and services, hiring professionals, filing regular tax returns, collecting assessments from its homeowners, etc.).[23]

10 *In re Blanchard*, 2020 Bankr. LEXIS 1909 (Bankr. E.D. La. 7/16/20) (finding that "engaged in" has no temporal limit); In re Wright, 2020 Bankr. LEXIS 1240 (Bankr. D. S.C. 4/27/20) (debtor need not be "currently" engaged in commercial or business activities on the petition date).

11 *E.g., NetJets Aviation*, 638 B.R. at 409-410; *In re Offer Space, LLC*, 629 B.R. 299, 305-07 (Bankr. D. Utah 2021).

12 *NetJets Aviation*, 638 B.R. at 411.

13 *Id.*

14 *Id.*

15 629 B.R. 299, 306-307 (Bankr. D. Utah 2021).

16 629 B.R. 233, 237-238 (Bankr. S.D. Tex. 2021).

17 2023 Bankr. LEXIS 1448 (Bankr. N.D. NY 6/2/23).

18 *Offer Space*, 629 B.R. at 305-06.

19 *In re Blue,* 630 B.R. 179, 189 (Bankr. M.D. NC 2021); *In re Johnson*, 2021 Bankr. LEXIS 471, 2021 WL 825156 (Bankr. N.D. Tex. 3/1/21).

20 638 B.R. at 411.

21 619 B.R. 519, 520-521 (Bank. M.D. Fla. 2020).

22 *Id*. at 521.

23 *Id*.

The requirement that debtor be engaged in "commercial or business activity" is broad, but not limitless. *In Thurmon*[24] illustrates a situation where debtors were not eligible to proceed under Subchapter V, because they were not engaged in commercial or business activities on the petition date. *Thurmon* involved joint debtors who were retired from their pharmacy businesses, did not intend to return to work and most of the companies' assets were sold. Merely maintaining an empty shell business in good standing with the state was not sufficient to qualify as a Subchapter V debtor. Similarly, the debtors in *In re McCune*[25] did not qualify for Subchapter V, because their business had not been operating for years, had no revenue, no employees, no customers, no vendors, were not liquidating assets or engaged in any activities required by § 1182(1)(A). Accordingly, debtor must be engaged in some minimal level of commercial or business activity to satisfy the requirements of § 1182(1).

4. WHICH DEBTS ARE COUNTED WHEN DECIDING SUBCHAPTER V ELIGIBILITY?

Subchapter V eligibility requires that debtor have noncontingent, liquidated, secured and unsecured liabilities that do not exceed $7,500,000. Debts that are contingent (such as a claim based on a guarantee of a third-party debt) or unliquidated (such as a tort claim) are not counted toward the $7.5 million threshold. Thus, a larger business that has reduced its liquidated non-contingent debts below $7.5 million -- but is facing significant contingent litigation claims -- might be able to squeeze its case into Subchapter V despite potentially large claims.

There is a split of authority on how unexpired lease damages are counted when deciding if debtor's liabilities are below the $7.5 million cap. The debtor in *In re Parking Mgmt.*[26] claimed it stayed under the debt limit by using a lower "lease rejection damage" figure, instead of the full unexpired lease amount, for the anticipated claim value. The bankruptcy court allowed the debtor to proceed under Subchapter V, holding the amount of unpaid lease rejection damages was "contingent" requiring post-petition court approval.[27] In contrast, the bankruptcy court in *In re Macedon Consulting, Inc.*[28] concluded on similar facts that debtor was not eligible to proceed under Subchapter V. Macedon rejected debtor's argument that it met the $7.5 million requirement by using the amount of lease rejection damages, and concluded the entire unpaid unexpired lease amount would be counted toward the debt limit. These conflicting decisions leave open the possibility that a debtor with a large unexpired lease debt may still qualify for a Subchapter V bankruptcy, or not.

Another issue relating to which debts count toward the Subchapter V debt limit arises when an affiliate of debtor also files bankruptcy. Section 1182(1)(B)(i) bars a debtor from Subchapter V status if it is a "member of a group of affiliated debtors under this title that has aggregate noncontingent liquidated secured and unsecured debts in an amount greater than $7,500,000." This provision has significant implications for debtors with related entities that may have substantial liabilities. The issue was recently considered by the court in *In re Free Speech Sys., LLC*[29] in connection with the bankruptcy filed by radio host Alex Jones, who gained notoriety for stating on his show that the Sandy Hook school massacre was a hoax. In July 2022, Free Speech Systems, LLC (the parent company of InfoWars) filed for bankruptcy and elected to proceed under Subchapter V. In December of that year, Alex Jones, the owner of Free Speech Systems, filed his own ordinary chapter 11 bankruptcy case. A group of plaintiffs with defamation lawsuits pending against Jones filed a motion to revoke the Subchapter V election of Free Speech Systems. Plaintiffs conceded that Free Speech Systems had less than $7.5 million in debt on the petition date, but contended it lost Subchapter V eligibility when Jones (an affiliate) filed his own chapter 11 petition. The court rejected this argument, since Subchapter V eligibility is determined on the petition date.[30] The decision in the Alex Jones bankruptcy case establishes that a debtor with debts below the $7.5 million limit may exploit the Subchapter V process by having an affiliate with a disqualifying amount of debts file bankruptcy later.[31]

5. WHAT IS REQUIRED TO PROVE 50% OF THE DEBTS AROSE FROM COMMERCIAL OR BUSINESS ACTIVITY?

Section 1182(1) requires that at least 50 percent of the debts must arise from commercial or business activities of the debtor to be eligible to satisfy the Subchapter V requirement. The Bankruptcy Code does not define when a debt arises from "commercial or business activities," so courts have looked to the definition of "consumer debt" when considering this issue. "Consumer debts" is defined under § 101(8) as a "debt incurred by an individual primarily for personal, family, or household purpose." *In Ellingsworth*,[32] the court determined that a debt that arises from a commercial or business activity is one that is not of a

24 625 B.R. 417, 421-422 (Bankr. W.D. Mo. 2020).

