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Taking a Stand Where Few Have Trodden

Structured Dismissal Held Clearly Authorized By Bankruptcy Code

By Charles M. Oellermann and Mark G. Douglas

A "structured dismissal" of a Chapter 11 case following a sale of substantially all of the debtor's assets has become increasingly common as a way to minimize cost and maximize creditor recoveries. However, only a handful of rulings have been issued on the subject, perhaps because bankruptcy courts are unclear as to whether the Bankruptcy Code authorizes the remedy. A Texas bankruptcy court recently added to this slim body of jurisprudence. In *In re Buffet Partners, L.P.*, 2014 BL 207602 (Bankr. N.D. Tex. July 28, 2014), the court ruled that sections 105(a) and 1112(b) of the Bankruptcy Code provide authority for such a structured dismissal, noting that the remedy "is clearly within the sphere of authority Congress intended to grant to bankruptcy courts in the context of dismissing Chapter 11 cases."

Structured Dismissals

In a typical successful Chapter 11 case, a plan of reorganization or liquidation is proposed, the plan is confirmed by the bankruptcy court, the plan becomes effective and, after the plan has

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The First Circuit's Non-Unanimous Rejection Of the Blanket Rule on Stay Relief Denials

By Steven B. Smith

Are orders denying relief from the automatic stay pursuant to Section 362 of the Bankruptcy Code considered final and, therefore, appealable as of right? This was the issue of first impression that was recently presented to the U.S. Court of Appeals for the First Circuit in *Pinpoint I Services, LLC v. Rivera* (*In re Atlas IT Export Corp.*), 761 F.3d 177 (1st Cir. 2014). Until this decision, it was a question with a predictable answer — yes. Predictable, because seven of the eight circuit courts that have considered this issue have reached the same result — yes, such orders are final and appealable.

The First Circuit, however, mindful of avoiding the apparently observable herding phenomenon, rejected the blanket-rule approach in favor of what it describes as a more nuanced one which requires courts to be mindful of the multiple layers and many moving parts inherent in bankruptcy litigation while scouting for "finality indicators." This article explores the reasoning behind the First Circuit's decision to create a circuit split rather than deciding the question presented by ruling on the merits.

The *Atlas* Facts and the First Circuit Appeal

Pinpoint IT Services, LLC, a Virginia company (Pinpoint) and Atlas IT Export Corp., a Puerto Rico company (Atlas) each filed dueling federal court actions based upon a contract between them. Pinpoint commenced a breach of claim action against Atlas in the Eastern District of Virginia, but before the Virginia court could issue a ruling on Atlas' motion to change venue to the District of Puerto Rico, Atlas commenced its own action against Pinpoint in the District of Puerto Rico. Shortly thereafter, the Virginia court denied the change of venue motion, and, as a result, Pinpoint requested that the Puerto Rico action be stayed. Atlas, however, commenced a Chapter 7 bankruptcy case, thereby automatically staying both the Virginia and Puerto Rico actions.

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Stay Relief Denials

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While the bankruptcy court ultimately granted the Chapter 7 trustee's request for stay relief, allowing the Puerto Rico action — including Atlas' claims and Pinpoint's counterclaims — to proceed to judgment, the court denied Pinpoint's lift-stay motion, which sought to allow the Virginia action as the first-filed action, to proceed. The court held, among other things, that the parties could seek adjudication of the first-filed rule in the non-stayed Puerto Rico action. Pinpoint appealed to the BAP, which dismissed it for lack of jurisdiction, holding that the order denying stay relief was not a final order because it did not prevent Pinpoint from raising its first-to-file argument in the Puerto Rico action.

Pinpoint's appeal to the First Circuit focused on the following two issues: 1) whether the First Circuit had jurisdiction; and 2) whether the bankruptcy court and BAP decisions violated the first-filed rule.

The Relevant Jurisdiction Standard and the Blanket Rule on the Appealability of Stay Relief Denials

The relevant standard for jurisdiction can be found in 28 U.S.C. § 158(d)(1), which provides, in pertinent part, that "courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, *orders*, and decrees … " *See* 28 U.S.C. §(d)(1) (emphasis added). The threshold question presented to the First Circuit, then, was whether the BAP and the bankruptcy court's orders denying stay relief constituted "final" orders. Now there is no dispute — even within the First Circuit — that orders granting stay relief are considered final orders, and appealable as of right, because they dispose of all the issues of a discrete dispute within a larger case. But can the same be said for orders denying stay relief? The answer, at least according to the Second, Fourth, Fifth, Eighth, Ninth, Tenth and Eleventh circuits, is yes. Orders denying stay relief are final and therefore appealable of right. That's the blanket rule.

