Benchnotes

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Due-on-Sale Clause Not Required for § 1111(b); Any One Class of Votes Will Do for Cramdown

The Ninth Circuit Court of Appeals recently issued an opinion in *Transwest Resort Prop. Inc.*[1] that is sure to aid creative debtors in crafting successful cramdown reorganization plans in the Ninth Circuit for years to come. In *Transwest*, the bankruptcy court confirmed a cramdown of the debtors' joint reorganization plan over the objections of an undersecured creditor that the plan (1) improperly interfered with its rights as an undersecured creditor electing treatment under U.S.C. § 1111(b) by excluding a due-on-sale requirement during the first 10 years of the proposed plan, and (2) cannot be confirmed under 11 U.S.C. § 1129(a)(10) without accepting impaired creditors for each of the plan's joint debtors. In a case of first impression on both issues, the Ninth Circuit affirmed plan confirmation.

Section 1111(b)

The Ninth Circuit acknowledged that § 1111(b) allows a creditor to elect to have its claim treated as fully secured and that the effect of such an election is that the undersecured creditor obtains certain benefits reserved for secured, but not unsecured, creditors.[2] However, the Ninth Circuit rejected the creditor's assertion that without the requirement of a due-on-sale provision, the benefits intended by Congress to be preserved under § 1111(b) are improperly diminished.

The Ninth Circuit held that the objection was not supported by the plain text of § 1111(b), or more broadly in confirmation requirements included in 11 U.S.C. § 1123. Further, not requiring a due-on-sale clause is consistent with the fair-and-equitable provisions of 11 U.S.C. § 1129(b)(2)(A)(i)(I), which "expressly allows a debtor to sell collateral to another entity so long as the creditor retains its lien."[3] If Congress intended differently, it would have crafted the statute differently.

Section 1129(a)(10)

Section 1129(a)(10) of the Bankruptcy Code requires that "[i]f a class of claims is impaired under the plan, at least one of the claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider."[4] The creditor's objection to the *Transwest* plan was that § 1129(a)(10) should be read to require that a plan be accepted on a "per-debtor" as opposed to a "per-plan" basis. In other words, a debtor should not be allowed to propose a jointly administered plan for the debtor's own convenience while also sidestepping the requirements of § 1129(a)(10) that could not otherwise be satisfied if each debtor had proposed an individual plan.

As it did in considering the creditor's § 1111(b) objection, the Ninth Circuit focused its analysis of § 1129(a)(10) on the plain text of the statute. According to the Ninth Circuit, the plain language of the statute supports a "per-plan" interpretation, something that Congress could have easily drafted around if that was not its intent.[5] As noted by the Ninth Circuit, only the U.S. Bankruptcy Court for the District of Delaware has elected to adopt the "per-debtor" interpretation.[6] The Delaware bankruptcy court did so in reliance on the 11 U.S.C. § 102(7) rule of construction, which indicates that a singular reference in the Bankruptcy Code includes the plural. According to the Delaware bankruptcy court, this construction supports that § 1129(a)(10) requires "per debtor" approval for cramdown of a joint chapter 11 plan.[7] The Ninth Circuit flat-out rejected the Delaware interpretation, and in so doing gave chapter 11 debtors a helping hand in confirming jointly administered plans over the objections of their major creditor constituencies.[8]

For further analysis of the *Transwest* case, see the article on p. 30.

Second Circuit Broadly Interprets § 1334(b) Related-to Jurisdiction

In *SPV Osus Ltd. v. UBS AG (Luxembourg) SA*,[9] the plaintiff filed a suit in New York state court against UBS AG and certain of its foreign affiliates, alleging that they had aided and abetted the frauds perpetrated by Bernie Madoff and his affiliated entities prior to their Ponzi scheme being revealed and their ultimate bankruptcy filings.[10] The defendants removed the complaint to the U.S. District Court for the Southern District of New York, invoking the district court's jurisdiction under the "related-to" provision of 11 U.S.C. § 1334(b).[11] On the plaintiff's motion for remand of the action to state court, the defendants argued that the action should not be remanded because the matter was related to the *Madoff* bankruptcy cases. The Second Circuit was asked to review the district court's determination that it had related-to jurisdiction under § 1334(b). The Second Circuit affirmed.