25 635 B.R. 409, 420-21 (Bankr. D.N.M. 2021).

26 620 B.R. 544 (Bankr. D. Md. 2020).

27 *Id.*, 620 B.R. at 554-555.

28 2023 Bankr. LEXIS 1551 (Bank. E.D. Va. 6/14/22).

29 649 B.R. 729 (Bankr. S.D. Tex. 2023).

30 *Id,* at 732-733.

31 *In re Dobson*, 2023 Bankr. LEXIS 1311 (Bank. W.D. Va. 5/17/23) (The debts of an affiliate did not disqualify individual debtors from seeking Subchapter V relief, since the affiliate filed its chapter 7 bankruptcy one day after the individuals' Subchapter V filing.).

32 *Ellingsworth*, 619 B.R. at 520.

personal, family, or household nature. The *Sullivan*,[33] decision followed this approach and concluded that debtor's marital property settlement debt to pay his ex-wife a share of the value of his business did not arise from a commercial or business purposes, so debtor could not reorganize under Subchapter V.

Courts are split on whether there must be a nexus between the qualifying debt and the debtor's commercial or business activities on the petition date. The genesis of this conflict is the Bankruptcy Code's language stating in § 1182(1)(A) that more than half of debtor's debts must have arisen from "*the* commercial or business activities" of the debtor. The *In re Ikalowych*[34] decision is often cited as the seminal case finding a nexus requirement between the debtor's engagement in commercial or business activities and the qualifying debt necessary to be eligible for Subchapter V. In so finding, the bankruptcy court explained as follows:

> But there is an important "the" in the Section 1182(1)(A) statutory text. More than half of the Debtor's debts must have arisen from "the commercial or business activities of the Debtor." So, the debt must be tied to the particular type of commercial or business activities the Debtor engaged in.[35]

Over 50% of the bankruptcy debt in *Ikalowych* was based on loan guarantees the individual debtor gave to the lender of his failed business. The court concluded that debtor was required to show that the debt was "directly and substantially connected to the 'commercial or business activities' of debtor."[36] Debtor qualified for Subchapter V relief since over half the debt related to his guarantee of his business' loan default.

Other courts have rejected this "nexus" requirement. They hold that fifty percent or more of the total debt relating to any commercial or business activity is sufficient, even if debtor is no longer engaged in the activities producing the debt.[37] Recently, the court in *In re Reis*[38] was called to decide if a doctor's medical school debt could be relied upon to satisfy Subchapter V requirement that 50% of the debt must be related to her medical business. The court concluded debtor was not required to prove a nexus between the medical school debt and her medical practice. Nevertheless, debtor could not proceed under Subchapter V, because the student loan debt was incurred over ten years prior to opening her medical practice, so it was too far removed from her ultimate business activity and could not be categorized as a business debt. Although the language of § 1182(1)(A) can be read to require a nexus between the qualifying debt and debtor's commercial or business operations, the expansive approach to Subchapter V eligibility followed by many bankruptcy courts suggests that the nexus requirement will not be widely imposed.

CONCLUSION

Numerous judicial decisions have been issued interpreting the eligibility requirements of Subchapter V since it took effect in 2020. Not surprisingly, courts have reached conflicting results as they struggle with unique fact patterns and novel legal arguments. Bankrupt parties have pushed the limits of Subchapter V's eligibility requirements with some courts allowing the case to proceed, while others have reached the opposite conclusion under essentially the same facts. Consequently, it is critical to understand the key Subchapter V eligibility issues currently dividing the courts to assess how the law is likely to develop in the future. ■

33 626 B.R. 326, 331 (Bankr. D. Colo. 2021).

34 629 B.R 261, 287-288 (Bankr. D. Colo 2021).

35 *Id.*

36 *Id.* at 288.

37 *E.g., In re Blue*, 630 B.R. 179, 191 (Bankr. M.D.N.C. 2021) ("Nothing in the statute requires that there be a nexus between the qualifying debts and the Debtor's current business or commercial activities.").

38 2023 Bankr. LEXIS 1169 (Bank. D. Idaho 5/2/23).

Our Way of Saying...

Thank You!

REFER A PROSPECT FOR MEMBERSHIP WHO JOINS AND RECEIVE A $50 GIFT CARD*

COMMERCIAL LAW LEAGUE OF AMERICA
EXPERTISE • INSIGHT • RESULTS

CONTACT Dawn Federico at 312-240-1400
or
at dawn.federico@clla.org

** Former CLLA members do not qualify for gift card promotion.*
You must fill out the referral form online at https://clla.formstack.com/forms/clla_membership_referral_form in order to receive the gift card once your prospect joins.

Amy Kiser, Esq.
Partner
Gilbert Garcia Group, P.A.

THE ISSUES WITH POST-PETITION FEE NOTICES

As most bankruptcy attorneys know, the rules vary depending on the jurisdiction and the judge. Even judges in the same district follow different procedures. This is especially true when it comes to recovery of creditor's attorney fees in Chapter 13 cases.

Rule 3002.1 sets forth the requirements for providing notices related to claims secured by the debtor's primary residence. Pursuant to 3002.1 holders of secured claims must file a notice itemizing fees and charges incurred after the petition date within 180 days of the date the fees are incurred. Sounds simple enough, but as evidenced by the significant increase in objections to creditor's fee notice, it has become anything but simple. More and more creditors are faced with the dilemma of whether or not to file a post-petition fee notice.