The 'Herding' Phenomenon and the First Circuit's Rejection of the Blanket Rule

The First Circuit was unimpressed with the numbers favoring the blanket rule because it implied that one or more of the circuits favoring such a rule had likely succumbed to the apparently observable phenomenon called "herding" or "cascading" whereby, in the words of the First Circuit, "decisionmakers who first encounter a particular issue … are more likely to rely on the record presented to them and their own reasoning, while later courts are increasingly more likely to simply go along with the developing group consensus." *Pinpoint*, 761 F.3d at 182-83. Reviewing the question presented "afresh," the First Circuit seemed troubled by the fact that the blanket rule applied regardless of the specific circumstances of the case, and it pointed to the Third Circuit's decision in *In re West Electronics, Inc.*, 852 F.2d 79 (3d Cir. 1988) as an example of another circuit that refused to adopt the blanket rule without performing a more fact-specific, case-by-case analysis.

In *West*, the Third Circuit noted that when the other circuits applied the blanket rule, they did so because the orders in dispute had conclusively decided the contested issue as evidenced by the fact that the bankruptcy courts in those cases had nothing further to do. *Id*. at 81-82. But, where an order denies stay relief without prejudice for, among other issues, 1) an incomplete record; or 2) ongoing discovery, those are signs of nonfinality. *Id*. at 82.

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Steven B. Smith is counsel in the Financial Restructuring & Bankruptcy practice of Dickstein Shapiro LLP in New York. A member of this newsletter's Board of Editors, he focuses on complex corporate restructuring and creditors' rights, including in-court Chapter 9, 11 and 15 bankruptcy cases and out-of-court workouts. He can be reached at smiths@dicksteinshapiro.com.

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‘Triggering Event Test’

By Aram Ordubegian and M. Douglas Flahaut

In the preference avoidance context, the insolvency of the debtor is an element of the *prima facie* case that is not commonly litigated. When it is litigated, however, the scope of a debtor’s liabilities can make or break the case. This is because under established case law, if a liability is determined to be “contingent,” then courts are required to discount the face value of that liability by the estimated probability of the contingency occurring and the contingent liability becoming an actual liability. If the liability is deemed to be “non-contingent,” then the entire amount of the judgment can be added to the liability side of the balance sheet to usually make the debtor insolvent, thereby satisfying the insolvency element.

In August 2014, the Bankruptcy Appellate Panel for the Ninth Circuit (the Panel) issued a decision upholding a published decision by Judge Julia W. Brand in the Central District of California that left no doubt that the so-called “triggering event test” was the appropriate test to determine whether a liability is contingent or not for the purpose of showing insolvency under 11 U.S.C § 547. The decisions are notable because prior to the bankruptcy court’s decision, no court in the Ninth Circuit had provided clear guidance as to what constitutes a contingent liability in the specific context of an insolvency analysis under 11 U.S.C. § 547. Applying the “triggering event test” to the facts at hand, the Panel held that a state court judgment is a non-contingent liability in its full amount for purposes of determining the insolvency of the debtor, even though on the date in question the judgment was not final under state law and the debtor had expressed optimism that the judgment would likely be overturned on appeal.

Factual Background

The debtor, Imagine Fulfillment Services, Inc. (IFS), is a full-service fulfillment company providing assembly, warehouse, and shipping services. Prior to the filing of its bankruptcy petition, a multimillion-dollar judgment was entered against IFS in California Superior Court. With judgment in hand, the judgment creditor then perfected a judgment lien on all of IFS’s assets and, shortly thereafter, began to exercise its state law rights as a secured creditor by, among other things, levying on IFS’s bank accounts.

IFS filed a timely appeal of the state court judgment and was optimistic about its chances on appeal. However, it nevertheless decided to seek bankruptcy protection and filed its voluntary petition under Chapter 11 within 90 days of the perfection of the judgment lien. After filing for Chapter 11 protection, IFS immediately commenced an adversary proceeding in bankruptcy court against the judgment creditor seeking to avoid the judgment lien pursuant to 11 U.S.C. § 547, as a preferential transfer.

