2014 – A Year in Review from the Perspectives of Judges and Attorneys"

Recent Decisions Impacting the Second and Third Circuits
(2013-present)

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"2014 – A Year in Review from the Perspective of Judges and Attorneys"
Recent Decisions in the Second and Third Circuits
(2013 – present)[1]

I. Supreme Court Decisions

A. *Exec. Bens. Ins. Agency v. Arkison*, 134 S. Ct. 2165 (2014) (bankruptcy court jurisdiction)

Facts: Arkison, the bankruptcy trustee in a chapter 7 proceeding, filed a complaint in the bankruptcy court against petitioner Executive Benefits Insurance Agency (EBIA) and others alleging the fraudulent conveyance of assets from the debtor to EBIA. The bankruptcy court granted summary judgment for Arkison and the district court affirmed the decision after *de novo* review. While EBIA's appeal to the Ninth Circuit was pending, the Court entered its decision in *Stern v. Marshall*, and EBIA accordingly moved to dismiss its appeal for lack of jurisdiction. The Ninth Circuit rejected the motion and affirmed the decisions of the lower courts. While the Ninth Circuit considered Arkison's claims to be "*Stern* claims," i.e., claims designated for final adjudication in the bankruptcy court as a statutory matter ("core" claims) but prohibited from proceeding in that way as a constitutional matter, it held that EBIA impliedly consented to jurisdiction and that the bankruptcy court's judgment could be considered proposed findings of fact and conclusions of law that were reviewed *de novo* by the district court.

Issue: How should a bankruptcy or district court proceed when a "*Stern* claim" is identified?

Holding: Claims identified as "*Stern* claims" that fit within the category of claims governed by section 157(c)(1) of the Bankruptcy Code should be treated as non-core claims: "the bankruptcy court should hear the proceeding and submit proposed findings of fact and conclusions of law to the district court for *de novo* review and entry of judgment." Accordingly, because the district court conducted a *de novo* review of the bankruptcy court's findings, the Court affirmed the judgment of the Ninth Circuit. However, the Court did not make a decision as to whether parties can consent to having a bankruptcy judge make a final ruling on a "*Stern* claim."

B. *Daimler AG v. Bauman*, 134 S. Ct. 746 (2014) (jurisdiction)

Facts: Twenty-two (22) Argentinian residents filed a complaint in the United States District Court for the Northern District of California asserting claims under the Alien Tort Statute, the Torture Victim Protection Act of 1991, and California and Argentina law against DaimlerChyrsler Aktiengesellschaft (Daimler), a German public stock company that manufactures Mercedes-Benz vehicles in Germany, based on events that

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[1] In addition to recent decisions from the Second and Third Circuits, these materials include certain related decisions from the courts of appeals of other circuits.

occurred in Argentina. Personal jurisdiction over Daimler was predicated on the California contacts of one of its subsidiaries that was incorporated in Delaware with its principal place of business in New Jersey. The subsidiary distributed Daimler-manufactured vehicles throughout the United States, including California, and had several California-based facilities. Pursuant to the General Distributor Agreement between Daimler and the subsidiary, the subsidiary was an independent contractor. The district court granted Daimler's motion to dismiss for lack of personal jurisdiction, but the Ninth Circuit reversed, holding that the subsidiary was Daimler's "agent" for jurisdictional purposes and fell within the California courts' all-purpose or general jurisdiction, thereby making Daimler answerable to suit in California.

Issue: Whether the Due Process Clause of the Fourteenth Amendment precludes the district court from exercising general (all-purpose) personal jurisdiction over a claim brought by foreign plaintiffs against a foreign defendant based on events that occurred entirely outside the United States?

Holding: The district court did not have general jurisdiction over Daimler because Daimler was not "at home" in California and, accordingly, could not be sued there for conduct that occurred in Argentina. The Court held that the proper inquiry for general jurisdiction over a corporation is whether the corporation's "affiliations with the State are so 'continuous and systematic' as to render [it] essentially at home in the forum state."[2] Neither Daimler nor its subsidiary was incorporated in California or had its principal place of business there. While a corporation may be subject to general jurisdiction in a State absent those places, the Court held that "[i]f Daimler's California activities sufficed to allow adjudication of this Argentina-rooted case in California, the same global reach would presumably be available in every other State in which [the subsidiary's] sales are sizable. Such exorbitant exercises of all-purpose jurisdiction would scarcely permit out-of-state defendants 'to structure their primary conduct with some minimum assurance as to where that conduct will and will not render them liable to suit.'" Considerations of international rapport also played into the Court's decision that Daimler should not be subject to the general jurisdiction of the courts of California.

C. *Law v. Siegel*, 134 S. Ct. 1188 (2014) (breadth of 105(a))

Facts: After filing for chapter 7 bankruptcy, Law valued his California home at $363,348 and claimed that $75,000 of that value was covered by California's homestead exemption and was therefore exempt from the bankruptcy estate. He also claimed that two voluntary liens exceeded the home's nonexempt value, leaving no equity recoverable for his other creditors. The bankruptcy estate trustee challenged one of these liens in an adversary proceeding and, after five years of litigation, the bankruptcy court ultimately found that the loan was a fiction created by Law to preserve his equity in the house.

[2] In contrast, the proper inquiry for specific jurisdiction is whether the suit arises out of or relates to the defendant's contacts with the forum, as set forth in *International Shoe* and its progeny. Because the suit was based on events that occurred in Argentina, and not in California, and the plaintiffs never argued that the suit fit into the specific jurisdiction category, the Court only considered whether the suit fit into the general jurisdiction category.

Accordingly, the court granted the trustee's motion to surcharge Law's entire $75,000 homestead exemption to defray the trustee's attorneys' fees, which amounted to over $500,000 in fees and costs from litigating the dispute and overcoming Law's fraudulent misrepresentations. The Ninth Circuit Bankruptcy Appellate Panel and the Ninth Circuit Court of Appeals affirmed the bankruptcy court's decision.

Issue: Whether a bankruptcy court may order that a debtor's exempt assets be used to pay administrative expenses incurred as a result of the debtor's misconduct?

Holding: No, in exercising its statutory and inherent powers, a bankruptcy court may not contravene specific provisions of the Bankruptcy Code. Section 522 of the Bankruptcy Code (by reference to California law) entitled Law to exempt $75,000 of equity in his home from the bankruptcy estate, thereby making that $75,000 "not liable for payment of any administrative expense." Accordingly, by surcharging that amount, the bankruptcy court exceeded the limits of its authority under section 105(a) of the Bankruptcy Code and its inherent powers.

D. *Asarco, LLC v. Baker Botts, LLP (In re Asarco, LLC)*, 751 F.3d 291 (5th Cir. Apr. 30, 2014), *cert. granted* 83 U.S.L.W. 3094 (U.S. Oct. 2, 2014) (No. 14-103) (professional fees)

Facts: Baker Botts LLP and Jordan, Hyden, Womble, Culbreth & Holzer, P.C. represented Asarco LLC during its chapter 11 bankruptcy. During the course of their representation, Baker Botts and Jordan Hyden successfully prosecuted complex fraudulent transfer claims against Asarco's parent company, thereby recovering Asarco's controlling interest in its former subsidiary, valued at between $7 and $10 billion, the largest fraudulent transfer judgment in chapter 11 history. Asarco emerged from bankruptcy with little debt, $1.4 billion in cash, and the successful resolution of its environmental, asbestos, and toxic tort claims. In their final fee applications, Baker Botts and Jorden Hyden sought lodestar fees, expenses, a 20% fee enhancement for the entire case, and fees and expenses for preparing and litigating their final fee applications. Asarco, once again controlled by the parent company, objected to the fees. The bankruptcy court approved percentage fee enhancements pursuant to section 330(a) of the Bankruptcy Code only for the work performed on the fraudulent transfer litigation, not on the entire case and, accordingly, awarded $4.1 million to Baker Botts and over $125,000 to Jordan Hyden based on their "rare and exceptional" performance and results. The bankruptcy court also authorized fees and expenses for the firms' litigation in defense of their attorneys' fee claims, resulting in an award of $5 million to Baker Botts and $15,000 to Jordan Hyden. The district court affirmed the fee enhancement and, after confirming that the defense-fee award did not include any fees incurred in pursuit of the enhancement, affirmed the defense-fee award.

Issues:

- Whether the bankruptcy court abused its discretion in authorizing fee enhancements to Baker Botts and Jordan Hyden for their unusually successful fraudulent transfer litigation?

- Whether the bankruptcy court was authorized, consistent with section 330 of the Bankruptcy Code, to award attorneys' fees to the firms for defending their fee applications in court?