When faced with an objection to a post-petition fee notice, a creditor must prove they are entitled to the fee. Courts will look to the underlying agreements and non-bankruptcy law to determine entitlement to attorney fees.[1] Most residential mortgages include provisions providing for recovery of fees incurred in connection with the enforcement of the mortgage and incurred to protect the secured creditor's interest. However, one court disallowed the requested fees where the mortgage did not unambiguously provide for the collection of attorney fees for bankruptcy plan review or for filing fees or court costs related to proof of claim preparation.[2] In *Clark*, the debtor's plan proposed to pay the mortgage direct.[3] The creditor filed a post-petition fee notice in the amount of $300.00 for filing fees and court costs related to its proof of claim and $350.00 for the plan review.[4] The debtor objected and argued that the underlying agreement does not allow for recovery of attorney's fees from the debtor.[5] A lender is only permitted to collect mortgage fees, expenses, and charges in bankruptcy if the underlying agreement or applicable non-bankruptcy law so permit.[6] The court held that within the four corners of the underlying loan documents, the mortgage did not contain unambiguous language establishing a mortgagor obligation for mortgagee attorney fees for bankruptcy plan review or for filing fees or court costs related to proof of claim preparation.[7] As such the court ruled the the fees are disallowed.[8] Accordingly, the loan documents must always be reviewed prior to filing a post-petition fee notice to ensure recovery of said fees is allowed under the terms of the loan documents.

1 11 U.S.C 1322(e)

2 *In re Clark*, 593 B.R. 661 (Bankr. S.D. Ala. 2018).

3 *Id.*

4 *Id.*

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.*

Objections related to reasonableness of the creditor's requested fees filed by debtors and trustees have become routine. Unfortunately, many judges are agreeing with the debtors and trustees and are significantly reducing the amount of fees owed to creditors. One of the most common arguments alleges that preparation of proof of claims and Chapter 13 plan reviews are inconsequential ministerial tasks. In Florida, these reasonableness objections are usually sustained in part and creditor attorney's fees are drastically reduced.[9] A creditor in the Southern District of Florida filed a post-petition fee notice seeking fees in the amount of $950.00 for the proof of claim and plan review.[10] The court, without providing any reasoning, reduced the fees to a total of $225.00.[11] In another Southern District of Florida case, a creditor filed its post-petition fee notice seeking $510.00 for the proof of claim and $390.00 for a plan review.[12] The debtor, whose plan proposed to the pay the claim directly, objected and argued the fee was not reasonable.[13] The court agreed with the debtor and found the fees were excessive and unreasonable as the debtor's case is simple and the plan proposes to pay the claim directly.[14] In In re Cousins, another Southern District of Florida case, the debtor objected to creditor's fees in the amount of $500.00 for a proof of claim and $450.00 for a plan review.[15] The plan in *Cousins* proposed to cure the arrears and maintain the ongoing monthly payment.[16] Despite the proposed plan treatment, the Court found the fees excessive and unreasonable.[17] The court reduced creditor's fees to $500.00.[18]

However, some courts do recognize the risks posed to lenders when a borrower files for bankruptcy and recognize that the risks can be mitigated by having an attorney review the plan, petition, loan documents and by having an attorney prepare the proof of claim.[19] The court in Mandeville details the consequences of filing an inaccurate proof of claim.[20] Filing a proper proof of claim constitutes prima facie evidence of the validity and amount of the claim.[21] Moreover, filing a defective claim could deprive a creditor of the prima facie evidentiary presumption of validity and amount, or, it could preclude the creditor from presenting the omitted information, as evidence in any contested matter or

9 *See In re England*, 586 B.R. 795 (Bankr. M.D. Ala. 2018)

10 *In re Zabchuck*, 21-10815-EPK (May 17, 2021)

11 *Id.*

12 *In re Chiarenza*, 21-10492-MAM (September 29, 2021)

13 *Id.*

14 *Id.*

15 *In re Cousins*, 20-23868- MAM (September 29, 2021)

16 *Id.*

17 *Id.*

18 *Id.*

19 *See In re Mandeville*, 596 B.R. 750 (Bankr. N.D. Ala 2019).

20 *Id.*

21 *Id.*

adversary proceeding and entitle the objecting party to reasonable attorney's fees caused by the failure.[22] Another risk to creditors is that creditors are bound by the provisions of the confirmed plan, even if that plan improperly modifies their claim.[23] These risks demonstrate the importance of having an attorney file the proof of claim and review the plan on behalf of the creditor and justify reimbursement of the attorney's fees as contemplated by the terms of the underlying loan documents.[24]

To combat the uncertainty, some jurisdictions have instituted a "no look" threshold, which means the trustee will not object if the fee is below those threshold amounts. For example, the Northern District of Texas has a "no look" fee amount of $700 whereby any fees requested below $700 are presumptively reasonable and anything above $700 requires supporting documentation with an attached itemization of services provided.[25] The Southern District of Florida also has recently enacted a "safe harbor" amount of $525.00 for preparation and filing of the proof of claim, plan review and filing of any objections to the plan.[26] Other courts have an unwritten or informal no look threshold. For example, one trustee's office in Florida has a "no look" threshold of $865.00 for creditor attorney's fees incurred during the proceedings.

The "no-look" threshold will not prevent a creditor from seeking fees in excess of the "no-look" threshold. The Northern District of Texas allowed a creditor to recover fees in the amount of $900.00, which is $200.00 over the "no-look" threshold.[27] The Trustee in *Garcia* objected after the creditor filed two post-petition fee notices which totaled $900.00 in fees and expenses.[28] The Trustee argued that the creditor was stacking its attorney fees in an attempt to avoid the the "no-look" threshold.[29] The creditor filed a response to the Trustee's objection and included an exhibit detailing the Fannie Mae maximum allowable fee schedule.[30] The court stated that the "no-look" threshold does not prejudice the creditor from seeking an amount greater than $700.00 by application or motion.[31] The Court held that the servicer satisfactorily explained the basis for the fees and expenses[32] and approved the requested fees and expenses. However, the court noted that this should not be construed as an endorsement of secured creditors seeking fees in excess of the "no-look" fee without filing a proper application or motion as required by the General Order. [33]

As a result of these objections and differing treatment throughout the country, creditors are faced with the dilemma of whether to file a notice that includes the actual fees incurred and risk incurring additional fees defending their notice or file a notice with a significantly decreased amount to avoid objections. Creditors will continue to face this dilemma until such a time as there is uniformity or all districts publish guidelines related to standard allowable fees. ■

22 *Id.*

23 11 U.S.C. 1327.