After substantial discovery and significant litigation in the adversary case, IFS and the judgment creditor eventually agreed that all the elements of a preferential transfer had been established, except the requirement under 11 U.S.C. § 547 that the transfer in question be made “while the debtor was insolvent.” More specifically, the judgment creditor argued that at the time it perfected its lien over the assets of IFS, the latter’s balance sheet as well as the other evidence presented to the court showed IFS to be solvent, so long as the multimillion dollar state court judgment was not included as a liability of the debtor in its full amount. Both parties agreed, however, that that if the state court judgment against IFS was added into the equation as a liability in its full face amount, IFS would have been hopelessly insolvent at the time of the contested transfer.

In the course of cross motions for summary judgment, the judgment creditor argued that because the state court judgment had been appealed and was not final under California state law, the bankruptcy court should consider it a contingent liability, which under established case law may be reduced for purposes of determining insolvency by a factor related to the likelihood that the judgment would actually have to be paid. *See, e.g., Covey v. Commercial Nat’l Bank of Peoria*, 960 F.2d 657, 659-61 (7th Cir. 1992). IFS, however, argued that the judgment should not be considered contingent because, on the date of the alleged preferential transfer, the judgment was enforceable and therefore should be construed as a liability in its full face amount, with no reductions.

The Bankruptcy Court’s Decision and the ‘Triggering Event Test’

After the matter was fully briefed, the bankruptcy court took the matter under submission and eventually issued a published opinion holding that the perfection of the judgment lien in favor of the judgment creditor constituted a preferential transfer and the lien could therefore be avoided. Crucial to the bankruptcy court’s ruling was its finding that the state court judgment should be included as a liability in its full face amount. S*ee Imagine Fulfillment Services, LLC vs. DC Media Capital, LLC*, 489 B.R. 136 (Bankr. C.D. Cal. 2013). Besides being a major win for IFS, which allowed it to later confirm its plan of reorganization and to successfully emerge as a reorganized debtor, the bankruptcy court’s published opinion is notable for its holding that a judgment on appeal was not a contingent liability for purposes of an insolvency analysis

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Aram Ordubegian is a Bankruptcy & Financial Restructuring partner and **M. Douglas Flahaut** is an associate at Arent Fox LLP in Los Angeles. The authors represented Imagine Fulfillment Services in the Chapter 11 case, and on appeal before the Bankruptcy Appellate Panel for the Ninth Circuit.

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under 11 U.S.C. § 547, even though: 1) the judgment was not final under California state law; and 2) the judgment debtor was optimistic that it would prevail on appeal and pay nothing on the judgment.

In ruling that a judgment on appeal is not "contingent," Judge Brand relied on the "triggering event" test from the *All Media* case published over 30 years ago. In *All Media*, a dispute regarding the meaning of "contingent" arose in the context of an involuntary petition. At the time of the *All Media* decision, 11 U.S.C. § 303 allowed creditors to file an involuntary petition against an alleged debtor so long as each creditor held a "claim … that is not contingent as to liability." To determine the appropriate definition of "contingent," the court in *All Media* first looked to the very broad definition of "claim" under the 11 U.S.C. § 101(4)(A). Then the court noted that the Code's definition of "claim" combined with the plain language of 11 U.S.C. § 303(b) made it clear that "there is a difference between a disputed claim, an unmatured claim, an unliquidated claim and a contingent claim. Otherwise, there would be no necessity to include the word 'contingent.'" *In re All Media Properties, Inc.*, 5 B.R. 126, 133 (Bankr. SD Texas 1980). Thus, the court concluded that:

> [C]laims are contingent as to liability if the debt is one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event which will trigger the liability of the debtor to the alleged creditor and if such triggering event or occurrence was one reasonably contemplated by the debtor and creditor at the time the event giving rise to the claim occurred. … On the other hand, if a legal obligation to pay arose at the time of the original relationship, but that obligation is subject to being avoided by some future event or occurrence, the claims is not contingent as to liability, although it may be disputed as to liability for various reasons.

In re All Media Properties, Inc., *supra* at 133.

