2021 Commercial Law Panel: Selected Cases of Interest from Outside the Eleventh Circuit

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I. LIMITS ON NOTICE BY PUBLICATION

A. *Alliance WOR Props., LLC v. Illinois Methane, LLC (In re HNRC Dissolution Co.)*, --- F.4th ---, 2021 WL 2910528 (6th Cir. July 12, 2021):

This case examined the extent to which a debtor may rely on providing notice by publication to parties with known, present, and vested interests in real property. In 1998, Old Ben Coal Company ("Old Ben") acquired a block of coal reserves and leases across several Illinois counties. *Id.* at *1. Because it decided not to actively mine coal, Old Ben conveyed its rights to "all of the methane gas" in its coal estates to Illinois Methane, LLC for the purchase price of $2.6 million. *Id.* The deed was recorded with the county treasurer. *Id.*

As part of that transfer, Old Ben also agreed to a "delay rental obligation," which provided that if Old Ben applied to open a new mine, expand an existing mine, or reopen an inactive mine, it would notify Illinois Methane of its application and would not thereafter grant any additional leases or contracts for the exploration or production of methane gas in the area. *Id.* If there were no outstanding leases of methane gas or permits issued to drill new wells in Old Ben's application area, then Old Ben was to pay Illinois Methane an adjusted delay rental, which varied with the number of acres that were unavailable to Illinois Methane and the current price of light sweet crude oil. *Id.* at *1-2. The agreement further provided that if either party conveyed surface, coal, or methane gas rights, the covenants encapsulated by the purchase documents ran with the land. *Id.* at *2. Shortly after the deed was executed, Old Ben and its parent company merged into a new company called AEI Resources. *Id.*

AEI Resources and its affiliates filed for Chapter 11 protection in 2002. *Id.* In that bankruptcy proceeding, the debtors moved for approval of a section 363 sale, part of which included the sale of Old Ben's coal reserves. *Id.* The debtors published notice of the bankruptcy sale in several regional and national newspapers, but they did not attempt to provide direct notice to Illinois Methane. *Id.*

The bankruptcy court approved the section 363 sale and found that the debtors' publication by notice was sufficient and that "no other or further notice [was] required." *Id.* The bankruptcy court further provided that the sale was to be free and clear, with the exception of certain permitted liens, and that all entities that held interests in the debtors' property were "permanently barred from commencing . . . any action or other proceeding of any kind with respect to such . . . interest." *Id.* As part of the section 363 sale, Old Ben conveyed its coal reserves to Lexington Coal Company, a buyer who is in privity with the appellant, Alliance WOR Properties, LLC ("Alliance"). *Id.* at *1-2.

Alliance's predecessor-in-interest applied for a permit to mine coal, and Illinois Methane sought to collect approximately $11 million due under its delay rental obligation from Alliance (now the owner of the Old Ben coal reserves) in state court. *Id.* at *1. Alliance filed a motion to enjoin the state court lawsuit in the bankruptcy proceeding, arguing that Old Ben's "free and clear" sale extinguished Illinois Methane's interest in the land. *Id.* The bankruptcy court held that Old Ben's publication by notice was insufficient for purposes of due process to extinguish Illinois Methane's known property interest. *Id.* The bankruptcy court ruled that the section 363 sale had

not erased Illinois Methane's interest, and denied Alliance's motion for an injunction, allowing the state court lawsuit to proceed. *Id.* at *1-2. The district court affirmed. *Id.* at *2.

Ruling: The delay rental obligation was a covenant that ran with the land, and as such, Illinois Methane was a "known party with a known, present, and vested interest in real property . . . entitled to more than publication notice." *Id.* at *7.

- The case turned on "the constitutional sufficiency of the notice afforded to [Illinois Methane]. If the Debtors' attempted notice by publication satisfied the Due Process Clause, then Old Ben could sell the coal reserves 'free and clear' of Methane's interest, and the bankruptcy court could enjoin the State Court Action. But if the Constitution required more, then the bankruptcy court could conclude . . . that [Illinois Methane was] not 'bound by the terms' of the court's previous orders." *Id.* at *3 (internal citation omitted).