24 *See Mandeville*, 596 B.R. 750.

25 See *General Order* 2017-01.

26 See *Guidelines For Chapter 13 Attorney Fees For Secured Creditors.*

27 *In re Garcia*, 17-60124-RLJ-13, 2018 WL 3203385 (Bankr. N.D. Tex. June 28, 2018)

28 *Id.*

29 *Id.*

30 *Id.*

31 *Id.*

32 *Id.*

33 *Id.*

CALL FOR WRITERS

The Commercial Law League of America and CLW magazine are looking for articles from our membership. We know many of you are subject matter experts in one field or another and we are hoping you will be willing to share your knowledge with your fellow members. ***Our next issue, October/November/December, is focused on the Creditors' Rights. Submission deadline: October 15.*** *If you are interested in being a contributing author for CLW, please contact Beau Hays at* ***beau@hayspotter.com****.*

Wanda Borges, Esq.
Principal Member
Borges and Associates, LLC

A SUCCESS STORY WITHOUT BORDERS

The bankruptcy Abuse Prevention and Consumer Protection Act of 2005 "created an entirely new chapter 15 to the Bankruptcy Code. Chapter 15 is designed to specifically address the unique jurisdictional and process issues raised by ancillary and cross-border proceedings involving multinational debtors. Chapter 15 was largely derived from the model law on cross-border insolvency which was promulgated by the United Nations Commission on International Trade Law."[1] Nevertheless, what was shown by one recent Chapter 11 proceeding is that a successful multinational bankruptcy proceeding can be had without resort to chapter 15.

MULTINATIONAL PARTIES INVOLVED

The *Kumtor* case was a Chapter 11 proceeding used by multinational debtors in order to resolve their fight with a foreign government. On May 31, 2021, Kumtor Gold Company CJSC ("KGC") and Kumtor Operating Company CJSC ("KOC") each filed a voluntary Chapter 11 petition for relief under the Bankruptcy Code.[2] On June 4, 2021, each Debtor filed an amended voluntary petition. What made this a most unique Chapter 11 proceeding was 1) each of the Debtors is a Kyrgyz Closed Joint Stock Company, with their headquarters located in Bishkek, Kyrgyz Republic. The principal business of the Debtors is to operate and develop the Kumtor gold mine located in the Tian Shen mountains of Central Asia (the "Kumtor Mine"); 2) each of the Debtors is 100% owned by Centerra Gold Inc. ("Centerra"), a mining company incorporated pursuant to the Canada Business Corporations Act. Centerra's common shares are publicly listed on the Toronto Stock Exchange and the New York Stock Exchange. Kyrgyzaltyn JSC ("Kyrgyzaltyn"), a corporation incorporated under the laws of the Kyrgyz Republic and wholly-owned by the government of the Kyrgyz Republic, owns approximately 26% of Centerra's issued and outstanding common shares ("KZN Centerra Shares") and is Centerra's largest shareholder; and 3) the Chapter 11 proceedings were filed in the Southern District of New York. The sole commercial output of the Kumtor Mine is gold doré. Traditionally, all gold doré produced by the Debtors at the Kumtor Mine has been purchased by Kyrgyzaltyn JSC ("Kyrgyzaltyn"), a state-owned corporation incorporated under the laws of, and wholly owned and controlled by, the government of the Kyrgyz Republic.[3] Proceeds from gold sales payable to KGC have been deposited in US Dollars in KGC's New York bank account (the "New York Account") since 2008. Creditors of the Kumtor Mine were global. The creditor which our firm represented was headquartered in Germany with its manufacturing plant located in Australia.

HISTORY OF THE RELATIONSHIP BETWEEN THE DEBTORS AND THE KYRGYZ REPUBLIC

The gold deposits in the area that would become the Kumtor Mine were first discovered by authorities of the Union of Soviet Socialist Republics (the "USSR") during explorations that took place during the period from 1979 to 1989. This exercise culminated in an initial reserve statement issued by the USSR State Committee on Reserves in 1990. During this period, the Republic was part of the USSR and was known as the Kirghiz Soviet Socialist Republic. Following the democratic reforms in the USSR during the leadership of Mikhail Gorbachev, the Republic declared independence from the USSR on August 31, 1991. Thereafter, the Kyrgyz Republic entered into negotiations with a number of non-Kyrgyz developers with respect to what eventually became the Kumtor Mine.[4]

The first agreement between the Debtors and the Government took place in 1992. That "Original Project Agreement" provided the exclusive rights to evaluate and develop the Kumtor Mine to an entity that ultimately became Kumtor Gold Company. Between 1992 and 2012, there were several restructuring agreements resulting in ownership interests as they existed on the Petition Date. in June 2012, the new Parliament of the Kyrgyz Government (the "Government") issued a resolution requiring a review of the operations at the Kumtor Mine with a purported focus on its compliance with operational, environmental, health and safety, and community standards.

THEN THE BATTLE BEGAN

In the years that followed, the Government took a number of steps that Centerra viewed as further attempts to pressure Centerra into making concessions to the Government. These included:

a. In 2014, the Government had an INTERPOL Red Notice (an international arrest warrant) issued for the arrest of Leonard Homeniuk, Centerra's former Chief Executive Officer, for alleged 'involvement in corruption' as a result of his involvement in the process of entering into the 2009 Agreements. No evidence was ever put forward to substantiate that allegation, and Centerra publicly denied any wrongdoing by Mr.