Recognizing that courts in the Ninth Circuit had not specifically discussed the definition of a "contingent liability" in connection with a solvency analysis, Judge Brand concluded that because the 'triggering event test' has been widely applied to determine whether a debt it contingent in other contexts since *All Media*, the "triggering event test" should also control in an insolvency analysis under 11 U.S.C. § 547. Applying the "triggering event test" to the facts of IFS's avoidance action, the court concluded that because the breach of contract giving rise to the state court judgment in favor of the creditor (and entry of the judgment itself) occurred prior to the allegedly preferential transfer at issue with nothing else left to be decided by the state trial court, the judgment was not a contingent liability and IFS was therefore entitled to include the full face value of the judgment as a liability when determining whether or not IFS was insolvent at the time of the transfer.

With the full amount of the judgment on IFS's balance sheet in the liability column, the bankruptcy court found that IFS easily satisfied the required element of insolvency and, because all other elements of a preferential transfer had also been established, IFS was entitled to avoided the creditor's pre-petition judgment lien pursuant to 11 U.S.C. § 547.

The Bankruptcy Appellate Panel's Opinion

Not happy with the bankruptcy court's decision and recognizing that no other court in the Ninth Circuit had specifically applied the "triggering event test" to determine whether or not a judgment on appeal could be discounted for purposes of an insolvency analysis under Section 547, the judgment creditor appealed the bankruptcy court's decision to the Ninth Circuit Bankruptcy Appellate Panel. In a decision dated Aug. 6, 2014, the Panel affirmed the bankruptcy court's "well-reasoned … Memorandum Decision." *In re Imagine Fulfillment Services, LLC*, 2014 WL 3867531 *4 at fn. 8 (9th Cir. BAP Aug. 6, 2014).

In its decision, the Panel specifically held that because the events giving rise to the state court judgment occurred before the date of the allegedly preferential transfer, the liability was not contingent as a matter of law at the time of the transfer and therefore should be considered as a liability of the debtor in the full amount of the judgment for purposes of an insolvency analysis under 11 U.S.C. § 547. *Id.* at *6 (citing *In re Fostvedt*, 823 F.2d 305, 306 (9th Cir. 1987)) ("We see no reasoned or statutorily supported purpose to deviate, for insolvency determination purposes, from the definition of 'contingent debt' as one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event which will trigger the liability of the debtor to the alleged creditor.").

By affirming the bankruptcy court's use and application of the "triggering event test" in the context of the insolvency element of a preferential transfer, the Panel's recent ruling validated IFS's efforts to avoid the judgment lien and provides more clarity going forward with respect to when a bankruptcy court can estimate the probability of future liability and when a bankruptcy court must accept the entire amount the liability without any reduction.

Open Questions and Practice Pointers

The Imagine Fulfillment Services decisions leave little doubt as to the definition of a "contingent liability." However, some questions still remain when applying the definition to different facts and it seems that courts will in the future still look closely at the underlying facts specific to each particular case to determine whether or not a liability satisfies the definition of contingent.

For example, what if instead of having a judgment at the time of the transfer in question the creditor in the IFS case only had a pending lawsuit against the debtor for breach

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of contract. According to the "triggering event test," the liability in that scenario would still be a non-contingent liability because the breach of contract was alleged to have occurred years prior to the petition date. However, in a case where the liability is non-contingent under the "triggering events test," will courts still permit a debtor to claim as a liability the full amount of the claim made by the defendants in their breach of contract complaint before any judgment has been entered? Indeed, in that scenario, the judgment is not contingent, but it would certainly seem to be disputed.

Furthermore, what if a judgment had been entered, but enforcement of the judgment was stayed pending the state court appeal and the judgment creditor was not allowed to enforce its rights? In that scenario, again, the liability would certainly not be contingent under the 'triggering events test' since the events giving rise to liability all happened prior to entry of the judgment. However, if enforcement of the judgment was stayed would a court be more inclined to find the judgment to be disputed even though the trial court had already ruled?

Without discounting the uncertainties discussed above, knowing that the "triggering event test" is applicable to the insolvency analysis under 11 U.S.C § 547 should not be overlooked in future avoidance actions and will give lawyers representing debtors and trustees additional ammunition to potentially increase the liability side of a balance sheet in those cases where the insolvency of the debtor is disputed.

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Structured Dismissals

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been substantially consummated and the case is fully administered, the court enters a final decree closing the case. However, because Chapter 11 cases can be prolonged and costly, prepackaged or prenegotiated plans and expedited asset sales under section 363(b) of the Bankruptcy Code have been increasingly used as methods to short-circuit the process, minimize expenses and maximize creditor recoveries.