Holding: The Fifth Circuit affirmed the fee enhancements but reversed the defense-fee awards. The Fifth Circuit found that the fee enhancements were warranted under section 330(a)(3) of the Bankruptcy Code and the *Johnson* factors[3] due to the "rare and exceptional" results achieved by the attorneys and clarified that the Supreme Court's decision in *Perdue* did not remove the discretion of bankruptcy courts to award a fee enhancement in rare and exceptional circumstances. Turning to the defense-fee award issue, the Fifth Circuit, noting that "[c]ase law addressing this issue is divided," held that section 330(a) of the Bankruptcy Code does not authorize compensation for the costs counsel or professionals bear to defend their fee applications. In reaching its holding, the Fifth Circuit reasoned that section 330 only permits payment for professional services that are likely to benefit a debtor's estate or are necessary to case administration. Thus, because the "primary beneficiary of a professional fee application, of course, is the professional," such fees should not be awarded pursuant to section 330(a).

II. Equitable Mootness

A. *Czyzewski v. Jevic Holding Corp. (In re Jevic Holding Corp.)*, Civ. Nos. 13-104-SLR, 13-105-SLR, 2014 U.S. Dist. LEXIS 8813 (D. Del. Jan. 24, 2014) (equitable mootness)

Facts: The debtors entered into a settlement involving a structured dismissal[4] with (i) Sun Capital Partners IV, LP, Sun Partners Management IV, LLC and Sun Capital

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3 After calculating a lodestar amount pursuant to section 330(a)(3) of the Code, bankruptcy courts retain the discretion to adjust the lodestar upwards or downwards following consideration of the facts outlined in *Johnson v. Ga. Highway Express, Inc.*, 488 F.2d 714, 717-19 (5th Cir. 1974). These factors include: (1) the time and labor required; (2) the novelty and difficulty of the questions; (3) the skill requisite to perform the legal service properly; (4) the preclusion of other employment by the attorney due to acceptance of the case; (5) the customary fee; (6) whether the fee is fixed or contingent; (7) time limitations imposed by the client or other circumstances; (8) the amount involved and the results obtained; (9) the experience, reputation, and ability of the attorneys; (10) the "understandability" of the case; (11) the nature and length of the professional relationship with the client; and (12) awards in similar cases.

4 The settlement provided for "'a) the exchange of releases, (b) the payment of $2 million by CIT to the [d]ebtors, to be used to satisfy unpaid chapter 11 administrative claims, (c) the

Partners, Inc. (collectively, "Sun"), who bought the debtors prior to their bankruptcy, (ii) The CIT Group/Business Credit, Inc. ("CIT"), who provided the loan Sun used to refinance the acquisition, and (iii) the committee. Before the settlement was reached, certain employees whose employment was terminated by the debtors filed a complaint asserting claims under the WARN Act and the New Jersey Millville Dallas Airmotive Notification Act. After the settlement was proposed, these employees objected to the settlement, but the bankruptcy court overruled their objections and approved the settlement because it was unlikely the employees would recover anything on their claims, even if they did recover something, it would take years, and the debtors did not possess any funds that were not subject to the liens of CIT and Sun to continue with the litigation. A few months later, the employees sought clarification from the bankruptcy court as to whether the settlement could be implemented. The bankruptcy court confirmed the lack of a stay, the settlement was implemented, and the bankruptcy court dismissed the debtors' chapter 11 cases. The employees appealed the bankruptcy court's approval of the settlement.

Issues:

- Whether the bankruptcy court properly evaluated the proposed settlement?
- Whether the appeal is equitably moot?

Holding: The bankruptcy court properly evaluated the proposed settlement by considering the *Martin*[5] test's four criteria and determining that the settlement was "fair and equitable." Even though the settlement did not follow the absolute priority rule, the court held that "this is not a bar to the approval of the settlement as it is not a reorganization plan." The court agreed with the appellees that the appeal was equitably moot because the settlement had been substantially consummated as all the funds had been distributed and an appeal could seriously affect the settlement because it did not provide for funds for appellant's "speculative recovery."

B. *Samson Energy Res. Co. v. SemCrude, L.P. (In re Semcrude, L.P.),* 728 F.3d 314 (3d Cir. 2013) (equitable mootness)

Facts: The debtors, a midstream oil and gas business involved in the gathering, transportation, storage, and marketing of crude oil and other petroleum products, filed for

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dismissal with prejudice of [an adversary proceeding brought by the committee against CIT and Sun], (d) the assignment by Sun of its lien on the estates' remaining assets to the Jevic Holding Corp. Liquidating Trust for the benefit of the [d]ebtors' unsecured creditors and certain priority tax claimants, (e) the reconciliation of administrative and unsecured claims, and (f) the dismissal of the chapter 11 cases.'"

5 *See Myers v. Martin (In re Martin),* 91 F.3d 389, 393 (3d Cir. 1996) (listing the relevant criteria as including "(1) the probability of success in litigation; (2) the likely difficulties in collection; (3) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it; and (4) the paramount interest of the creditors").

bankruptcy in July 2008. Many of their creditors were producers who supplied oil and gas to the debtors on credit prior to their bankruptcy filing, including four Oklahoma producers (the "Appellants"). The producers asserted claims against the debtors for the distribution from the proceeds of the oil and gas ahead of other creditors and the debtors filed a motion to establish global procedures to administer the producers' claims. The Appellants objected to the use of these procedures, argued that they were entitled to prosecute an adversary proceeding on their claims, and filed suit. The bankruptcy court approved the debtors' use of the global procedures and stayed the adversary proceeding but noted that the question of whether the Appellants would be bound by the resolution procedures could be litigated at a later time. The debtors then reached a settlement resolving the claims of all of the producers and filed a plan of reorganization that incorporated the settlement and required the voluntary dismissal of all adversary proceedings and other litigation related to the producers' claims. While the settlement set the cash distribution the Appellants would receive, they obtained a waiver of the requirement that they dismiss their adversary proceeding.

The bankruptcy court confirmed the plan and Appellants appealed to the district court, arguing that the plan could not validly discharge their claims without affording them the procedural protections of an adversary proceeding. Because the Appellants did not request a stay pending appeal, the plan went into effect shortly after confirmation. Accordingly, the district court dismissed the appeal as equitably moot because it found that the plan had been substantially consummated and that granting Appellants' requested relief would undermine the reorganization plan and harm third parties.

<u>Issue</u>: Whether the appeal should be dismissed as equitably moot?

<u>Holding</u>: The Third Circuit held that the appeal should not be dismissed as equitably moot and reversed the district court's decision because the record did not support the district court's findings that granting Appellants' relief would undermine the reorganization plan and harm third parties. The Third Circuit noted that the dismissal of an appeal under the equitable mootness doctrine should be "the rare exception" and placed the burden of proof on the party seeking dismissal. The Third Circuit found that the reorganization plan would not be undermined because, even if the Appellants were successful in their adversary proceeding, the amounts involved only amounted to roughly one-hundredth of one percent of the total amount involved in the plan. Moreover, allowing the Appellants to bring their adversary proceeding would not result in adversary proceedings by other producers, who were all required to dismiss with prejudice any adversary proceedings they had filed as part of the settlement. Similarly, a successful appeal would not harm third parties due to the relatively insignificant amount of the Appellants' claims. Finally, considering public policy, the Third Circuit noted the Appellants' repeated contention that they were entitled to an adversary proceeding from the inception of the debtors' chapter 11 cases and held that the "presumptive position remains that federal courts should hear and decide on the merits cases properly before them."

III. Plan Confirmation/Structured Dismissals

A. *In re MPM Silicones, LLC*, Case No. 14-22503-rdd, 2014 Bankr. LEXIS 3926 (Bankr. S.D.N.Y. Sept. 9, 2014) (cramdown)

Facts: In 2012, the debtors issued $1.1 billion of first-lien notes and $250 million of 1.5-lien notes due in 2020 under indentures that included an optional redemption provision which contained introductory language providing that, except for in circumstances triggering payment of the make-whole, the Noteholders could not voluntarily redeem the Notes before October 15, 2015. Shortly after the debtors filed voluntary petitions for bankruptcy under chapter 11, the debtors filed declaratory judgment actions challenging the Noteholders' right to more than $200 million in claims for make-whole premiums. The debtors proposed a plan which provided that the Noteholders would receive: (i) payment of their claims in full in cash, without a make-whole premium, if they voted in favor of the plan or (ii) seven-year replacement notes in the face amount of their allowed claims, bearing a below-market interest rate equal to the applicable Treasury rate plus a modest risk premium, and the right to litigate their entitlement to the make-whole premiums, if they rejected the plan. The Noteholders overwhelmingly rejected the plan and filed objections arguing that: (i) they were entitled to the make-whole premiums based on the automatic acceleration of their debt resulting from the bankruptcy filing and the Debtors' early repayment of this debt in the form of the replacement notes issued under the plan and (ii) their treatment under the plan as a result of their rejection was not "fair and equitable" because the plan did not apply the market interest rate to the replacements notes and, therefore, the debtors could not cramdown the plan over their objections. The Noteholders also sought permission to change their votes to accept the plan and concede the make-whole premium argument after the confirmation hearing but before the court issued a ruling.