- The principles of due process operate in the same manner in bankruptcy and non-bankruptcy proceedings. *Id.* Constructive notice, such as notice by publication, is sufficient for purposes of due process in attempting to contact unknown parties. *Id.* The "'general rule' is that 'notice by publication is not enough with respect to [an entity] whose name and address are known or very easily ascertainable and whose legally protected interests are directly affected by the proceedings in question.'" *Id.* (internal citation omitted).

- Because the sufficiency of notice was intertwined with the nature of the property interest at issue, the Sixth Circuit analyzed the nature of the delay rental obligation and found it to be a known, present, vested interest in real property held by a known party, and not merely a pre-petition contingent claim. *Id.* at *4-7.

- Although Alliance tried to argue that Illinois Methane's interest was not reasonably known, the Sixth Circuit pointed to the parties' direct dealings in the original conveyance of methane gas, the fact that Old Ben filed for bankruptcy less than five years after the transaction, the recordation of the deed, and the due diligence performed in preparation for Old Ben's merger into AEI Resources. *Id.* at *7-8.

- The Sixth Circuit failed to credit Alliance's public policy arguments that reversal of the district court's decision would further the "federal interest in encouraging the finality of bankruptcy sales" on the ground that the Bankruptcy Code is "founded in fundamental notions of procedural due process." *Id.* at *10 (internal quotation omitted). "We do not doubt that a 'free and clear' sale under §363(f) is a powerful tool that can further the 'general Code policy of maximizing the value of the bankruptcy estate.' But it cannot be used indiscriminately to short-circuit the paramount protections of due process." *Id.* (internal citation omitted).

II. NUNC PRO TUNC ORDERS AND RETROACTIVE STAY RELIEF

A. *In re Merriman*, 616 B.R. 381 (B.A.P. 9th Cir. 2020), *appeal dismissed*, No. 20-60036 (9th Cir. Feb. 26, 2021):

A chapter 13 debtor appealed a bankruptcy court order retroactively lifting the automatic stay to permit a state court wrongful death action to proceed against the debtor, which had been filed post-petition by claimants who had no knowledge of the bankruptcy case. *Id.* at 385-86. On motion by the state court plaintiffs, the bankruptcy court found cause to retroactively lift the automatic stay to allow the state court suit to liquidate the plaintiffs' claim against the debtor. *Id.* at 386.

The court published its opinion to address the impact of a recent Supreme Court decision on the issue of *nunc pro tunc* orders. *Id.* In *Roman Cath. Archdiocese of San Juan v. Acevedo Feliciano*, 140 S.Ct. 696 (2020) (per curiam) ("*Acevedo*"), active and retired employees of certain Catholic schools sued the Roman Catholic and Apostolic Church of Puerto Rico, as well as other affiliated entities, for terminating a pension plan administered by a trust created by the Office of the Superintendent of Catholic Schools of the Archdiocese of San Juan. *Id.* at 697-98. The Supreme Court declined to reach the standing issues presented by the parties on the ground that the state-level trial court lacked jurisdiction to issue orders related to seizure and payment of the trust's funds, where those orders were issued after the proceeding had been removed to federal district court. *Id.* at 699-700. The Supreme Court particularly discredited the federal district court's attempt to remand the case to the state court via a *nunc pro tunc* order because such orders are not "some Orwellian vehicle for revisionist history—creating 'facts' that never occurred in fact" and stated "the court cannot make the record what is not." *Id.* at 701 (internal citations omitted).

In *Merriman*, the debtor opposed the request for stay relief on the ground that the state court claimants did not demonstrate that "cause" existed to lift the stay pursuant to section 362(d)(1). 616 B.R. at 386. The bankruptcy court granted retroactive stay relief for cause on the ground that the claimants did not have notice of the bankruptcy case before filing the state court suit, and that it made sense to try the issues in the state court suit in one forum, "potentially obtain[ing] findings and conclusions from the state court that could be applied preclusively in a nondischargeability proceeding." *Id.*

Ruling: The debtor did not show that the bankruptcy court abused its discretion in granting retroactive annulment of the stay to allow the state court litigation to proceed. *Id.* at 395. The BAP explained that "Congress left to the judgment of bankruptcy courts (via the reference) the decision about where a claim or action should be litigated by leaving the concept of 'cause' to terminate, annul, modify, or condition the stay purposefully undefined and flexible." *Id.* at 394.