After a bankruptcy court approves a sale of substantially all of a Chapter 11 debtor's assets under section 363(b), a number of options are available to deal with the debtor's vestigial property and claims against the bankruptcy estate and to wind up the bankruptcy case. Namely, a debtor could propose and seek confirmation of a liquidating Chapter 11 plan, the case could be converted to a Chapter 7 liquidation or the case could be dismissed. The first two options commonly require significant time and administrative costs.

As a consequence, "structured dismissals" of Chapter 11 cases following a section 363(b) sale have become a popular exit strategy. A structured dismissal is a dismissal conditioned upon certain elements agreed to in advance by stakeholders and later approved by the court, as distinguished from an unconditional dismissal of the Chapter 11 case under section 1112(b) of the Bankruptcy Code. Structured dismissals typically have been granted in cases where: 1) the debtor has sold, with court authority, substantially all of its assets outside of a plan, but is either administratively insolvent or lacks sufficient liquidity to fund the plan confirmation process; or 2) after approval of a section 363(b) asset sale, the debtor could confirm a liquidating Chapter 11 plan, but costs associated with the confirmation process would likely eliminate or significantly reduce funds available for distribution to creditors.

Typical Terms of a Structured Dismissal

Some common provisions included in court orders approving structured dismissals include:

- Expedited procedures to resolve claims objections.
- Provisions specifying the manner and amount of distributions to creditors.
- Releases and exculpation provisions that might ordinarily be approved as part of a confirmed Chapter 11 plan.
- Senior creditor carve outs and "gifting" provisions, whereby, as a quid pro quo for a consensual structured dismissal, a senior secured lender or creditor group agrees to carve out a portion of its collateral from the sale proceeds and "gift" it to unsecured creditors.
- Provisions that, notwithstanding section 349 of the Bankruptcy Code (vacating certain bankruptcy court orders when a case is dismissed), prior bankruptcy court orders survive dismissal and the court retains jurisdiction to implement the structured-dismissal order, to resolve certain disputes and to adjudicate certain matters, such as professional fee applications.

Sources of Authority for Structured Dismissals

The Bankruptcy Code does not expressly authorize or contemplate structured dismissals. Even so, sections 1112(b), 305(a)(1) and 105(a) are commonly cited as predicates for the remedy.

Section 1112(b) authorizes a bankruptcy court to convert a Chapter 11 case to a Chapter 7 liquidation or to dismiss a Chapter 11 case, "whichever is in the best interests of creditors and the estate, for cause." "Cause" is defined in section 1112(b)

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Charles M. Oellermann is of counsel with Jones Day in the firm's Columbus, OH, office. **Mark G. Douglas**, a member of this newsletter's Board of Editors, is the Restructuring Practice Communications Coordinator and managing editor of the *Jones Day Business Restructuring Review*. The authors can be contacted, respectively, at coellermann@jonesday.com and mgdouglas@jonesday.com.

Stay Relief Denials

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The First Circuit ultimately relied upon several of its prior decisions, including *United States v. Fleet Bank* (*In re Calore Express Co.*), 288 F.3d 22 (1st Cir. 2002), in considering whether to adopt or reject the blanket rule. In *Calore*, for example, the First Circuit highlighted the caselaw underlying the blanket rule, but then performed an analysis which enabled it to properly scout for finality indicators. *Id*. at 34-35. Relying on *Calore*, among other cases, the First Circuit concluded that it was ultimately required to reject the blanket rule because, like the Third Circuit, it concluded that there could be orders denying stay relief that lack finality. *Pinpoint*, 761 F.3d at 185. Instead, the First Circuit adopted a more nuanced, fact-specific approach which, it concluded, will: 1) help courts avoid "unnecessary judging" when appeals have been superseded by events; and 2) encourage parties to fully consider finality issues before reflexively appealing from stay relief denials. *Id*.

Performing the more nuanced approach by scouting for finality telltales, the First Circuit concluded that the challenged order denying stay relief was in fact not final for the following reasons. First, the venue-related first-filed issue had yet to be adjudicated in the non-stayed Puerto Rico action. And, once adjudicated, Pinpoint can re-file its stay relief request, and the bankruptcy court will get to decide that issue, but on a better developed record. Second, Pinpoint was in a position to litigate everything it wanted to — both the first-filed and the contract issues — but not necessarily in its venue of choice. The First Circuit held that these reasons simply undercut Pinpoint's finality claim. *Id*. at 186.