Issues:

- Whether the Noteholders were entitled to the make-whole premiums?
- Whether the proposed replacement notes satisfied the cramdown requirements of section 1129(b) of the Bankruptcy Code?

Holding: The bankruptcy court held that the Noteholders were not entitled to the make-whole premiums because the plain language of the indentures did not provide for a valid make-whole claim, there was no claim for breach of a purported "no-call" provision under the indentures, and the automatic stay barred deceleration of the debt. The court found that the replacement notes would satisfy the cramdown requirements if the rate was slightly increased. The court agreed with the debtors that the formula approach,[6] and not the market interest rate, is the correct way to calculate cramdown interest for secured creditors in a chapter 11 case. However, because the Treasury rate was used rather than

[6] In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), the Supreme Court applied a "formula" approach under which the proper interest rate is determined by taking a risk-free base rate, such as the prime rate or the Treasury rate, and adding a risk premium to reflect the repayment risks unique to that debtor, which is generally between 1-3%.

the prime rate, the rate had to be slightly increased to make the plan confirmable, although the interest rate was still well below market rates.

B. *In re Genco Shipping & Trading Ltd*, 513 B.R. 233 (Bankr. S.D.N.Y. 2014) (releases)

Facts: The debtors' chapter 11 plan provided for certain standard releases and exculpations, including releases granted by the debtors and exculpation for released parties, which were uncontested. The plan also included non-debtor releases granted by certain non-debtor third parties, including parties holding unimpaired claims and equity interests who were deemed to accept the plan and thus not entitled to vote on the plan. The non-debtor parties to be released under the plan included the prepetition agent and lenders under the debtors' three credit facilities, convertible noteholders and their indenture trustee, and parties agreeing to backstop the debtors' rights offering. The U.S. Trustee and the official committee for equity holders objected to the third-party releases, arguing, respectively, that (i) unimpaired creditors and equity holders did not affirmatively consent to the releases and releases granted solely because a party was deemed unimpaired under a plan violated section 1124 of the Bankruptcy Code because requiring an unimpaired holder of a claim or interest to grant a release effectively required such holders to relinquish certain legal rights, thereby impairing them[7] and that (ii) the equity holders were not given the opportunity to vote, the releases were non-consensual, and the releases otherwise failed to satisfy Second Circuit law to permit approval of the releases. The debtors argued that they had overwhelming creditor support for the plan, no unimpaired creditor stepped forward to object to the releases, despite ample notice, that binding unimpaired creditors to non-consensual third party releases is an "unremarkable feature," and that the releases were qualified by the phrase "to the extent permissible under applicable law," and thus overcame any problem regarding overbreadth.

Issues:

- Whether classifying a party as unimpaired means that the party should be automatically deemed to grant a release where the requirements of *Metromedia*[8] have not been met?
- Whether the releases comply with Second Circuit law?

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7 The U.S. Trustee confirmed that there was no case law addressing this issue.

8 The *Metromedia* requirements consider whether "the provisions are important to a debtor's plan; the claims are 'channeled' to a settlement fund rather than extinguished; the enjoined claims would indirectly impact the debtor's reorganization by way of indemnity or contribution; the released party provides substantial consideration; and where the plan otherwise provides for the full payment of the enjoined claims." *In re DBSD N. Am., Inc.*,419 B.R. 179, 218 (Bankr. S.D.N.Y.2009) (citing *Deutsche Bank AG v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136, 142 (2d Cir. 2005)).

Holding: Even if a party is classified as unimpaired, the requirements of *Metromedia* must be met before that party can be automatically deemed to grant a release. The bankruptcy court explained that the releases, as currently defined, were too broad and did not all comply with *Metromedia*, but approved the releases that did comply with *Metromedia*. This included three groups of releases: (i) "releases with respect to any affected party that consented to grant the releases or may be deemed to have done so through its ability to 'check the box' on the Plan ballots;" (ii) releases "for claims that would trigger indemnification or contribution claims against the Debtors and thus impact the Debtors' reorganization," excluding any indemnification obligations that arose out of the restructuring support agreement or plan negotiations; and (iii) releases "as to those parties who have provided substantial consideration to the reorganization."

C. *In re Lab. Partners, Inc.*, Case No. 13-12769 (PJW), Confirmation Hr'g Tr., at 35-36; *In re Fisker Auto. Holdings, Inc.*, Case No. 13-13087 (KG), Confirmation Hr'g Tr., at 26-28 (exculpation for non-estate professionals)

Facts:

- In *Laboratory Partners*, the debtors' plan provided for the exculpation of non-estate professional Marathon, the senior lender, where Marathon stepped in as part of a joint venture to buy Laboratory Partners' long-term care division, which saved roughly 900 jobs and prevented the liquidation of the asset. The U.S. Trustee objected to the exculpation, arguing that such a provision should only apply to fiduciaries of the debtor and that Marathon was not entitled exculpation under the bankruptcy rules.
- In *Fisker*, the debtors' plan provided for the exculpation of two non-estate fiduciaries based on their substantial contributions to the case: (i) Wanxiang Group Corp., a subsidiary of Fisker and (ii) Hybrid Tech Holdings LLC. A class of former employees and officials at the Internal Revenue Service objected to the exculpations, but these objections were resolved prior to the confirmation hearing. At the confirmation hearing, the U.S. Trustee challenged the releases.

Issue: Whether exculpation of non-estate professionals is appropriate?

Holdings:

- In *Laboratory Partners*, Judge Walsh overruled the U.S. Trustee's objection and approved the exculpation of Marathon based on Marathon's major contribution to the case. He noted that he thought "this was going to be a liquidation case" and that the "exculpation is unusual, but the senior lender's activity in this case was surely unusual."
- In *Fisker*, Judge Gross held that the releases were appropriate and permissible due to the significant contributions by the released parties.[9] However, he noted that "I

[9] The contributions by Wanxiang included claims waivers and an enhanced warranty program that would be directly administered by Wanxiang, something that the Fisker car owners

certainly am not telling people and not ruling that in other cases an exculpation provisions would be applied to a nonfiduciary."

D. *Czyzewski v. Jevic Holding Corp. (In re Jevic Holding Corp.),* Civ. Nos. 13-104-SLR; 13-105-SLR, 2014 U.S. Dist. LEXIS 8813 (D. Del. Jan. 24, 2014) (structured dismissal)

Facts: The debtors entered into a settlement involving a structured dismissal[10] with (i) Sun Capital Partners IV, LP, Sun Partners Management IV, LLC and Sun Capital Partners, Inc. (collectively, "Sun"), who bought the debtors prior to their bankruptcy, (ii) The CIT Group/Business Credit, Inc. ("CIT"), who provided the loan Sun used to refinance the acquisition, and (iii) the committee. Before the settlement was reached, certain employees whose employment was terminated by the debtors filed a complaint asserting claims under the WARN Act and the New Jersey Millville Dallas Airmotive Notification Act. After the settlement was proposed, these employees objected to the settlement, but the bankruptcy court overruled their objections and approved the settlement because it was unlikely the employees would recover anything on their claims, even if they did recover something it would take years, and the debtors did not possess any funds that were not subject to the liens of CIT and Sun to continue with the litigation. A few months later, the employees sought clarification from the bankruptcy court as to whether the settlement could be implemented. The bankruptcy court confirmed the lack of a stay, the settlement was implemented, and the bankruptcy court dismissed the debtors' chapter 11 cases. The employees appealed the bankruptcy court's approval of the settlement.

Issues:

- Whether the bankruptcy court properly evaluated the proposed settlement?
- Whether the appeal is equitably moot?

Holding: The bankruptcy court properly evaluated the proposed settlement by considering the *Martin*[11] test's four criteria and determining that the settlement was "fair

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"have been vocal about from the beginning which is something that they very much wanted into the plan and Wanxiang is committed to do in a materially enhanced way." Hybrid contributed by working with other parties to resolve its issues, rather than fighting which would have driven up expenses and reduced recoveries for creditors.