1 --- F.3d ---, 2018 WL 615431 (9th Cir. 2018).
2 *Id.* at 5.
3 *Id.* at *3.
4 11 U.S.C. § 1129(a)(10).
5 *Transwest* at *4.
6 *Id.* at 5.
7 *See In re Tribune Co.*, 464 B.R. 126 (Bankr. D. Del. 2011).
8 *Transwest* at 5.
9 --- F.3d ---, 2018 WL 798291 (2d Cir. 2018).
10 *Id.* at *2.
11 *Id.*

In affirming, the Second Circuit recited its own prior precedent in which the Second Circuit has ruled that related-to jurisdiction broadly encompasses an action that "might have any conceivable effect on the bankruptcy estate."[12] The Court further held that although the claims in the action did not directly implicate the bankruptcy cases, "courts have generally found jurisdiction where there is a reasonable legal basis for the claim," even if such claims are contingent in nature.[13]

So, what did the Second Circuit find to be a reasonable legal basis for a claim of related-to jurisdiction? According to the Second Circuit, the defendants held a putative contribution claim against the Madoff debtors for any liabilities arising out of the lawsuit, despite the claims bar date having passed and there being insufficient funds remaining in the Madoff estates to make any distributions on account of the defendants' claims. There was a possibility that there could be a late claim filed by the defendants, and the mere specter of such a proceeding (regardless of the outcome) was sufficient to implicate related-to jurisdiction.[14]

Miscellaneous

• *Zazzali v. U.S. (In re DBSI Inc.)*, 869 F.3d 1004 (9th Cir. 2017) (liquidation trustee brought fraudulent transfer action against IRS under state law and § 544(b) to recover $17 million in payments that debtor (S-corporation) made on behalf of its shareholders; IRS moved for summary judgment on theory that any creditor would have been barred from suing government outside of bankruptcy due to sovereign immunity; creating a circuit split, Ninth Circuit held that waiver of sovereign immunity contained in § 106(a)(1) enables trustee to bring a derivative state law fraudulent-transfer claim against IRS under § 544(b), even though unsecured creditor could not);

• *Sheedy v. Bankowski (In re Sheedy)*, 875 F.3d 740 (1st Cir. 2017) (counsel's second job as church music director did not excuse late-filed notice of appeal; "The district court found that [the debtor's] counsel knew about his responsibilities around Easter, well in advance of the appeal deadline. Therefore, counsel's explanation for the delay 'seem[ed] to amount to mere inadvertence,' and did not constitute excusable neglect'.... While we do not doubt the demanding nature of counsel's musical duties during this time of year, the religious holidays occur annually and their dates were known well in advance of the two-week filing deadline. Counsel could and should have planned his legal responsibilities accordingly.");

• *In re Cgg SA*, 2017 Bankr. LEXIS 4535 (Bankr. S.D.N.Y. Dec. 21, 2017) (bankruptcy court recognized French foreign proceedings and granted relief under § 1521(a) by enforcing French court's "Sanctioning Order" as "necessary to ensure that the Financing Restructuring contemplated by the Safeguard Plan and the confirmed Chapter 11 plan can be implemented..."; bankruptcy court further held that securities issued under Safeguard Plan did not require federal or state registration, because issuance of such securities were exempt under § 1145(a)(1));

• *In re Fresh-G Rest. Intermediate Holding LLC*, 2017 Bankr. LEXIS 4326 (Bankr. D. Del. Dec. 20, 2017) (purchaser of restaurants was allowed to exercise lease-renewal option under California law, despite payment defaults that existed at time of renewal; "Here, the Landlord and the Purchaser already bargained in good faith around the adequate assurance objections to the assumption and assignment of the Lease.... To prevent the renewal, which was not in the initial objection of the Landlord and argued after the settlement of the adequate assurance objection and post-petition cures, would provide the Landlord with a windfall as it attempts to enforce lease provisions in selective fashion and in strategic timing"; court further held that § 365(d) did not pre-empt California's anti-forfeiture law);

• *Slovak Republic v. Loveridge (In re EuroGas Inc.)*, 576 B.R. 648 (B.A.P. 10th Cir. 2017) (even though Slovak Republic was creditor in debtor's chapter 7 case, court found that trustee's settlement with estate's largest unsecured creditor resulted in significant increase in distribution to unsecured creditors; thus, only logical reason for Slovak Republic's appeal of settlement order was to improve its position in unrelated arbitration proceeding pending in Paris, which appellate panel held to be "insufficient to confer standing to appeal the Decision" or to establish appellate jurisdiction);

• *Physiotherapy Holdings v. Water St. Healthcare*, 2017 U.S. Dist. LEXIS 209723 (D. Del. Dec. 21, 2017) (after bankruptcy court dismissed some — but not all — fraudulent-transfer counts against defendants, defendants moved for leave to appeal, arguing that § 546(e) should have precluded liquidating trustee from pursuing all fraudulent claims, not just those asserted on behalf of debtor and its bankruptcy estate; district court denied motion for leave, finding no controlling question of law based on bankruptcy court's well-reasoned and specific analysis of facts; by its express terms, § 546(e) was only intended to protect market intermediaries, not corporate insiders like defendants; district court thus concluded that "systemic risk concerns were not at issue");