The Dissent: Does the Majority Approach Value Abstraction Born of Theory Rather Than Pragmatism Born of Experience?

The decision of the First Circuit was not unanimous. While Judge William J. Kayatta agreed with his colleagues that Pinpoint's appeal did not provide a basis to reverse the bankruptcy court's lift stay denial, he dissented from the judgment of dismissal, holding, instead, that his colleagues should have decided the case by ruling on the merits rather than preferring to create a circuit split. *Id*. at 188. To be sure, Judge Kayatta, like his colleagues, is mindful not to join other circuits "simply to form a herd." That said, Judge Kayatta did emphasize the positive value of uniformity, "especially in setting federal bankruptcy law." *Id*. at 189.

Distilled to its essence, the dissent disagrees with the majority approach in the following respects. First, the majority's decision to reject the uniform approach of seven other circuits in favor of a more nuanced approach — which purports to preserve resources and inhibit unnecessary appeals — "values abstraction borne of theory rather than pragmatism borne of experience." *Id*. In support of this proposition, Judge Kayatta notes that even the Third Circuit — "the only federal court of appeals [until now] to so much as feint in the direction of a rule admitting of an exception" — has never encountered an order that fell within its hypothesized exception. *Id*. at 188. And, argues Judge Kayatta, the challenged order in this case should similarly fall outside the West exception for the simple reason that the Puerto Rico district court's decision on the first-filed issue has no relevance on the question of whether that court is entitled to decide that issue in the first place. *Id*. at 188. N. 23.

Second, the majority's insistence that the reallocation of the burden of changing the status quo — *i.e.*, in bankruptcy, the party seeking to alter the default position of the automatic stay bears the burden of doing so — justifies "a heightened degree of stinginess in allowing an appeal from a ruling preventing such a change" is conceptually erroneous. As the dissent notes, appeals of orders denying requests for injunctive relief outside of bankruptcy are routinely allowed and so, Judge Kayatta concludes, the question of who has the burden of altering the status quo has no relevance to the question of appealability. *Id*. at 189.

Third, the majority should have decided the case on its merits rather than creating "an idiosyncratic exception to the norm." Simply put: The relevant dispute was not about which court should consider the merits of the case; rather, it was about which court will decide that question. That dispute, argues Judge Kayatta, was decided by the bankruptcy court against Pinpoint. *Id*. at 189-90.

Fourth, the majority's approach fails to satisfy judicial economy, the very purpose of the finality rule as articulated by Judge Ralph K. Winter in *Sonnax Indus., Inc. v. Tri Component Products. Corp.* (*In re Sonnax Industries, Inc.*), 907 F.2d 1280 (2d Cir. 1990). As the *Sonnax* court noted, "the jurisdictional ruling will necessarily require a full briefing of all issues and consume as much judicial resources as an appeal." *Id*. at 1285. And that, argues Judge Kayatta, is precisely what happened in the case at bar. *Pinpoint*, 761 F.3d at 190.

For these reasons, Judge Kayatta would have considered the merits of Pinpoint's appeal rather than dismissing the appeal for lack of jurisdiction, and would have ultimately rejected the appeal on its merits because the bankruptcy court's order: 1) reasonably balanced competing claims of harm; 2) protected the estate assets against potential waste by preventing a race to the courthouse; and 3) did not deprive Pinpoint of its opportunity to be heard. *Id*. at 191.

The Nascent Sub-Sub Specialty of Appellate Jurisdiction over Bankruptcy Court Orders Denying Stay Relief

What are some of the takeaway lessons from this decision? Well, the First Circuit rejected the blanket rule that all stay relief denials are final and appealable as of right, a decision that rejects the uniform approach of seven other circuits thereby creating a circuit split. That's noteworthy, and that rejection certainly injects a measure of uncertainty going forward. And, at least according to Judge

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(4) to include, among other things, "substantial or continuing loss to or diminution of the estate and the absence of a reasonable likelihood of rehabilitation" and "inability to effectuate substantial consummation of a confirmed plan." Dismissal or conversion of a Chapter 11 case under section 1112(b) is a two-step process. First, the court must determine whether "cause" exists for dismissal or conversion. Second, the court must determine whether dismissal or conversion of the case is in the best interests of creditors and the estate.