10 The settlement provided for "'a) the exchange of releases, (b) the payment of $2 million by CIT to the [d]ebtors, to be used to satisfy unpaid chapter 11 administrative claims, (c) the dismissal with prejudice of [an adversary proceeding brought by the committee against CIT and Sun],6 (d) the assignment by Sun of its lien on the estates' remaining assets to the Jevic Holding Corp. Liquidating Trust for the benefit of the [d]ebtors' unsecured creditors and certain priority tax claimants, (e) the reconciliation of administrative and unsecured claims, and (f) the dismissal of the chapter 11 cases.'"

11 *See Myers v. Martin (In re Martin)*, 91 F.3d 389, 393 (3d Cir. 1996) (listing the relevant criteria as including "(1) the probability of success in litigation; (2) the likely difficulties in

and equitable." Even though the settlement did not follow the absolute priority rule, the court held that "this is not a bar to the approval of the settlement as it is not a reorganization plan." The court agreed with the appellees that the appeal was equitably moot because the settlement had been substantially consummated as all the funds had been distributed and an appeal could seriously affect the settlement because it did not provide for funds for appellant's "speculative recovery."

IV. Asset Sales

A. *Dishi & Sons v. Bay Condos LLC*, 510 B.R. 696 (S.D.N.Y. 2014) (363(f) v. 365(h))

Facts: The debtor owned a 97.2% interest in two commercial condominium units, two of which were leased. The debtor owed a creditor (the "Creditor") approximately $13.5 million, which was secured by a mortgage on the condominium units. The chapter 11 plan proposed the sale of the condominiums free and clear of all interests, assumed one of the leases, and rejected the other. Appellant Dishi & Sons was the successful bidder for the condominiums. After the bankruptcy court approved the sale and confirmed the plan, but before an order was entered, the other lessee submitted a letter to the court asserting its rights to retain possession of the unit for the duration of the lease pursuant to section 365(h) of the Bankruptcy Code and, alternatively, as adequate protection under section 363(e) of the Bankruptcy Code. The Creditor then filed a motion seeking a determination of the lessee's rights under the lease. The bankruptcy court held that the lessee had a right to remain in possession pursuant to section 365(h) and as adequate protection.

Issue: Whether section 365(h) of the Bankruptcy Code preserves the lessee's appurtenant rights even if they could otherwise be extinguished in a section 363(f) sale?

Holding: Yes, the lessee's rights will generally be enforceable against the transferee of the property in a section 363 sale. The district court explained that "[a]lthough § 365(h) is applicable to § 363(f) sales, it does not give the lessee absolute rights that take precedence over the trustee's right to sell free and clear of interests. Rather, it clarifies that the lessee may retain its appurtenant rights notwithstanding the trustee's rejection of the lease. Section 363(f), in turn, authorizes the trustee to extinguish the lessee's appurtenant rights—like any other interest in property—but only if one of five conditions is satisfied with respect thereto. The two sections thus work in harmony to establish that the lessee's appurtenant rights may not be terminated by rejection and must be taken into account in any proposed free and clear sale. If § 363(f) authorizes the trustee to sell property free and clear of such rights, nothing in § 365(h) mandates a contrary result. As this case demonstrates, however, § 363(f) will rarely permit such a sale, and consequently, the lessee's rights will generally be enforceable against the transferee of the property." The district court found that none of the five conditions listed in section 363(f) for a sale free and clear of the lessee's rights was satisfied and that, accordingly, the lessee retained its appurtenant rights.

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collection; (3) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it; and (4) the paramount interest of the creditors").

B. *In re Fisker Auto. Holdings, Inc.*, Case No. 13-13087-KG, 2014 Bankr. LEXIS 230 (Bankr. D. Del. Jan. 17, 2014); *In re Free Lance-Star Publ'g Co.*, Case No. 14-30315-KRH, 2014 Bankr. LEXIS 1611 (Bankr. E.D. Va. Apr. 14, 2014) (credit bidding)

Facts:

- *Fisker* – Before filing for bankruptcy, the debtors manufactured plug-in hybrid electric vehicles and were extended a secured loan by the United States Department of Energy, $168 million of which was outstanding when the DOE sold the loan to Hybrid Tech Holdings, LLC for $25 million. Following this sale, the debtors filed for bankruptcy and agreed to sell all of their assets to Hybrid in exchange for a credit bid of $75 million. The debtors filed a sale motion seeking approval of the sale, but the creditors' committee objected and proposed a competitive auction, noting that another party had already expressed genuine interest in purchasing the debtors' assets.
- *Free Lance-State* – Prior to their bankruptcy, when the debtors were expanding their commercial printing business, they borrowed approximately $50.8 million from Branch Banking & Trust ("BB&T"). A few years later, the debtors fell out of compliance with certain loan covenants and BB&T sold the loan to Sandton Capital Partners ("Sandton"), an affiliated entity of DSP Acquisition, LLC ("DSP"). Shortly thereafter, Sandton informed the debtors that it wanted them to file a chapter 11 bankruptcy case and sell substantially all of their assets pursuant to a section 363 sale and that it would keep the debtors' management in place and continue to operate the business. The debtors then began to work on implementing a plan whereby they would file a chapter 11 bankruptcy case and sell all of their assets to DSP. DSP continued to pressure the debtors into filing for bankruptcy, objected to any marketing of the debtors' assets, and insisted that any marketing materials contain on the front page, in bold print, a statement that DSP had a right to a $39 million credit bid. DSP did not have a valid, perfected security interest in all of the debtors' assets. When Protiviti, the debtors' financial consultant developed cash flow projections indicating that the debtors could survive in bankruptcy without a post-petition DIP loan facility, the relationship between the debtors and DSP "turned sour," DSP withdrew its support for a bankruptcy filing, and ceased all work in connection with the filing.

Issue: Whether it is appropriate to limit a credit bid?

Holdings:

- *Fisker* – The bankruptcy court limited Hybrid's credit bid to the $25 million Hybrid paid for the DOE loan and ordered an auction of the debtors' assets because i) by not limiting Hybrid's credit bid, an auction was unlikely to occur at all, which would undermine the importance of a competitive bidding environment, (ii) Hybrid's claim was partially secured, partially unsecured, and part had an uncertain status, so no one knew how much of Hybrid's claim would actually be allowed as a secured claim; and (iii) the proposed timing of the sale, which provided only 24 business days during the holiday season for parties to objection to the sale motion and even less time for the creditors' committee, was troublesome.

- *Free Lance-State* – The bankruptcy court limited DSP's credit bid to $13.9 million, the value of assets for which DSP had a valid, properly perfected lien, and held that the "confluence of (i) DSP's less than fully-secured lien state; (ii) DSP's overly zealous loan-to-own strategy; and (iii) the negative impact DSP's misconduct has had on the auction process has created the perfect storm, requiring the curtailment of DSP's credit bid rights."

C. *Emoral, Inc. v. Diacetyl (In re Emoral Inc.)*, 740 F.3d 875 (3d Cir. 2014) (successor liability)

Facts: Aaroma Holdings LLC ("Aaroma") purchased certain assets and assumed certain liability of Emoral, Inc. ("Emoral"), a manufacturer of diacetyl. At the time of the sale, the parties were aware of potential claims relating to Emoral's production of diacetyl and accordingly provided in the asset purchase agreement that Aaroma was not assuming Emoral's liabilities related to "the Diacetyl Litigation" and that it was not purchasing Emoral's corresponding insurance coverage. At the time of sale, Emoral no longer manufactured diacetyl and Aaroma never manufactured diacetyl. Thus, the only cause of action against Aaroma was based on a mere continuation theory of successor liability, as Aaroma could not be held liable for a direct personal injury claim. When Emoral filed for bankruptcy the following year, disputes arose between the trustee and Aaroma, including the trustee's claim that Emoral's asset sale to Aaroma constituted a fraudulent transfer. These disputes were resolved by a settlement agreement and the trustee agreed to release Aaroma from any "causes of action . . . that are property of the Debtor's Estate." Certain plaintiffs objected to the settlement but ultimately consented based on language in the order indicating that only estate causes of action were being released. Subsequently, these plaintiffs filed individual complaints against Aaroma in New Jersey state court alleging personal injury and product liability claims under the theory that Aaroma was a "mere continuation" of Emoral and thus, liable. Aaroma filed a motion to enforce the settlement in the bankruptcy court, arguing that the plaintiff's claims were barred by the agreement. The bankruptcy court denied Aaroma's motion and held that the plaintiff's personal injury causes of action were not property of the estate because the plaintiffs alleged "a particular injury not generalized injury suffered by all shareholders or creditors of Emoral." The district court reversed and held that the plaintiffs had no cause of action against Aaroma except on a successor liability theory, which was a generalized cause of action because the facts giving rise to the cause of action were common to all creditors and if the plaintiffs succeeded in establishing that Aaroma constituted a mere continuation of Emoral, the creditors of Emoral would benefit generally.