- "In determining whether retroactive annulment of the stay is appropriate, courts have focused on two main factors: (1) whether the creditor was aware of the bankruptcy petition; and (2) whether the debtor engaged in unreasonable or inequitable conduct, or prejudice would result to the creditor." *Id.* at 387 (internal citation omitted). Because the state court action involved exclusively state law claims, and because there were five

other defendants in the state court proceeding, the bankruptcy court noted that "judicial economy dictates that the matter be tried in one forum." *Id.* at 387-88.

- The BAP also noted that the state court plaintiffs lacked notice of the bankruptcy filing, and that if retroactive relief were not granted, their wrongful death claim may be time-barred by the applicable state law statue of limitations. *Id.* at 388.

- The court noted that the Supreme Court's *Acevedo* decision had been entered during the pendency of the parties' appeal, and that at least one bankruptcy court interpreted the decision as prohibiting a grant of retroactive or *nunc pro tunc* stay relief. *Id.* at 391. The *Merriman* court did not interpret *Acevedo* to prohibit a bankruptcy court's ability to grant retractive stay relief, but noted that "this court should always carefully consider the scope and reach of Supreme Court opinions." *Id.* at 391-93. The *Merriman* court found that the *Acevedo* holding pertained to the court's ability to create jurisdiction where none exists, rather than to the bankruptcy court's power to annul the stay under section 362(d). *Id.*

- The *Merriman* court analyzed the language of section 362(d) and explained that "Congress' decision to deploy four verbs to describe the various ways in which a bankruptcy court might grant relief from stay indicates an express decision to grant bankruptcy courts the broadest possible range of options in respect of the stay, including annulling it, which has the effect of treating it as if it had never existed." *Id.* at 393. "The conclusion that *Acevedo* prohibits the annulment of the stay based on jurisdiction and property of the estate concerns reads too much into the Supreme Court's opinion." *Id.*

- "This result is perfectly consistent with the requirement that, in the performance of its 'traffic cop' role, bankruptcy courts must have broad authority to determine the appropriate forum for dispute resolution, taking into account and giving full respect to the panoply of interests to be weighed and protected in these matters, as well as to the dignity and power of other judicial processes." *Id.* at 394.

III. THE DEFINITION OF OFFICER UNDER THE BANKRUPTCY CODE

A. *Harrington v. LSC Commc'ns, Inc. (In re LSC Commc'ns, Inc.)*, 2021 WL 2887708 (S.D.N.Y. July 9, 2021) (Oetken, J.):

A United States Trustee appealed from a bankruptcy court order authorizing the debtor to pay retention bonuses to six employees. *Id.* at *1. As part of its bankruptcy, the debtor sought to implement a "Key Employee Retention Plan" ("KERP"), which selected 190 employees for compensation designed to retain individuals critical to continue operations during the uncertainty created by the bankruptcy filing. *Id.* The proposed KERP payments totaled $8 million and were conditioned on the employees' continued employment and the length of service with the company. *Id.*

The Trustee objected on the ground that the debtor failed to provide sufficient information as to whether the KERP employees qualified as "insiders" under the Bankruptcy Code (the "Code"), focusing on six employees who were also elected officers. *Id.* The debtor maintained that these employees were not insiders because they lacked the authority to bind the debtor, to implement company policies, or to have discretion over the debtor's operating budgets. *Id.*

The bankruptcy court analyzed the "economic substance" of the six employees' situations and found that the employees were "officers in title only," and so approved the plan and the payment of KERP payments on the ground that the six employees were not statutory corporate insiders. *Id.* at *2. The Trustee appealed the bankruptcy court's ruling that the six employees were not "insiders" under the Code. *Id.* The debtor argued the appeal was equitably moot because the Trustee did not seek a stay of the bankruptcy court's order and the debtor had already made KERP payments to the relevant employees. *Id.*

Ruling: The district court found that the circumstances did not warrant a finding of equitable mootness because the KERP payments, if found to be illegal, could be clawed back. *Id.* at *4. The district court reversed the bankruptcy court's order approving the KERP as to the six employees at issue, finding that the bankruptcy court erred by inquiring beyond the fact that the six employees were appointed by the debtor's board which gave them officer status under Delaware law. *Id.* at *7.