Section 305(a)(1) of the Bankruptcy Code provides that a bankruptcy court can dismiss or suspend all proceedings in a bankruptcy case under any Chapter if "the interests of creditors and the debtor would be better served by such dismissal or suspension." Section 305(a)(1) has traditionally been used to dismiss involuntary cases where recalcitrant creditors involved in an out-of-court restructuring file an involuntary bankruptcy petition to extract more favorable treatment from the debtor. However, the provision has also been applied to dismiss voluntary cases, albeit on a more limited basis. Because an order dismissing a case under section 305(a) may be reviewed on appeal only by a district court or a bankruptcy appellate panel, and not a court of appeals or the U.S. Supreme Court (*see* 11 U.S.C. § 305(c)), section 305(a) dismissal is an "extraordinary remedy." *See In re Kennedy*, 504 B.R. 815, 828 (Bankr. S.D. Miss. 2014); *see also In re Gelb*, 2013 BL 166941, *6 n.13 (B.A.P. 9th Cir. Mar. 29, 2013) (dismissal or suspension order under section 305(a) reviewable by bankruptcy appellate panel).

Section 105(a) of the Bankruptcy Code provides that a bankruptcy court "may issue any order, process, or judgment that is necessary or appropriate to carry of the provisions" of the Bankruptcy Code. However, section 105(a) "does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code." *Law v. Siegel*, 134 S. Ct. 1188, 1194 (2014).

Most structured dismissals are consensual. The few reported and unreported decisions on the issue reflect that some courts have been willing to order structured dismissals due to the consent of stakeholders and because a structured dismissal is a more expeditious, cost-effective and beneficial means of closing a Chapter 11 case. *See, e.g., In re Felda Plantation, LLC*, 2012 WL 1965964 (Bankr. N.D. Fla. May 29, 2012); *Omaha Standing Bear Pointe, LLC v. REW Materials* (*In re Omaha Standing Bear Pointe, LLC*), 2011 BL 69859 (Bankr. D. Neb. Mar. 17, 2011); *see also In re Fleurantin*, 420 Fed. Appx. 194, 2011 BL 80633 (3d Cir. Mar. 28, 2011) (Chapter 7 case structured dismissal). *But see In re Strategic Labor, Inc.*, 467 B.R. 11, 11 and n.10 (Bankr. D. Mass. 2012).

Regardless of stakeholder consent, the U.S. Trustee frequently objects to structured dismissals. Among other things, the U.S. Trustee has argued that structured dismissals: 1) distribute assets without adhering to statutory priorities; 2) include improper and overbroad releases and exculpation clauses; 3) violate the express requirements of section 349(b); 4) may constitute "sub rosa" Chapter 11 plans that seek to circumvent plan confirmation requirements and creditor protections; 5) improperly provide for retention of the bankruptcy court's jurisdiction; and 6) fail to reinstate the remedies of creditors under applicable non-bankruptcy law. *See* Nan Roberts Eitel, T. Patrick Tinker & Lisa L. Lambert, "Structured Dismissals, or Cases Dismissed Outside of Code's Structure?" 30 *Am. Bankr. Inst. J.* 20 (March 2011).

A RECENT CASE STUDY: *IN RE BUFFET PARTNERS*

Buffet Partners, L.P. and its affiliates (collectively, "Buffet") owned and operated Furr's — a buffet-style restaurant chain that, at its height in 2009, had 50 locations primarily in the southwest U.S. Buffet filed for Chapter 11 protection in the Northern District of Texas on Feb. 14, 2014. Shortly afterward, Buffet sought court authority to sell substantially all of its assets under section 363(b) to stalking-horse bidder and secured lender Chatham Credit Management III, LLC ("Chatham").

The official committee of unsecured creditors performed substantial due diligence regarding Buffet's business, the liens and claims against Buffet's assets and estate, and various restructuring alternatives. After completing due diligence, the committee and Buffet jointly filed a motion for approval of a settlement that would resolve the open issues in the case, pay allowed administrative and priority claims in full, and provide a meaningful recovery for general unsecured creditors.

In particular, under the proposed settlement: 1) Buffet's assets would be sold to Chatham or any qualified overbidder; 2) the purchaser would pay $500,000 into a trust created for the benefit of unsecured creditors; 3) the purchaser would pay administrative expenses, provided that the fees and expenses of professionals retained by Buffet and the committee would be capped, respectively, at $600,000 and $250,000; 4) the committee would support entry of a final cash collateral order in the case; 5) Chatham would waive any unsecured deficiency claim; and 6) Chatham, Buffet and the committee would exchange releases.