Issue: Whether a mere continuation theory of successor liability is a general cause of action and therefore property of the estate which can be released and discharged by the bankruptcy court?

Holding: Yes. The Third Circuit, affirming the district court's ruling, held that, because the plaintiffs' only theory of liability against Aaroma, a third party not alleged to have caused any direct injury to the plaintiffs, is that Aaroma constitutes a "mere continuation" of Emoral, the plaintiffs failed to demonstrate any factual allegations unique to them as compared to other creditors of Emoral. Accordingly, the Third Circuit held that the plaintiffs' successor liability cause of action was general, rather than individualized and, as such, was property of the estate and was released by the trustee in the settlement agreement.

D. *In re Interstate Bakeries, Corp.*, 751 F.3d 955 (8th Cir. 2014) (intellectual property licenses)

Facts: Prior to the bankruptcy filing of Interstate Bakers Corporation ("Interstate Bakeries") and eight of its subsidiaries and affiliates, including Interstate Brands Corporation ("IBC"), the Justice Department challenged Interstate Bakeries acquisition of Continental Baking Company under antitrust laws, resulting in a judgment that required Interstate Bakeries to divest at least one of its Labels[12] in each of four territories. Accordingly, IBC entered into an asset purchase agreement and a license agreement with Lewis Brothers Bakeries, Inc. ("LBB") selling two of its operations and assets and providing for an exclusive license to thirteen different trademarks. When the debtors filed for bankruptcy in 2004, the license agreement was identified as an executory contract that Interstate Bakeries intended to assume as part of its plan of reorganization. In 2008, LBB filed an adversary complaint seeking a declaratory judgment that the license agreement was not an executory contract under section 365 of the Bankruptcy Code and therefore could not be assumed or rejected by Interstate Bakeries. Relying on *In re Exide Techs.*, 340 B.R. 222 (Bankr. D. Del. 2006), which was later reversed, the bankruptcy court concluded that the license agreement was executory because both IBC and LBB had material, outstanding obligations. The district court affirmed and a divided panel of the Eighth Circuit affirmed. After receiving the views of the Antitrust Division of the Department of Justice and the Federal Trade Commission, the Eighth Circuit granted LBB's petition for a rehearing *en banc*.

Issue: Whether the trademark license agreement between IBC and LBB is an executory contract pursuant to section 365(a) of the Bankruptcy Code?

Holding: The Eighth Circuit reversed the previous decisions and held that the license agreement was not executory because it was part of a larger, integrated agreement that IBC had substantially performed. Under the applicable Illinois law, "where two or more instruments are executed by the same contracting parties in the course of the same transaction, the instruments will be considered together." Accordingly, the court considered the license agreement and the asset purchase agreement as a single agreementand found that the essence of the agreement was the sale of IBC's operations

[12] The Labels at issue included Wonder, Mrs. Karl's, Butternut, Sunbeam, and Weber's. "Label" was defined to include, *inter alia*, "all legal rights associated with a brand's trademarks, trade names, copyrights, designs, and trade dress."

and assets, and not just the licensing of the trademarks. Because IBC had "transferred all of the tangible assets and inventory to LBB, executed the License Agreement, and received the full $20 million purchase price from LBB," the court held that the contract was not executory. The only remaining obligation concerned the license, which did not relate to the central purpose of the agreement, which was to sell the operations and assets to LBB in certain territories.

V. Claims

A. *In re MPM Silicones, LLC,* Case No. 14-22503-rdd, 2014 Bankr. LEXIS 3926 (Bankr. S.D.N.Y. Sept. 9, 2014) (make-whole, subordination)

Facts: In 2012, the debtors issued $1.1 billion of first-lien notes and $250 million of 1.5-lien notes due in 2020 under indentures that included an optional redemption provision which contained introductory language providing that, except for in circumstances triggering payment of the make-whole, the Noteholders could not voluntarily redeem the Notes before October 15, 2015. Shortly after the debtors filed voluntary petitions for bankruptcy under chapter 11, the debtors filed declaratory judgment actions challenging the Noteholders' right to more than $200 million in claims for make-whole premiums. The debtors proposed a plan which provided that the Noteholders would receive: (i) payment of their claims in full in cash, without a make-whole premium, if they voted in favor of the plan or (ii) seven-year replacement notes in the face amount of their allowed claims, bearing a below-market interest rate equal to the applicable Treasury rate plus a modest risk premium, and the right to litigation their entitlement to the make-whole premiums, if they rejected the plan. The Noteholders overwhelmingly rejected the plan and filed objections arguing that: (i) they were entitled to the make-whole premiums based on the automatic acceleration of their debt resulting from the bankruptcy filing and the Debtors' early repayment of this debt in the form of the replacement notes issued under the plan and (ii) their treatment under the plan as a result of their rejection was not "fair and equitable" because the plan did not apply the market interest rate to the replacements notes and, therefore, the debtors could not cramdown the plan over their objections. The Noteholders also sought permission to change their votes to accept the plan and concede the make-whole premium argument after the confirmation hearing but before the court issued a ruling.

Issues:

- Whether the Noteholders were entitled to the make-whole premiums?
- Whether the proposed replacement notes satisfied the cramdown requirements of section 1129(b) of the Bankruptcy Code?

Holding: The bankruptcy court held that the Noteholders were not entitled to the make-whole premiums because the plain language of the indentures did not provide for a valid make-whole claim, there was no claim for breach of a purported "no-call" provision under the indentures, and the automatic stay barred deceleration of the debt. The court found that the replacement notes would satisfy the cramdown requirements if the rate was slightly increased. The court agreed with the debtors that the formula approach,[13] and not the market interest rate, is the correct way to calculate cramdown interest for secured creditors in a chapter 11 case. However, because the Treasury rate was used rather than the prime rate, the rate had to be slightly increased to make the plan confirmable, although the interest rate was still well below market rates.

B. *In re KB Toys, Inc.*, 736 F.3d 247 (3d Cir. 2013) (claims trading and 502(d))

<u>Facts</u>: ASM Capital, L.P. and ASM Capital II, LLP (together, "ASM") purchased claims from various trade claimants to whom the debtors owed money. Each of the original claimants was listed on the debtors' statement of financial affairs as having received a payment within 90 days of the petition date and, accordingly, the trustee brought preference actions against the original claimants and eventually obtained a judgment in each case. The judgments were all uncollectible because all of the original claimants had gone out of business. ASM purchased eight of the nine claims before the trustee commenced the preference actions and one after the trustee obtained a judgment. The trustee filed an objection seeking to disallow the claims based on the preferences received by the original claimants. The bankruptcy court disallowed the claims and held that, under section 502(d), "disabilities attached to and travel with the claim" and noted that ASM is a sophisticated entity who had access to the SOFA and the original claimants and could have discovered the potential preference actions with very little due diligence. The district court affirmed the bankruptcy court's holding, but noted that the language of section 502(d) was ambiguous.

<u>Issue</u>: Whether a trade claim that is subject to disallowance under section 502(d) of the Bankruptcy Code in the hands of the original claimants is similarly disallowable in the hands of a subsequent transferee?

<u>Holding</u>: The Third Circuit held that the answer is yes and affirmed the holdings of the lower courts. The court explained that because section 502(d) focuses on claims, and not claimants, "claims that are disallowable under § 502(d) must be disallowed no matter who holds them." Any contrary holding could incentivize an original claimant to sell his claim and thereby receive value for an otherwise valueless claim. Allowing an original claimant to do this would negatively impact other creditors because the estate would have less money and so the other creditors would receive smaller amounts and it would undermine the purpose of section 502(d), "coercing compliance with judicial orders."