- A bankruptcy appeal should be dismissed as equitably moot, even if it is not constitutionally moot, when "even though effective relief could conceivably be fashioned, implementation of that relief would be inequitable." *Id.* at *2 (internal quotation omitted). In the context of bankruptcy proceedings, equitable mootness arises when an unstayed order results in a "comprehensive change in circumstances" or when a reorganization is "substantially consummated." *Id.* (internal citations omitted).

- The district court saw no reason why clawing back already-paid funds would be ineffective relief where the KERP payments were made to current employees who likely had notice of the case, only a handful of payments had been made, and the equities weighed in favor of requiring parties to disgorge the payments if those payments proved to be illegal. *Id.* at *3-4.

- "While a functional approach . . . may be appropriate in many cases, the Court agrees with the Trustee that with respect to officers *appointed or elected by the Board*, such individuals are "officers" under the Bankruptcy Code, at least absent a particularly strong showing that they do not perform a significant role in management." *Id.* at *6 (emphasis in original).

- Distinguishing between directors and officers, the district court noted that directors manage the corporation and have "the duty to establish or approve the long-term strategic, financial and organizational goals of the corporation; to approve formal or informal plans for the achievement of these goals; to monitor corporate performance; and to act, when in the good faith, informed judgment of the board it is appropriate to act." *Id.* at *7 (internal citation omitted). By contrast, officers "run the corporation on

a day-to-day basis including both purely ministerial duties and any responsibilities delegated by the board of directors." *Id.* (internal citation omitted).

IV. SETTLEMENT AGREEMENTS AS EXECUTORY CONTRACTS

A. *In re Fin. Oversight & Mgmt. Bd. for Puerto Rico*, --- F.Supp.3d ---, 2021 WL 2676983 (D. P.R. June 29, 2021) (Swain, J.):

The Commonwealth of Puerto Rico entered settlement agreements in two cases concerning the repayment of duplicate premiums for motor vehicle insurance. *Id.* at *1-2. Under state law, motorists are required to pay automotive insurance premiums upon vehicle registration to the Secretary of the Treasury, who then transfers the premiums to the Compulsory Liability Joint Underwriting Association of Puerto Rico. *Id.* at *1. Motorists could elect to opt out of the government's insurance scheme by obtaining private insurance and requesting reimbursement of any "duplicate" premiums already paid to the Commonwealth. *Id.* Pursuant to the settlement agreements, the Commonwealth would provide notice to class members to submit claims for reimbursement of the duplicate premiums. *Id.* at *2.

Following the Commonwealth's bankruptcy filing, the plaintiffs in the duplicate premium lawsuits sought stay relief to permit enforcement of the settlement agreements. *Id.* After supplemental briefing regarding whether the Commonwealth had established and complied with the notice and reimbursement procedures in the settlement agreements, the district court granted the stay relief motion in part, and denied it in part. *Id.* at *3. On appeal, the First Circuit ordered the district court "to make a preliminary determination of the parties' respective property interests in certain premium funds received by the Commonwealth" from the Joint Underwriting Association. *Id.* But before any such determination was made, the Oversight Board filed a motion pursuant to section 365 for entry of an order approving assumption of settlement agreements with the duplicate premium plaintiffs in an effort to resolve the matter consensually. *Id.* at *1, 3.

The unsecured creditors' committee objected to the motion on two grounds: first, that the settlement agreements were not subject to assumption under section 365(a) because they are not "executory contracts," and second, that the Oversight Board had not satisfied the business judgment standard applicable to section 365 motions. *Id.* at *3.

Ruling: The settlement agreements were executory contracts within the meaning of section 365(a) because under a functional test, there were substantial unfulfilled obligations on both sides, such as the obligation to jointly develop a website providing notice to class members, where segregated funds could not escheat to the Commonwealth until the reimbursement procedure met the "basic requirements of constitutional due process." *Id.* at *4 (internal citation omitted). The Oversight Board's assumption of the settlement agreements was a sound exercise of the Commonwealth's business judgment, as the settlement provided "an efficient benefit" to the Commonwealth by closing litigation that had been pending for nearly two decades. *Id.* at *6.

