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Baird & Jackson's Bankruptcy Cases, Problems, and Materials
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2023 Cumulative Update Letter

The Fifth Edition of the Baird & Jackson Bankruptcy casebook was published in the summer of 2020. The Sixth Edition is currently in draft and will be available for adoption in Spring Semester 2024. In the meantime, below are brief descriptions of some bankruptcy developments over the last three years. The selection is *not* intended to be comprehensive, but instead reflects highlights that we believe may be of interest to faculty and students who use our book.

Some recent legislative highlights:

- Bankruptcy casebooks, including ours, refer to statutory dollar amounts applicable at the time of publication. It is important to keep in mind, though, that these dollar amounts tend to increase over time. For example, the Bankruptcy Threshold Adjustment and Technical Corrections Act of 2022 raised the eligibility limits for small-business debtors under Subchapter V of Chapter 11 and for Chapter 13 debtors. Now small businesses are potentially eligible for Subchapter V if they have no more than $7.5 million in noncontingent liquidated debt to unaffiliated creditors while an individual is potentially eligible for Chapter 13 if she has less than $2,750,000 in noncontingent liquidated debt.

- Prompted by the controversial bankruptcies of firms like Purdue Pharma, the Boy Scouts, and U.S.A. Gymnastics, the Nondebtor Release Prohibition Act of 2021 would largely prohibit the release in bankruptcy of claims against nondebtors. The prospect of such releases, often opposed even under current law, is thought to induce approval of bankruptcy settlements by claimants who might otherwise seek greater recovery in a debtor's bankruptcy and then pursue any shortfall against nondebtor defendants. Because this legislation has not been enacted, questions over a bankruptcy court's authority to grant nondebtor third-party releases has generated heated litigation. As described below, the issue under current law may be resolved this spring by the Supreme court, which has granted cert in the Purdue Pharma case.

Some recent caselaw highlights:

- In City of Chicago v. Fulton, 141 S.Ct. 585 (2021), the Supreme Court held that the mere retention of property in which a debtor has an interest does not constitute an act to exercise control over property of the estate in violation of the Bankruptcy Code's automatic stay as provided by §362. In the case, the City of Chicago had impounded debtors' vehicles prior to the debtors' bankruptcy petitions. The Court ruled that retention of the vehicles, even after the debtors requested their return, could not subject the city to sanctions in the absence of a turnover order under Bankruptcy Code §542. Significantly, this means that debtors now may not even temporarily gain possession of property exempt from turnover.

- In re Weinstein Company Holdings LLC, 997 F.3d 497 (3rd Cir. 2021) addresses the determination of what qualifies as an executory contract under the Bankruptcy Code. The debtor film company was in breach of contract to the producer of the movie *Silver Linings Playbook*. The debtor attempted to sell its distribution rights under the contract and the producer objected on the ground that any such sale required the debtor first to assume the contract under Bankruptcy Code §365, which in turn conditions assumption on the debtor's cure of any contract default. The debtor argued that the contract was no longer executory and that §365 was, therefore, inapplicable. The court ruled that under state law the producer's only remaining contractual obligation was so insubstantial as to make it impossible for the producer even hypothetically to be in material breach. Consequently, held the court, with a substantial obligation owed only by the debtor, the contract was not executory and the debtor was free to sell its rights under the contract even if the debtor did not cure its breach. This result, though ironic, is not outside the mainstream. Of interest, though, is the court's dictum that parties can, but did not here, "contract around a state's default contract rule regarding substantial performance [by expressly declaring any obligation substantial], and by doing so they can also override the Bankruptcy Code's intended protections for the debtor."

- The case of In re Nuverra Environmental Solutions, Inc., 834 Fed. Appx. 729 (3rd Cir. 2021) dismissed on appeal an unfair discrimination objection to a reorganization plan. The dismissal was not on the merits of the objection, or because the appeal was untimely or the like, but because the reorganization plan had been put into effect prior to the appeal. The court held that the appeal was equitably moot in that the remedy sought, even if otherwise deserved, would "fatally scramble" the reorganization. In her concurrence on other grounds, Judge Krause vehemently decried the very notion of equitable mootness, which can, as a practical matter, remove even important issues of bankruptcy law from appellate review. Judge Krause observed, for instance, that the majority used equitable mootness to duck "open issues around the nature of unfair discrimination under § 1129(b)(1): Does the Supreme Court's decision in *Czyzewski v. Jevic Holding* foreclose preferential treatment of a sub-class through horizontal gifting? Is the unfair discrimination test focused on a plan's results or the process that produced those results? And what are the limits on a plan's ability to divide creditors into classes?" The Supreme Court denied certiorari in the case, so these questions remain unanswered.