C. *Official Comm. of Unsecured Creditors v. UMB Bank, N.A. (In re Residential Capital, LLC)*, 501 B.R. 549 (Bankr. S.D.N.Y. 2013) (OID, adequate protection)

<u>Facts</u>: In 2008, before the debtors filed voluntary petitions for bankruptcy under chapter 11, Residential Capital, LLC ("ResCap") issued junior secured notes in connection with a

[13] In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), the Supreme Court applied a "formula" approach under which the proper interest rate is determined by taking a risk-free base rate, such as the prime rate or the Treasury rate, and adding a risk premium to reflect the repayment risks unique to that debtor, which is generally between 1-3%.

debt-for-debt exchange offering. Pursuant to the exchange, ResCap offered to exchange $9.537 billion face value amount of its then-outstanding unsecured notes (the "Old Notes") for the junior secured notes. ResCap exchanged $1,000 face amount of Old Notes for $800 face amount of junior secured notes. Holders of the Old Notes had the option to elect to receive cash instead of the junior secured notes pursuant to a modified Dutch auction, at which the clearing price was $650 per $1,000 principal amount of junior secured notes. Based on the trading activity, the issue price of the junior secured notes was established as $613.75. Because the issue price was below the face amount of the junior secured notes, the exchange created an original issue discount ("OID") for tax purposes, which remained unamortized in the amount of $386 million as of the petition date. ResCap and the creditors' committee (collectively, the "Plaintiffs") and the junior secured noteholders (the "JSNs") do not dispute that the exchange was a "fair value" exchange (i.e., that "old securities were exchanged for new securities with a reduced principal amount that in theory approximated the market value of the old securities"), but the Plaintiffs argue that the OID should be disallowed in bankruptcy as unmatured interest. The JSNs argue that the OID should be allowed as part of their claim based on the Second Circuit's precedent in *LTV Corp. v. Valley Fidelity Bank & Trust Co. (In re Chateaugay Corp.)*, 961 F.2d 378 (2d Cir. 1992), where the Second Circuit held that OID created by face value exchanges are allowable in bankruptcy.

The JSNs also argued that they are entitled to recover an adequate protection claim of $515 million based on an alleged diminution in value of their prepetition collateral used during the case under a series of consensual cash collateral orders. The Plaintiffs disagreed and argued that the JSNs collateral has not declined in value since the petition date and thus the JSNs could not assert an adequate protection claim. The parties agreed that the amount of any adequate protection claim should be measured by the difference in value of the collateral on the petition date and on the effective date, and essentially agreed on the effective date value of the collateral, but disputed the petition date value of the collateral.

Issues:

- Whether the JSNs are entitled to recover all original issue discount?
- Whether the JSNs are entitled to an adequate protection claim?

Holding: The bankruptcy court held that, pursuant to Second Circuit law, the JSNs are entitled to recover all OID. The court rejected the Plaintiff's argument that *Chateaugay* was distinguishable and held that the same rule on allowance of unamortized OID should apply to both face value debt-exchanges (as held in *Chateaugay*) and fair value debt-exchanges. The court explained that there is "no commercial or business reason, or valid theory of corporate finance, to justify treating claims generated by face value and fair value exchanges different in bankruptcy." However, the court held that the JSNs failed to carry their burden of proving a diminution in the value of their collateral and, accordingly, their adequate protection claim failed. In reaching its holding, the court agreed with the JSNs that the fair market value of the collateral in the hands of the debtors, rather than the foreclosure value, applied but ultimately held that the JSNs fair market valuation evidence was unreliable and "vastly" overstated the value of the collateral on the petition date.

D. *In re NE OPCO, Inc.*, 501 B.R. 233 (Bankr. D. Del. 2013); *P.R. Elec. Power Auth. v. Rentas (In re PMC Mktg. Corp.)*, Bankruptcy Case No. 09-02048-BKT, 2014 Bankr. LEXIS 4085 (B.A.P. 1st Cir. Sept. 23, 2014)(electricity as "good" under 503(b)(9))Facts:

- *In re NE OPCO, Inc.* – A utility provider requested an administrative expense claim under section 503(b)(9) of the Bankruptcy Code in the amount of $93,262.55 for the electricity and natural gas it provided to the debtors in the 20 days prior to the debtors' bankruptcy. The debtors did not dispute that the utility provider delivered electricity and natural gas in the ordinary course of the business within the 20-day period, but objected that electricity did not constitute a good within the meaning of section 503(b)(9), and therefore the claim was not entitled to administrative priority status.
- *Puerto Rico Electric Power Authority* – A utility provided filed a motion requesting an administrative expense claim under section 503(b)(9) of the Bankruptcy Code in the amount of $89,336.42, representing the value of its claim for electricity supplied to the debtors in the 20-day period preceding the petition date and argued that electricity satisfies the definition of a "good" under the U.C.C. and section 503(b)(9). The chapter 7 trustee did not address the issue of whether electricity is a good but objected that the motion was a disguised and extremely belated proof of claim. The bankruptcy court dismissed the trustee's timeliness challenge but found that the provider's provision of electricity was a service and that the provider was not entitled to an administrative expense claim under section 503(b)(9). In reaching its holding, rather than considering whether electricity is a "good," the bankruptcy court first determined that the provider was a utility and then considered whether a utility provides services rather than a "good." Accordingly, the bankruptcy court focused on the relationship between the utility provider and the debtors, rather than considering whether electricity is, in and of itself, a "good" or a "service."

Issues:

- *In re NE OPCO, Inc.* – The bankruptcy court considered three issues: (i) whether electricity and natural gas are "goods" under section 503(b)(9); (ii) are the details of the bills adequate under the apportionment test to establish the amount of any allowed section 503(b)(9) claim; and (iii) whether the court should require immediate payment of any section 503(b)(9) claim.
- *Puerto Rico Electric Power Authority* – Whether the bankruptcy court erred in concluding that the electricity the provider supplied to the debtors within 20 days of the petition date is a "service" rather than a "good" entitled to priority treatment as an administrative expense under section 503(b)(9)?

Holdings:

- *In re NE OPCO, Inc.* – The court agreed with the debtors that electricity is not a good within the meaning of section 503(b)(9) because "in order for something to be a good under the U.C.C. and, thus, section 503(b)(9) of the Bankruptcy Code, it must be movable at the time of identification to the contract for sale" and, while electricity is identified as it passes through a meter, it is almost immediately consumed. The lack of a "meaningful delay" between identification and consumption is too short to establish that electricity is moveable at the time of identification and, accordingly, the court held that electricity is not a good. However, because natural gas is specifically identified as a "good" under the U.C.C., the court still had to determine the amount of the utility provider's 503(b)(9) claim. The court explained that, because the U.C.C. governs the sale of goods and not the sale of services, courts have developed two tests, the predominate purpose test and the apportionment test, to address hybrid claims that involve both goods and services. The court adopted the apportionment test, "where the Court considers each element of the bill item by item and then awards an administrative expense claim for that portion of the transaction relating to the sale of goods." Applying the apportionment test, the bankruptcy court found that several categories of the provider's bill were for services and not goods and that there was insufficient detail regarding how the provider calculated certain goods. Accordingly, the court limited the claim to $78.08. Finally, the court noted its discretion in determining when an administrative expense claim will be paid and, because the provider did not present any evidence necessitating immediate payment, the court did not require immediate payment of the claim.
- *Puerto Rico Electric Power Authority* – The bankruptcy appellate panel held that the bankruptcy court's approach to determining whether the provision was a good or a service was "inherently flawed" and that a proper analysis of whether electricity constitutes a "good" for the purposes of section 503(b)(9) must begin with an analysis of the term "good." Accordingly, the court vacated the bankruptcy court's order and remanded to the bankruptcy court for further proceedings.

E. *Jacobs v. Kraken Inv. Ltd. (In re Salander-O'Reilly Galleries, LLC)*, 506 B.R. 600 (Bankr. S.D.N.Y. 2014) (blanket lien trumps unperfected consignment)

Facts: An involuntary chapter 7 case (which was later converted to a voluntary chapter 11 case) was commenced against the debtor while the debtor was in possession of over 4,000 works of art, many of which were subject to the claims or interest of various parties, including Boticelli's *Madonna and Child* (the "Boticelli"). The Boticelli is owned by Kraken Investments Limited ("Kraken") and was consigned to the debtor's gallery for a one-year period in 2004. In 2006, Kraken entered into a second agreement to consign the Boticelli to the debtor for another one-year period. Pursuant to this agreement, the debtor agreed to list the Boticelli for sale for $9.5 million, with a sale to result in a commission to the debtor of $1 million and no less than $8.5 million payable to Kraken. Kraken did not file a UCC-1 financing statement with respect to either consignment. After the second consignment ended, one of Kraken' agents moved the Boticelli to her apartment for storage, and it was later loaned to the debtor's gallery for an exhibition. The liquidation trustee (the "Trustee") argued that there was no evidence that the Boticelli was ever removed from the gallery after the second consignment ended. Before the debtor's bankruptcy, Kraken demanded the return of the Boticelli and filed suit in New York state court seeking seizure of the Boticelli, but after the bankruptcy case was commenced, Kraken's state court action was stayed. The bankruptcy court later approved a protocol for the assertion and resolution of claims of ownership against artwork in the possession, custody, or control of the debtor. In compliance with this protocol, Kraken filed an art claim. The working group charged with determining whether such claims constituted claimed estate assets or non-estate assets did not label the Boticelli a non-estate asset, but, instead, sent a letter to Kraken proposing a mediation, which mediation was ultimately unsuccessful.