1 *Bankruptcy Abuse Prevention & Consumer Protection Act of 2005: An Overhaul of U.S. Bankruptcy Law*, by Wanda Borges, Bruce S. Nathan, Catherine Bump and Scott Cargill, published by National Association of Credit Management (2005)

2 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman

3 *See* Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Declaration of Daniel Desjardins in Support of the Debtors' Chapter 11 Petitions and First Day Pleadings [Dkt 9]

4 Ibid

Homeniuk. Mr. Homeniuk described the charges as an attempt to pressure Centerra into signing a new revenue-sharing deal with the Government in respect of the Kumtor Mine. Due to the Red Notice, Mr. Homeniuk was arrested in Bulgaria on July 27, 2015 and detained for several months, until a Bulgarian court determined that the Government did not produce adequate evidence to justify Mr. Homeniuk's extradition to the Republic.

b. In 2014, the Government also commenced criminal cases against certain of KGC's managers, alleging that the managers had somehow deprived the Kumtor Mine of assets or had caused unspecified damage to the Republic. The Government additionally restrained certain KGC managers from leaving the Republic, and from conducting certain financial transactions.

c. In 2016, the Kyrgyz regulatory authorities commenced claims in Kyrgyz domestic courts against KGC and KOC, alleging environmental damages in breach of Republic laws, particularly in connection with the Kumtor Mine's historical practice of storing production tails on glaciers located at the Kumtor Mine – a practice which had been repeatedly approved by Kyrgyz regulators. In May 2016, a Kyrgyz court issued multiple orders against KGC and KOC, including final orders purporting to award $102 million to the Government, as well as an interim order requiring KGC to pay approximately $217 million to the Government and prohibiting KGC from transferring property or assets, declaring or paying dividends, pledging assets, or making loans.[5]

Naturally, the Debtors asserted that there was no justification for any of the Government allegations, insisting that the mine was maintained and operated in material compliance with all the regulations "under the Republic and in accordance with the 2009 Agreements."[6]

THE DISPUTES IMMEDIATELY LEADING TO THE BANKRUPTCY FILING

On May 6, 2021, the Kyrgyz Parliament passed legislation (the "Temporary Management Law") that purported to empower the Cabinet of Ministers of the Kyrgyz Republic to install temporary external management of a company in the event that such company's right to use subsoil resources was suspended for certain unremedied violations of Kyrgyz law that posed an immediate threat to the life and health of persons working or living in the zone of influence of the company's operation.[7]

On May 14, 2021, the Debtors and Centerra initiated arbitration proceedings seeking injunctive relief against the Kyrgyz Republic for violations of agreements between it, the Debtors and Centerra.

On May 17, 2021, a temporary external manager was appointed to oversee the operations of the Kumtor Mine.

Having lost control of the mining operations, on May 31, 2021, the Debtors filed the Chapter 11 proceedings. Among other things, the Debtors claimed the appointment of the temporary external manager was illegal and cited to the corruption in the Kyrgyz Republic quoting "Corruption continues to be a major constraint to business development, particularly in the state customs and border agencies ... [t]he country's judicial system is not fully independent and susceptible to external political influence. While the legal and regulatory framework is set up to be in accordance with international norms, poor implementation, and weak enforcement ... is an endemic problem."[8]

THE CATCH 22 DURING THE CHAPTER 11 PROCEEDING WHICH HINDERED CREDITORS FROM FULFILLING CONTRACTS OR GETTING PAID

The Debtors and the Kyrgyz Republic were embroiled in litigation in the U.S. Bankruptcy Court with KGC asserting that the actions of the Kyrgyz Government were illegal and the Kyrgyz asserting that KGC does not belong in a chapter 11 proceeding in the United States.

Our client was a party to a certain contract with KGC by which it was committed to sell to KGC two IBIS-ArcSAR radar units. The total purchase price was (EUR) 905,715.00. The IBIS-ArcSAR radar unit is a slope monitoring radar that is now the standard practice for the active monitoring of slope in open pit mines and for safety critical landslide monitoring with the aim of providing alerts in the event of progressive movements which could potentially lead to slope failure and assessing worker safety. With the safety of workers at risk and equipment threatened, safely monitoring slope around-the-clock is a necessity. With early detection, accidents can be prevented. With long-term analysis, mine and civil engineering design can be optimized. The IBIS-ArcSAR unit provides reliable early-detection alerts on impending failures in near real time, as well

5 Ibid

6 Ibid

7 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Debtors' Motion to Dismiss Chapter 11 Case [Dkt 383]

8 U.S. Department of State. (2020). 2020 Investment Climate Statements: Kyrgyz Republic. https://www.state.gov/reports/2020-investment-climate-statements/kyrgyz-republic

as, accurate geo-referenced outputs over long periods of time allowing users to integrate radar data into geotechnical analysis of slope failure mechanisms.

The delivery date for those units was scheduled for mid-July, 2021 which meant that the contract was a pre-petition executory contract requiring the creditor to fulfill its contract post-petition. The Debtors had obtained an Order Enforcing Sections 362, 365(e)(1) and 525 of the Bankruptcy Code from Judge Beckerman. The Order provided, *inter alia*:

Pursuant to section 362 of the Bankruptcy Code, all persons (including individuals, partnerships, corporations, and all those acting for or on their behalf) and all foreign or domestic governmental units (and all those acting for or on their behalf) are stayed, restrained, and enjoined from

c. collecting, assessing, or recovering a claim against the Debtors that arose before the commencement of these Chapter 11 Cases;

3. All persons and all foreign and domestic governmental units, and all those acting on their behalf, including sheriffs, marshals, constables, and other or similar law enforcement officers and officials are stayed, restrained, and enjoined from in any way seizing, attaching, foreclosing upon, levying against, or in any other way interfering with any and all property of the Debtors and the Debtors' estates, wherever located.[9]

The creditor could not merely cancel the order and issue a new order to the Kyrgyz Government. The equipment was manufactured and ready to be delivered. The question was to whom would it deliver the equipment? The Debtors who were not operating the Kumtor Mine? Or the temporary manager who was operating the Kumtor Mine but whom the Debtors refused to recognize? The contract was with KGC and delivery was to be made to the mine site.