The court approved the settlement on April 16, 2014. Chatham's $25 million bid prevailed at an auction conducted the following week. On June 19, 2014, Buffet and the committee jointly moved to dismiss the Chapter 11 cases. In their motion, they proposed that the Buffet cases be dismissed upon certification that: 1) the committee has completed the claims reconciliation process; 2) all U.S. Trustee fees have been paid; 3) funds have been distributed to unsecured creditors; and 4) the court has ruled on professional fee applications.

In addition, the proposed dismissal order provided that: 1) any

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Structured Dismissals

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orders entered by the court during the case would remain in force, notwithstanding section 349; 2) Buffet was authorized to take appropriate action to wind up and dissolve as a corporate entity without further approval by the board of directors, shareholders or any other entity; and 3) the court retained jurisdiction to review fee applications and to resolve disputes regarding any orders entered during the case (including the dismissal order).

Only the U.S. Trustee objected to the structured dismissal motion, arguing that, after approval of the sale to Chatham, the case should be converted to Chapter 7 or, in the alternative, Buffet should seek confirmation of a Chapter 11 plan.

The Bankruptcy Court's Ruling

The bankruptcy court approved the structured dismissal as being in the best interests of creditors and the estate. The court acknowledged that "[n]ot much law, statutory or otherwise, exists regarding structured dismissals of this type." Even so, it reasoned that both alternatives proposed by the U.S. Trustee would add significant and unnecessary time and expense. The court also emphasized that "the economic value of the Debtor in this case will be served by dismissing the case, rather than converting it" and that the parties do not wish "to go through the time and expense of a plan, which will cause the pool of money left to be greatly diminished." Given appropriate notice and a process that does not "illegally or unfairly trample on the rights of parties," the court concluded, the structured dismissal should be approved.

However, the court cautioned that "parties do not have carte blanche to enter into any settlement they choose." Among other things, a proposed settlement must comply with the Bankruptcy Code's distribution rules and cannot "short circuit" the Chapter 11 plan confirmation requirements by establishing the terms of a sub rosa plan in connection with a section 363(b) asset sale. "While the proposed dismissal does have certain plan aspects," the court wrote, "it does not cut off the rights of any parties without giving them the chance to voice an objection and it does not violate the absolute priority rule." Finally, the court characterized as "worthy of consideration," albeit not "outcome determinative," the fact that "not one party with an economic stake in the case has objected to the dismissal in this manner."

The court concluded its ruling by unequivocally endorsing a structured dismissal in an appropriate case:

> 11 U.S.C. §§ 1112(b) and 105(a) provide this court with the requisite authority to fashion the dismissal order that the parties seek. Although this process is not explicitly spelled out in § 1112(b), it is clearly within the sphere of authority Congress intended to grant to bankruptcy courts in the context of dismissing Chapter 11 cases. This dismissal, which all of the economically-interested parties support, is in the best interests of the creditors and the estate. For the following reasons, the proposed dismissal is hereby GRANTED.

Outlook

Buffet Partners does not signal a significant departure from existing bankruptcy jurisprudence or practice — structured dismissals are becoming more commonplace as a way to minimize costs and maximize creditor recoveries. Still, the decision is important because it is one of the few published rulings on the issue. Moreover, the court expressly identifies the source of its authority — sections 1112(b) and 105(a) — to approve a structured dismissal. As such, *Buffet Partners* may be viewed as a positive development both for debtors considering the structured dismissal as a possible strategy for exiting from Chapter 11 and for bankruptcy courts contemplating whether they have authority to order a structured dismissal and under what circumstances.

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Stay Relief Denials

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Kayatta, the majority approach has transformed "what was until today a non-issue into fodder for briefing and analysis in the nascent sub-sub specialty of appellate jurisdiction over bankruptcy court orders denying stay relief." *Id*. That's also noteworthy.

Regarding Judge Kayatta's final comment that the majority approach created "a new and entirely unnecessary precursor battleground that will add expense and delay while likely never altering the practical outcome of even a single case," I guess only time will tell. I think practitioners should take some comfort in the fact that the facts underlying the First Circuit's decision were unique in that the prepetition litigation could proceed notwithstanding the stay relief denial. Query whether the First Circuit would have ruled differently had the prepetition litigation not been pending in two courts, where the stay relief denial would have resulted in the continued stay of the prepetition litigation.

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