Under a prepetition loan agreement, the debtor had granted Bank of America (the "Bank") a continuing security interest in all of the debtor's "personal and fixture property of every kind and nature including without limitation all goods (including inventory, equipment, and any accessions thereto) . . . and all products and proceeds of the foregoing." The Bank perfected its blanket security interest in substantially all of the debtor's assets by filing a UCC-1 financing statements stating that the collateral securing the loan agreement included "all works of arts." In connection with allowing the Bank's claim pursuant to the debtor's liquidating plan, the debtor was assigned the Bank's lien. Ultimately, the Trustee objected to Kraken's claim and argued that Kraken failed to perfect its interest in the Boticelli and that the Trustee had a superior right to Boticelli, either (i) pursuant to section 544 of the Bankruptcy Code, which permits a trustee to avoid certain unperfected interests in the debtors' property or (ii) as an assignee of the Bank's perfected lien in the Boticelli. In response, Kraken argued that the trustee could not exercise any rights under section 544 with respect to the Boticelli because the debtor did not have any interest in the Boticelli as of the petition date and that the Bank's lien did not extend to goods that the debtor held on consignment, like the Boticelli.

Issues:

- Whether a perfected blanket lien on the debtor's inventory attached to the Boticelli while it was on consignment to the debtor's art gallery; and
- If so, whether the lien has priority over the consignor's interest in the return of the painting?

Holding: The bankruptcy court held that material issues of fact precluded summary judgment for either party. The court agreed that Kraken owns the Boticelli but explained that certain provisions of the Uniform Commercial Code allow creditors of a consignee such as the debtor to obtain rights in consigned goods that are superior to those of the actual owner of the goods if the owner fails to take steps to perfect its interest. However, because the burden of proof was on the Trustee to establish that the applicability of the relevant UCC provisions, and the Trustee failed to produce any evidence on this issue, the court held that it could not hold one way or another as to whether the transaction by which the Boticelli came into the debtor's possession was governed by the UCC. The court held that Kraken had not established its entitlement to summary judgment. First, the court concluded that the Bank's blanket lien on artwork held by the gallery applied to the Botticelli while it was on consignment in the debtor's art gallery. Second, the court held that the pre-petition termination of the second consignment did not necessarily entitle Kraken to the Boticelli because (i) the case cited by Kraken for the proposition that the pre-petition termination of a consignment agreement requires the return of the consigned goods did not involve the rights of a competing lienholder in the consigned goods, and thus was not controlling, (ii) the protocol approved by the bankruptcy court regarding art claims did not mandate the return of the Boticelli because the working group did not unanimously believe that the Boticelli was a non-estate asset, and (iii) Kraken's argument that the removal of the Boticelli following the second consignment was based on a disputed issue of fact, which the court could not resolve at the summary judgment stage.

VI. Chapter 15

A. *In re ABC Learning Ctrs. Ltd.*, 728 F.3d 301 (3d Cir. 2013) (recognition and the public policy exception)

Facts: ABC Learning Centres Ltd. ("ABC") is an Australian child care and educational service provider that conducted business in the United States through subsidiaries ABC Developmental Learning Centres (USA) Inc. ("ABC Delaware") and the Learning Care Group ("LCG"). RCS Capital Development LLC ("RCS") contracted with ABC Delware to develop child care facilities in the U.S. RCS won an award of $47 million in a breach of contract action against ABC Delaware on May 14, 2010. ABC and ABC Delaware brought a separate action seeking damages against RCS. In November, 2008, ABC entered into Voluntary Administration in Australia, in breach of its loan agreements with its secured creditors. As a result, ABC's secured creditors exercised their right to appoint a receiver. ABC was entirely leveraged, so all of its assets were encumbered by the secured creditors'. In June 2010, ABC entered into liquidation proceedings, and two of the administrators were appointed as liquidators to wind down the company. The receivership continued and operated in conjunction with the liquidation. On May, 26. 2010, the liquidators petitioned for recognition of the Australian insolvency proceedings in the Bankruptcy Court for the District of Delaware. The Bankruptcy Court ordered recognition, serving to impose the automatic stay. The award against ABC Delaware had not yet been rendered into a judgment, and the court in that action was thus stayed from entering the judgment. RCS appealed from the order of the District Court upholding the decision of the Bankruptcy Court, arguing that the Australian proceedings were not subject to mandatory recognition because the receivership was not "collective in nature." RCS further argued that, even though the liquidation proceedings were collective in nature, they were dominated by the receivership because of the debtors' leveraged nature, and recognition would therefore public policy.

Issues:

- Did liquidation proceeding meet the requirements for mandatory recognition despite the fact the ABC's assets were entirely leveraged?
- Does recognition of a foreign liquidation proceeding violate U.S. public policy where all of the benefit of the proceedings will be realized through a non-collective receivership proceeding?

Holding: The Australian liquidation proceeding was entitled to mandatory recognition because leveraged nature of the debtors assets and the disposal of those assets in a receivership proceeding did not affect the collective nature of an Australian liquidation proceeding. The receivership proceeding, through which secured creditors were entitled to recover the full value of their debts by realizing the value of the assets securing those debts, was not manifestly contrary to U.S. public policy. The receivership proceeding was just another way to achieve a similar goal as the U.S. Bankruptcy Code, which also prioritizes secured creditors.

B. *Drawbridge Special Opportunities Fund LP v. Barnet (In re Barnet)*, 737 F.3d 238 (2d Cir. 2013) (recognition and 109(a))

Facts: On October 3, 2008, Octaviar Administration Pty Ltd. ("OA"), an Australian corporation, was placed into "external administration" in its home country. The Supreme Court of Queensland ordered that OA be liquidated. Certain Australian affiliates of the Drawbridge Special Opportunities Fund LP ("Drawbridge") were investigated in connection with the investigation of OA's affairs, and on April 3, 2012, a lawsuit was commenced against those affiliates in Australia. On August 13, 2012, OA's Australian liquidators (the "Foreign Representatives") petitioned the Bankruptcy Court for the Southern District of New York for recognition of the Australian liquidation proceedings as a foreign main proceeding under 11 U.S.C. § 1515. Drawbridge objected. The Bankruptcy Court entered an order recognizing the OA's foreign main proceeding on September 6, 2012, (the "Recognition Order") and Drawbridge appealed. On joint application of the Foreign Representatives and Drawbridge, the Bankruptcy Court certified the Recognition Order for direct appeal to the Second Circuit to determine whether a chapter 15 debtor must satisfy the requirements 11 U.S.C. § 109(a), which provides that "only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title." The Foreign Representatives argued that § 109(a) need not be satisfied because: (1) OA was not a debtor under Title 11, but rather a debtor under Australian law; (2) a chapter 15 debtor need only meet the requirements of the Chapter 15- specific definition of "debtor," and not also the § 109(a) requirements; and (3) the context of the statutes and purpose of Chapter 15 support the Foreign Representative's interpretation.[14]

[14] Specifically that 11 U.S.C. § 1528, which allows a chapter 15 debtor recognized in a foreign main proceeding to commence a case under another chapter of Title 11 "only if the debtor has assets in the United States" and 28 U.S.C. § 1410, which for venue for a chapter 15 debtor with

Issue: Must a chapter 15 debtor have "a domicile, a place of business, or property in the United States"?

Holding: The Court rejected the Foreign Representatives' arguments, holding that the plain language of section 109(a) requires that any title 11 debtor, including a chapter 15 debtor, have "a domicile, a place of business, or property in the United States." The Court reasoned that 11 U.S.C. § 103(a) makes chapter 1 of the Bankruptcy Code applicable in a case under chapter 15, and because § 109(a) is part of chapter 1 it is thus applicable to a chapter 15 debtor.