Complicating these facts even more, the creditor was contacted directly by the Kyrgyz Government. Its position was that the takeover by it of the Kumtor operations was in accord with Kyrgyz laws and completely legal. The Kyrgyz Government wanted the creditor to fulfill the terms of the contract and promised to pay for the two units. The Kyrgyz Government had objected to the Stay Order refusing to acknowledge that it was subject to the jurisdiction of the U.S. Bankruptcy Court.

This placed the creditor in an untenable position. If it proceeded to deliver the units to the Kyrgyz Government without Kumtor consent and approval of the U.S. Bankruptcy Court, it was at risk of violating the Automatic Stay and might have been subject to a Contempt Order by the U.S. Bankruptcy Court. If it refused to deliver to the Kyrgyz Government, it was at risk of being in breach of contract since the Kyrgyz Government was positing that it was rightly in control of all Kumtor assets and operations and had complete authority to demand the fulfillment of the contract by the creditor. Further, if the creditor refused to deliver to the Kyrgyz Government, and there was a problem at the mine which could have been prevented with the Radar units, the creditor might be held responsible for actual and punitive damages.

ATTEMPTS TO OBTAIN COOPERATION FROM THE DEBTORS WERE FUTILE

We tried to convince Debtors' counsel that it was in the best interests of Kumtor to consent to the sale by the creditor to the Kyrgyz Government for several reasons: 1. Kumtor was not in a position currently to assume the contract and had no funds with which to pay for those radar units; 2. If the units were delivered to the Kyrgyz Government and paid for by the Kyrgyz Government, that would ultimately be beneficial to Kumtor if it wins its battle with the Kyrgyz Government and gains back possession of its assets because Kumtor will receive the benefit of those Radar units without having paid for them; and 3. The gold mine would continue to operate in a safe manner which will protect the business operations and assets of Kumtor should it succeed.

A proposed stipulation was submitted to Debtors' counsel providing:

1. The creditor may proceed to deliver its two (2) sets of IBIS-ArcSAR equipment and accompanying software to the Kumtor Mine and be paid for same by the External Manager.
2. This delivery will not constitute a violation of any section of the U.S. Bankruptcy Code, including but not limited to 11 U.S.C.§§362 (a)(3), 365E(1) or 525
3. Once the creditor has been paid by the External Manager, it will have no claim in the KGC chapter 11 proceeding for these sums.
4. Delivery by the creditor of this equipment and software will constitute completion of the current executory contract rising from Purchase Order P28085 and creditor will be under no obligation to deliver any further equipment or software to KGC pursuant to this Purchase Order.
5. The creditor may continue to maintain, service and repair equipment that was delivered prior to the chapter 11 filing.

9 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Order Enforcing Sections 362, 365€(1) and 525 of the Bankruptcy Code. 6/8/2021 [Dkt.20}

6. The creditor may enter into new agreements to provide additional equipment and services which are critical to the safety of the Kumtor Mine.

The Debtors refused to sign the proposed stipulation and informed me that anything the creditor did was at its own risk.

THE BATTLE BETWEEN THE KYRGYZ GOVERNMENT AND THE DEBTORS RAGED ON

In June, 2021, the Debtors sought an order modifying the automatic stay to permit the continuation of a pre-petition UNCITRAL arbitration. The Debtors asserted that they were seeking the stay modification "out of an abundance of caution" but that they did not believe the arbitration proceeding was subject to the automatic stay. In addressing the question of "cause", they cited to the twelve factors detailed in the *Sonnax*[10] decision as to the inclusiveness of reasons that might provide "cause" for the stay to be modified. In their motion for a stay modification, the Debtors said:

The automatic stay does not preclude arbitrations, such as the Debtors' Arbitration, from continuing during the pendency of a chapter 11 case. Cases in this Circuit differ as to whether a full or a more modified consideration of the *Sonnax* factors is necessary in connection with a motion to lift the automatic stay to allow arbitration to proceed. Some courts suggest that a modified *Sonnax* test that heavily favors arbitration is appropriate. See, e.g., *Kittay v. Landegger (In re Hagerstown Fiber Ltd. P'ship)*, 277 B.R. 181, 204 (Bankr.S.D.N.Y.2002) (on motion to lift stay to compel arbitration "*Sonnax* balancing does not apply, and the strong federal policy favoring arbitration trumps the usual considerations of judicial economy and efficiency which are important factors under *Sonnax*"); *Kraken Inc. v. Jacobs* (*In re Salander-O'Reilly Galleries LLC*), 475 B.R. 9, 21 (S.D.N.Y. 2012) (laying out four-part test: "(1) whether the parties agreed to arbitrate; (2) whether the dispute falls within the arbitration clause; (3) if federal statutory claims are raised, whether Congress intended those claims to be arbitrable; and (4) [whether certain non-arbitrable claims should be stayed]").[11]

The Kyrgyz Republic filed a Limited Objection to the Debtors' Motion to Modify the Stay but specifically stated that the Objection did **not** "constitute a submission by the Kyrgyz Republic to the jurisdiction or authority of the Bankruptcy Court for the resolution of any matter involving the Kyrgyz Republic and the Debtors."[12] The Kyrgyz Republic did not consent to or recognize KGX or KOC as validly filed chapter 11 debtors. It asserted that "[T]he filing of this Objection shall not constitute a waiver or consent by the Kyrgyz Republic of any rights, claims, actions, defenses setoffs, recoupments, or other matters to which the Kyrgyz Republic is entitled under any agreements or at law or in equity. All of the foregoing rights are expressly reserved and preserved, without exception, and without the intention or purpose of conceding jurisdiction in any way by this filing or by any other participation in these Chapter 11 Cases. The Kyrgyz Republic expressly reserves all rights at law and equity to assert the jurisdiction of the courts of the Kyrgyz Republic, or arbitration in Stockholm, as applicable, with respect to any disputes involving the Kyrgyz Republic and the Debtors. The Kyrgyz Republic expressly reserves all rights at law and equity it may have with respect to sovereign immunity or otherwise under the Foreign Sovereign Immunities Act of 1976."[13]

On July 14, 2021, the Debtors commenced an adversary proceeding against the Kyrgyz Republic seeking a temporary restraining order and a preliminary and permanent injunction against the enforcement of an injunction obtained by the Defendant in the Kyrgyz Republic, the continued prosecution of the action commenced by the Defendant in the Kyrgyz Republic and any other actions by the Defendant in violation of the automatic stay.