- Generation Resources Holding Co., LLC, 964 F.3d 958 (10th Cir. 2020) is another controversial appellate court decision. There, the court held that Bankruptcy Code §550 does not permit a debtor to recover the proceeds of fraudulently conveyed property from anyone other than a transferee of that property. Under this interpretation of §550, if a debtor fraudulently transfers his horse to his sister, who then sells the horse for cash and gives the money to a cousin, the cousin is not deemed an "immediate or mediate transferee" of fraudulently transferred property and is not subject to a §550 collection action. The hyper-textual basis for this opinion has already been subject to pushback as inconsistent with the fundamental purposes of fraudulent conveyance law. See In re Giant Gray, Inc., 2020 WL 6226298 (Bankr. S.D. Tex.).

- In re Purdue Pharma LP, 69 F.4th 45 (2nd Cir. 2023) overturned a district court opinion and affirmed the bankruptcy court's nonconsensual third-party releases of the debtor's shareholders and officers—the Sackler family—from claims by victims of the debtor's opioid pharmaceutical products. The Second Circuit's endorsement of the releases focused on the approval by a large majority of the affected claimants as well as on the perceived difficulty the claimants would face outside bankruptcy in collecting from the Sacklers as much money as the family voluntarily offered to the bankruptcy estate as a condition of the releases. The court held that the "extraordinary remedy" of nonconsensual third-party releases "is based on bankruptcy courts' in rem jurisdiction over the property of the debtor." But the Second Circuit will not have the last word on the matter because the Supreme Court stayed enforcement of the opinion and granted certiorari in the case. Presumably it will now settle the circuit-split on the permissibility of nonconsensual third-party releases in bankruptcy.

- In re LTL Management, LLC, 64 F.4th 84 (3rd Cir. 2023) addresses what is known as a divisive merger followed by a bankruptcy petition (sometimes called the Texas Two-Step). JJCI, a subsidiary of healthcare giant Johnson & Johnson, faced tort liability for injury plaintiffs say they suffered from JJCI's talc baby powder product. In response to the looming talc liability, and as permitted under state law, the parent corporation divided JJCI into a new operating company and LTL Management. The latter received a specified funding obligation from other members of the corporate affiliate and was saddled with all JJCI's talc liability. LTL then filed for bankruptcy. The bankruptcy court found that LTL's talc liability was potentially enormous and observed that the LTL funding agreement amounted to a fair-value exchange for JJCI's assets. The court rejected arguments that the described machinations served no legitimate bankruptcy purpose and declined to dismiss the case. The Third

Circuit reversed. It concluded that LTL's potential talc liability was exaggerated and held that because LTL was, thus, not in financial distress the bankruptcy filing was a needless, bad faith attempt to move the forum for talc litigation from state court to bankruptcy court where the debtor believed it would fare better as a defendant.

- After the dismissal of its bankruptcy case, LTL filed a new bankruptcy petition that included an altered funding agreement and a newly proposed settlement of significant talc liability. Citing the Third Circuit's opinion in the original case, the bankruptcy court dismissed this case as well. In re LTL Management, LLC, 2023 WL 4851759 (Bankr. D. NJ 2023).

- A kindred case in which a court blocked what it saw as an illegitimate use of the bankruptcy process is In re National Rifle Association of America, 628 B.R. 262 (Bankr. N.D. Tex. 2021). In that case, the NY State Attorney General sought to dissolve the debtor for violation of state law. The NRA sought bankruptcy protection, but the case was dismissed "as not having been filed in good faith both because it was filed to gain an unfair litigation advantage and because it was filed to avoid a state regulatory scheme."

Hope this is helpful. Please do not hesitate to be in touch if any of us can answer any questions or be of any other assistance.

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