C. *Krys v. Farnum Place, LLC (In re Fairfield Sentry Ltd.),* No. 13-3000, 2014 WL 4783370 (2d Cir. Sept. 26, 2014) (independent review of asset sales);

Facts: Sentry is a British Virgin Islands ("BVI") investment fund, which had invested approximately 95% of its assets with Bernard L. Madoff Investment Securities, LLC ("BLMIS"). BLMIS was placed in liquidation under the Securities Investor Protection Act ("SIPA"). Sentry filed claims in the BLMIS SIPA liquidation. Sentry and BLMIS entered into a settlement by which Sentry's claims were allowed in an amount of $230 million. In July 2009, Sentry was placed into liquidation in the BVI, and Kenneth Krys ("Krys") was appointed as liquidator. Krys sought and received recognition of the BVI liquidation as a foreign main proceeding in the Bankruptcy Court for the Southern District of New York. Among Sentry's assets was its SIPA claim against the BLMIS estate. In 2010, Sentry auctioned off its SIPA claim to Farnum Place, LLC ("Farnum") for 32.125% of its allowed amount. Farnum and Krys entered into a Trade Confirmation, governed by New York law, setting forth the terms and conditions of the sale. Three days after the Trade Confirmation was signed, a settlement was reached in the BLMIS case which had the effect of increasing the value of the SIPA claim from 32% of its allowed amount to over 50% of its allowed amount. Thereafter, despite Krys's request that the court not approve the sale because of the increase in value of the SIPA claim, the BVI approved the sale to Farnum and ordering Krys to bring the issue of approval before the U.S. Bankruptcy Court. Krys then filed an application with the U.S. Bankruptcy Court, seeking an order disapproving the sale. The Bankruptcy Court denied Krys's application, holding that the sale did not "involve the transfer of an interest in property within the United States" so as to require a section 363 review under section 1502(a)(2), and that comity required the Bankruptcy Court to give deference to the BVI judgment.

Issues:

- Was the sale of the SIPA claim a "transfer of an interest of the debtor in property that is within the territorial jurisdiction of the United States" under 11 U.S.C. 1502(a)(2), thus requiring the Bankruptcy Court to conduct a review of the sale under section 363 of the Bankruptcy Code?

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no business or assets in the United States under, both contemplate recognition of a chapter 15 debtor with no business or property in the U.S.

- Do the principals of comity require a U.S. Bankruptcy Court to give deference to a foreign courts approval of a sale in a foreign main proceeding?

Holding: The sale of the SIPA claim required a review under section 363 because it was a transfer of an interest of property within the United States. The SIPA claim was within the U.S. because it was subject to attachment or garnishment under New York law, which provides that "any property which could be assigned or transferred" is subject to attachment or garnishment. Intangible property that "has as its subject a legal obligation to perform" is located where "the party of whom that performance is required pursuant to that obligation" is located. The SIPA claim obligated the SIPA trustee to distribute a pro rata share of the BLMIS estate to Sentry. Therefore, the SIPA claim was located in New York. Comity did not require deference by the Bankruptcy Court to the BVI approval of the sale because Chapter 15 expressly requires a section 363 review of such a sale. The Court also noted that the Bankruptcy Court was required to consider in its section 363 review the increase in value of the SIPA claim after the Trade Confirmation was signed because section 363 does not limit the review of a sale to the date the sale agreement was signed.

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Biographical information – Hon. Robert Drain

Robert Drain is a United States Bankruptcy Judge for the Southern District of New York.

He received his B.A. degree *cum laude* with honors from Yale University in 1979 and his J.D. degree in 1984 from the Columbia University School of Law, where he was a Harlan Fiske Stone Scholar for three years.

Judge Drain is a fellow of the American College of Bankruptcy and a member of the American Bankruptcy Institute, the International Insolvency Institute, and the National Conference of Bankruptcy Judges. He is a past member and secretary of the Bankruptcy and Reorganization Committee of the Association of the Bar of the City of New York. He is an adjunct professor at St. John's University School of Law's L.L.M. in Bankruptcy Program and has lectured and written on numerous bankruptcy-related topics.

Robert J. Feinstein, Esq.

Robert J. Feinstein is the Managing Partner of the New York office of Pachulski Stang Ziehl & Jones LLP, the nation's leading corporate restructuring boutique. For over thirty-plus years, he has represented official creditors' committees, debtors, equity committees, acquirers, trustees and examiners, among others, in business reorganizations and related bankruptcy litigation. Mr. Feinstein is a graduate of Lafayette College and received his J.D. magna cum laude from Boston University School of Law. He is an Adjunct Professor in the LL.M. in Bankruptcy Program at St. John's University School of Law, an Associate Editor of the Norton Journal of Bankruptcy Law and Practice, a Contributing Editor of Norton Bankruptcy Law and Practice 2d, a member of the American Bankruptcy Institute, and was a member of the Bar Association of the City of New York Committee on Bankruptcy and Corporate Reorganization (2008-2011). He was recently invited to join the International Insolvency Institute, which is comprised of the world's leading practitioners, academics, judges, and financial industry restructuring professionals. He has authored numerous articles and frequently lectures on bankruptcy topics for, among others, the American Bankruptcy Institute, the Norton Institutes on Bankruptcy Law, the Turnaround Management Association and the National Association of Credit Managers. He was named a leading bankruptcy and restructuring practitioner in Chambers USA, a "New York Super Lawyer" in Bankruptcy and Debtors/Creditors Rights by Thomson Reuters, and one of the top 100 restructuring and turnaround professionals by Global M&A Network. He holds an "AV Preeminent" peer rating, the highest awarded by Martindale Hubbell.

Mr. Feinstein's recent engagements include serving as lead counsel to the Ad Hoc Movie Studio Committee in the Blockbuster chapter 11 case; lead counsel to the official creditors' committees appointed in the chapter 11 cases of AMF Bowling Worldwide, Ashley Stewart, Circuit City, Salander O'Reilly Galleries, Movie Gallery, Freedom Communications, Coach Transportation, Reddy Ice Corporation, Frank Parsons, Inc., Neff Manufacturing, Flying J, Gas City, Palm Harbor Homes and National Envelope Corporation; conflicts counsel to the official creditors' committees appointed in the Residential Capital (ResCap) and Chrysler LLC chapter 11 cases and conflicts counsel to the 2nd lien debt holders of Energy Future Intermediate Holding, LLC in the 8th largest bankruptcy in U.S. history. On the debtor side, he represents movie special effects studio Digital Domain, and represented boxer Mike Tyson, Penthouse Magazine publisher General Media, Inc., Dice, Inc., Hvide Marine Incorporated and Hexcel Corporation in their chapter 11 reorganization cases.

ROSEMARY GAMBARDELLA
BIOGRAPHY

Rosemary Gambardella was sworn in as a United States Bankruptcy Judge on May 3, 1985, becoming the first woman to serve on the Bankruptcy Court in the District of New Jersey. A native of Newark, Judge Gambardella attended Rutgers University where she was elected to Phi Beta Kappa and obtained a bachelor of arts degree in history in 1976. After receiving her law degree from Rutgers Law School-Newark in 1979, Judge Gambardella served as law clerk to the late Chief Bankruptcy Judge Vincent J. Commisa from 1979 to 1980. From 1980 to 1985, she was senior staff counsel to Hugh M. Leonard, then United States Trustee for the Districts of New Jersey and Delaware. Judge Gambardella served as Chief Judge of the United States Bankruptcy Court for the District of New Jersey from August 12, 1998 to August 11, 2005. She is a member of the Lawyers Advisory Committee of the Bankruptcy Court for the District of New Jersey, a member and former President of the New Jersey Bankruptcy Inn of Court and a member of the Bankruptcy Committee of the Third Circuit Task Force on Equal Treatment in the Courts - Gender Commission. In addition, she is a member of the National Association of Women Judges, the National Conference of Bankruptcy Judges, the American Bankruptcy Institute, the Turnaround Management Association and former member of the Bankruptcy Judges Advisory Group for the Administrative Office of the United States Courts. Judge Gambardella was the Bankruptcy Judge representative to the Judicial Conference of the United States (2009-2011) and is a Fellow of the American College of Bankruptcy.

Christopher S. Sontchi is a United States Bankruptcy Judge for the District of Delaware and a frequent speaker in the United States and Canada on issues relating to corporate reorganizations. He is a Lecturer in Law at The University of Chicago Law School and an Adjunct Professor of Law at Widener Law School in Wilmington, Delaware. He is also a member of the National Conference of Bankruptcy Judges and the American Bankruptcy Institute. Judge Sontchi is currently serving on the *Committee on Financial Contracts, Derivatives and Safe Harbors* of the American Bankruptcy Institute's Commission to Study the Reform of Chapter 11. He also recently published *Valuation: A Judge's Perspective* in the American Bankruptcy Institute Law Review.

Judge Sontchi attended the University of North Carolina at Chapel Hill where he was elected to *Phi Beta Kappa* and obtained a B.A. with distinction in Political Science. He received his J.D. from The University of Chicago Law School, after which he returned to his native Delaware to serve as a law clerk to the Hon. Joseph T. Walsh in the Delaware Supreme Court.