The Order Modifying the Stay to permit the continuation of the arbitration proceeding was signed by Judge Beckerman on July 16, 2021. On July 17, 2021, the Kyrgyz Republic filed a Motion to Dismiss the Chapter 11 Bankruptcy Cases. On July 20, 2021, Judge Beckerman signed an Order finding that the Kyrgyz Government was in violation of the automatic stay. However, the Order would not be enforceable until the Kyrgyz Government was served with a copy of same in accordance with 28 U.S.C. §1608.

Although counsel for the Kyrgyz Republic had entered an appearance in the Chapter 11 proceedings, he informed the court that he was not authorized to accept service of the adversary proceeding on behalf of the Kyrgyz Republic and that the Debtors had to proceed to serve the Kyrgyz Republic under 28 U.S.C. §1608.

IT WAS TIME TO CIRCUMVENT THE BANKRUPTCY COURT

10 *Sonnax Indus., Inc. v. Tri Component Prods. Corp. (In re Sonnax Indus., Inc.)*, 907 F.2d 1280, 1286-88 (2d Cir. 1990)).

11 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Motion For Entry Of An Order Modifying The Automatic Stay With Respect To The UNCITRAL Arbitration, [Dkt 34]

12 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Limited Objection Of The Kyrgyz Republic To Debtors' Motion For Entry Of An Order Modifying The Automatic Stay With Respect To The UNCITRAL Arbitration [Dkt 52]

13 Ibid

Not only had the Kyrgyz Government not yet been served with the Order holding it in contempt, but it had also not been served with the adversary proceeding. It seemed as though the Debtors and the Kyrgyz Republic would battle forever. Neither side was budging. The creditor was being pressured by the Kyrgyz Government to deliver the equipment and be paid for it. The Debtors and the Kyrgyz Government were continuing their battles in the bankruptcy court and our client was anxious to deliver its equipment and get paid.

The Motion to Dismiss was pending but the creditor decided that such motion was not its battle and did not want to expend legal fees by joining that motion. Accordingly, in August, 2021, we reached out to bankruptcy counsel for the Kyrgyz Government to open discussions as to how best the creditor could work with the Kyrgyz Government to deliver its equipment to the Kumtor mine and get paid. Discussions resumed with Counsel for the Debtors who agreed that a re-directed sale to a third party that would result in the equipment being delivered to the Kumtor mine would be both beneficial to the Debtors and not violative of the automatic stay. Although counsel was amenable in discussion, the Debtors would not commit that agreement to a writing.

Nevertheless, discussions continued about re-directing the sale of the equipment through a third party. During the month of September, pressure was mounting on the creditor to get this sale done. Through a series of purchase orders and letters of credit, the sale was finally accomplished. By October, 2021, the sale transaction was completed. The equipment was delivered to the Kumtor mine. The client was paid.

ALL'S WELL THAT ENDS WELL!

Although the client was paid and had no further interaction with the Bankruptcy Court, it was most interesting to watch the ongoing proceedings. The initial Scheduling Order on the Adversary Proceeding made it clear that with discovery and motions, there would be no trial in that case before March of 2022. No trial ever took place. After hundreds of hours of arguments, discussions and arms-length negotiations, a Global Arrangement Agreement was entered into on April 4, 2022. Some of the pertinent terms of that Global Arrangement Agreement included:

Parties. The parties to the Global Arrangement Agreement are the government of the Kyrgyz Republic, Kyrgyzaltyn, Centerra, KGC and KOC. Due to these Chapter 11 Cases and the disputes over who controls the Debtors, KGC and KOC will be deemed to join the agreement as of the Closing Date (as defined in the Global Arrangement Agreement) when Kyrgyzaltyn will receive Centerra's 100% equity interest in KGC and KOC and these Chapter 11 Cases are dismissed.

Share Exchange. On the Closing Date, Centerra will purchase, and subsequently cancel, all of the KZN Centerra Shares for an aggregate purchase price of approximately C$972 million. In satisfaction of the purchase price for the KZN Centerra Shares, Centerra will deliver the KGC Shares and the KOC Shares and pay approximately $11 million to Kyrgyzaltyn and, on behalf of Kyrgyzaltyn, Centerra will pay approximately $25 million to the Canada Revenue Agency on account of Canadian withholding taxes. (Global Arrangement Agreement, §§ 2.1–2.5; 5.)

Certain Payments. On the Closing Date, Centerra will make a cash payment of $50 million to KGC, as partial repayment of principal amounts owing under the intercompany claim balance between Centerra and KGC, with the remaining balance being repaid by way of an offsetting dividend declared by KGC immediately before, and subject to the occurrence of, the Closing Date. (Global Arrangement Agreement, §§ 5.1–5.3.)