• *In re SunEdison Inc.*, 576 B.R. 453 (Bankr. S.D.N.Y. 2017) (after confirming debtors' plan, bankruptcy court concluded that third-party releases contained within plan were not binding on non-voting creditors who debtors said were "deemed to consent" to such releases by their silence; in rejecting this argument, bankruptcy court applied contract law and explained that silence could only be construed as consent if non-voting creditors had duty to speak, or if their silence was somehow misleading; here, debtors failed to identify source of any such duty to speak (*e.g.*, plan did not provide higher payout to releasing creditors); thus, mere references to conspicuous language in disclosure statements and ballots were unpersuasive — nothing else in plan demonstrated why creditors should have known that their silence would be construed as consent);

• *In re Mejia*, 576 B.R. 464 (Bankr. S.D.N.Y. 2017) (even though trustee had no objection to debtor's proposed sale of certain property, court would not approve sale under § 363(b); estate indisputably had no equity in property over and above debtor's claimed homestead exemption, but property had not been abandoned under

12 *Id.* at *3 (citing *Parmalat Capital Fin. Ltd. v. Bank of Am. Corp.*, 639 F.3d 572 (2d Cir. 2011)).
13 *Id.* at *4 (citations omitted).
14 *Id.* at *5.

continued on page 110

one of three methods provided under § 554: by notice of trustee, on motion of party in interest or upon closing of case; trustee's notice of no distribution following § 341 meeting was insufficient to abandon property to allow sale outside of bankruptcy, and only trustee or debtor in possession may sell property under § 363(b));

• *Hiner v. Koukhtiev (In re Koukhtiev)*, 576 B.R. 107 (Bankr. S.D. Tex. 2017) (court held that debtor acted willfully and maliciously to injure plaintiff by, *inter alia*, refusing to provide source code to software that debtor developed for plaintiff's company and selling unauthorized copies of software under assumed name; damages awarded by state court were held to be nondischargeable debts under § 523(a)(6));

• *In re Tempnology LLC*, 879 F.3d 389 (1st Cir. 2018) (First Circuit Court of Appeals aligned itself with Fourth Circuit regarding continued use of patents and trademarks by licensee to debtor-rejected licensing agreement; after a lengthy discussion of § 365, First Circuit determined that licensee of patents may elect to continue use of patents post-rejection pursuant to 11 U.S.C. § 365(n) but may not continue to use accompanying trademark; decision splits First and Fourth Circuits from Seventh Circuit, which determined that trademark use could continue post-rejection in *Sunbeam Products, Inc. v. Chicago American Manufacturing LLC*, 686 F.3d 372 (7th Cir. 2012));

• *In re Philadelphia Entm't & Dev. Partners*, 879 F.3d 492 (3d Cir. 2018) (Third Circuit Court of Appeals ruled that *Rooker-Feldman* doctrine did not preclude trustee from pursuing fraudulent-transfer action against state gaming board for its pre-petition revocation of debtor's gaming license; court of appeals held that fraudulent-transfer action is a separate and distinct cause of action from decision to revoke license; because trustee was not seeking to invalidate the revocation, *Rooker-Feldman* doctrine did not mandate dismissal of trustee's avoidance claims);

• *In re JFK Capital Holdings LLC*, --- F.3d ---, 2018 WL 564371 (5th Cir. 2018) (Fifth Circuit Court of Appeals joined Seventh Circuit in holding that trustee fees calculated pursuant to 11 U.S.C. § 326(a) are presumptively reasonable and only subject to adjustment in unusual circumstances; Fifth Circuit's decision was consistent with Ninth Circuit BAP's decision in *In re Salgad-Nava*, 473 B.R. 911 (B.A.P. 9th Cir. 2012));

• *Dahlin v. Lyondell Chem. Co.*, --- F.3d ---, 2018 WL 563985 (8th Cir. 2018) (Eighth Circuit Court of Appeals reversed judgment entered against Lyondell Chemical for liabilities related to toxic chemical exposure years before Lyondell reorganized in chapter 11 and discharged its pre-petition liabilities; at issue was whether claim could be asserted by plaintiff that had not been provided notice of chapter 11 proceeding; court of appeals found that district court had applied incorrect standard; court of appeals said that debtors cannot be expected to "anticipate speculative suits based on lengthy chains of causation" and instead must only provide notice to "reasonably ascertainable" plaintiffs (*id.* at *6); decision aligns Eighth Circuit with Third Circuit's decision in *Chemtron Corp. v. Jones*, 72 F.3d 341 (3d Cir. 1995)); and

• *In re Beem*, --- Fed. App'x. ---, 2018 WL 718608 (11th Cir. 2018) (Eleventh Circuit held that creditor's failure to timely file dischargeability complaint was not fatal because creditor's prior filing of motion containing requisite elements for asserting dischargeability complaint as otherwise required under Bankruptcy Rule 7008 was timely, and subsequent untimely filing of formal dischargeability complaint related back to previously timely filed motion under application of Bankruptcy Rule 7015). abi