KGC/KOC Cooperation. On and after the Closing Date, Centerra will cooperate in good faith and use commercially reasonable efforts to transfer to KGC and/or KOC certain data, deliver to certain agreed key suppliers and vendors to KGC a letter informing them of the termination of these Chapter 11 Cases and deliver a letter to the London Bullion Market Association informing them of the arrangement with the Kyrgyz Republic and Kyrgyzaltyn and withdrawing any previous complaints and/or objections regarding Kyrgyzaltyn's status as a Good Delivery Refiner. Centerra will not assert any claims against vendors and suppliers to the Kumtor Mine or other contract parties with KGC and KOC, in respect of their dealings with KGC, KOC and the Kumtor Mine, and shall inform the certain agreed key suppliers and vendors of such. (Global Arrangement Agreement, § 6.)[14]

On July 28, 2022, the "Order Dismissing Chapter 11 Cases Subject to, and Effective as of the Closing Date of The Global Arrangement Agreement" was signed. [Dkt 402]

Would everyone agree that a dismissal is a success story? In this case it was! Creditors were happy. The Debtors were happy. The parent company was happy. The Kyrgyz Government was happy. ■

14 Kumtor Gold Company CJSC and Kumtor Operating Company CJSC, Case No. 21-11051, U.S. Bankruptcy Court, Southern District of New York, Judge Lisa G. Beckerman, Motion To Dismiss Chapter 11 Cases Subject To, And Effective As Of, The Closing Date Of The Global Arrangement Agreement [Dkt383]


WE
WANT
YOU
JOIN

MUCH ADO ABOUT NOTHING

DIARY OF A MADMAN OR BLIZZARD OF ODD

Some columns are hard to write. Others just plain write themselves. This is the latter.

I was referred a client by a CLLA comrade (yes, that's why we come to meetings) to defend a federal case. My client, Dormouse Enterprises, was a low voltage electrical company that had done a job for the Plaintiff, Teapot Electrical. Teapot had hired an attorney named Madison Hatter. The Complaint was very long and claimed all sorts of nefarious intention on my client to breach an NDA and steal their business. I answered and counterclaimed for the fees owed on the projects.

First, I served discovery on the Plaintiff. I awaited responses, and none were forthcoming. I reviewed the documents and noticed some problems, such as Exhibits to the Complaint missing. Oh yes, and the complete lack of an Answer to my counterclaim.

You see, in Georgia state court practice, there is no requirement to Answer a Counterclaim. And, since less is more, unless the goal is to overcharge your client, they are generally not filed. I filed a Motion for Default. Mr. Hatter filed a Motion to Open Default. Here is an excerpt from his affidavit in support:

> I have practiced law in Georgia for 33 years. My practice is about 80% in Georgia state courts, 15% in arbitrations and around five percent in federal court. Of those cases that go to federal court, most are in bankruptcy court where there is no counterclaim practice. Accordingly, 80% of my cases, being in state court, are such that if a counterclaim is stated an Answer or Reply to the Counterclaim is not required. Similarly, no reply or answer to an arbitral counterclaim is needed.

The Court, in denying the Motion to Open Default, gently reminded Mr. Hatter that he chose the forum and, if he was not familiar with the rules, perhaps he should have chosen another venue.

I eventually was forced to write a letter, as the discovery period was expiring, in my good faith effort to secure discovery without involving the Court. I requested the discovery documents along with the Certificate of Interested Persons, Corporate Disclosure, and more documents required by the District Court Local Rules.

The response, excerpted:

So, as I sit here on the night before my fiancée's birthday, at almost 9:00 pm., when I'm supposed to be on a badly needed vacation and when I'm supposed to be making a pizza, instead I'm addressing your email which is written in such a way as to imply that I am due for detention as soon as you report me to the teacher. I started practicing law 33 years ago and, while opposing attorneys were always adversaries, it wasn't like this back then. The art form of emphasizing the non-issue has been elevated over the last two years to the point where some lawyers, it seems, have no talent or skill whatsoever EXCEPT in the practice of emphasizing the side show and avoiding the real issues.

Attempts to comply with the requirement of telephone contact before filing any discovery motion were fruitless. When I tried to address the issues, he would lapse into a monologue that sounded a great deal like these emails and explaining my client just needed to pay up and end this. After endlessly having to interrupt and try to steer the conversation back to the task at hand, I would inform him this was useless and I was hanging up.

He responded as follows, about a 40 minute call where I eventually gave up:

If I had to guess, your demeanor on the phone suggests some recent personal or family tragedy that is making you behave this way. It's sad to see in an otherwise good attorney, but I want to offer you hope, based on experience, that whatever it is I'm sure you will overcome it with time. If I can help in any way, such as consenting to the discovery extension you need to relieve some of the stress you are feeling, you only need to say the word. I'm one attorney who tries to never forget the duty to treat my colleagues with respect and professionalism no matter what other things are impacting my own well-being.

After he did send some pitifully inadequate responses to the discovery, I was forced to file a Motion to Compel. His response to me via email:

Rome, they say, wasn't built in a day. The cathedral of Sagrada Familia in Barcelona has been under construction for over a century and is still far from done. The earth is billions of years old. In context, the fact that Dormouse may get discovery responses perhaps 21 to 25 days after the last formal extension Dormouse granted does not strike me as anything of historic significance. Or, if I can add one more point to put this in context, ten years from now the additional time I needed to get you Teapot's responses will most likely not have resulted in your life experience, or your client's, having been any worse. Perhaps this is a good time for you and your client to consider the virtues of patience, an attribute that is much more beneficial than stressing over a minute lapse of time from when discovery responses were expected but, for very good and understandable reasons, have been deferred.

There's much more, but we only have so much space. The court held a discovery conference to address my Motion to Compel. During that conference with the judge, Mr. Hatter requested the Court enter an order that I could no longer hang up on him when he would call. I pointed out that he would harangue me forever, if forced not to stop. The Court gently explained that it would not be entering such an Order and granted my sanctions motion.

So, what happened? Mr. Hatter paid his sanctions, Teapot got a new attorney, and the case was settled amicably. ■

Emory Potter, Esq.
Hays & Potter, LLP

2023

EASTERN REGION CONFERENCE

NOVEMBER 8-9, 2023

Manhattan Penthouse • New York, NY

ATTEND IN-PERSON OR VIRTUALLY

Early Registration Deadline is October 6 2023.