- Outlining the two approaches to determine whether contracts are "executory" for purposes of section 365, the district court noted that the Countryman approach

"requires courts to determine whether, under applicable non-bankruptcy law, parties on both sides of an agreement remain obligated to render substantial performance." *Id.* at *3. "Although the Countryman test is favored by many courts, some courts have moved away from Professor Countryman's approach and have adopted a functional approach which works backward from an examination of the purposes to be accomplished by rejection, and if they have already been accomplished then the contract cannot be executory." *Id.* at *4 (internal citation omitted).

- In this case, it was material which test the district court applied "because the [unsecured creditors'] Committee contends that the Oversight Board has failed to demonstrate that the Plaintiffs have material obligations outstanding under the Settlement Agreements, and it argues, the Settlement Agreements therefore would not be executory contracts under the Countryman test." *Id.*

- Analyzing three sets of outstanding obligations, the district court characterized the first two obligations as insufficient unfulfilled obligations under the functional test. *Id.* at *5-8. First, the Oversight Board argued that the parties had an obligation to file claim forms and conduct the duplicate premium reimbursement process, which the district court did not credit as being purely executory because it was an obligation to exercise an option to receive a reimbursement of duplicate premiums, and case law is divided with respect to whether and when an option contract becomes executory. *Id.* at *4. Next, the district court found that the plaintiffs' obligations to cooperate with the Commonwealth to jointly develop the contents of notices to class members non-executory because there was "no basis to conclude that there remain[ed] outstanding cooperation requirements" where much of the work on the notices had been completed prior to the filing of the Commonwealth's bankruptcy case. *Id*.

- The district court did find a substantial unfulfilled obligation, however, in the settlement agreement's requirement that the creation of a website for the claims reimbursement process be agreed to by the parties because "the existence of the Plaintiffs' right to approve the website—and the corresponding prospect that they could withhold such approval and thereby cloud, complicate, or disrupt completely implementation of the Settlement Agreement," rendered the settlement agreement an executory contract. *Id.* at *5.

V. U.S. TRUSTEE FEES ON DISBURSEMENTS UNDER A CHAPTER 11 PLAN

A. *In re Paragon Offshore, PLC*, --- B.R. ---, 2021 WL 2655320 (Bankr. D. Del. June 28, 2021) (Sontchi, C.J.):

Paragon Offshore plc ("Paragon") and several affiliated debtors filed for chapter 11 protection. *Id.* at *1. The plan of reorganization established a litigation trust to pursue claims against Noble Corporation plc ("Noble") and others. *Id.* The debtors transferred these claims to the trust free and clear of all liens, and the debtors agreed that after the transfer, they had no further interest in the litigation trust or its assets. *Id.* The plan was confirmed, and the confirmation order

provided that the debtors were to pay all fees required by 28 U.S.C. § 1930 until the debtors' case was closed, dismissed, or converted to a case under Chapter 7 of the Bankruptcy Code. *Id.*

The litigation trust filed suit against several Noble entities and certain directors, and Noble filed for chapter 11 protection less than six weeks before the trial. *Id.* at *2. The parties eventually settled for $90,375,000 and sought court approval of the proposed settlement based on a plan provision that allowed the litigation trust to "seek instructions from the Bankruptcy Court concerning the administration or disposition of the Trust Assets and the Noble Claims" and protected the trust from liability for decisions made with court approval. *Id.* The bankruptcy court approved the settlement, and Noble filed a post-confirmation report indicating that it had paid the United States Trustee $250,000—the maximum statutory amount—for disbursements including the settlement paid to the liquidation trust. *Id.*

The Trustee filed a motion to compel filing of post-confirmation quarterly reports and payment of statutory fees, seeking to compel Paragon and the litigation trust to pay all quarterly fees when due in connection with the settlement, specifically on disbursements to trust beneficiaries. *Id.*

Ruling: The bankruptcy court denied the Trustee's motion to compel, holding that the litigation trust's final distribution to trust beneficiaries on account of trust interests was not a disbursement on behalf of the debtors for purposes of 28 U.S.C. §1930(a)(6) and therefore not subject to the statutorily required fees. *Id.* at *3-4.

- "For decades the Office of the United States Trustee (the "OUST") has held a critical role as the watchdog over the integrity and administration of the United States bankruptcy system – a role it has filled admirably. . . . In recent years, Congress has raised those fees [to support the OUST's operations] dramatically, increasing the administrative burden on debtors, and reducing creditor recoveries. Unfortunately, the OUST has been compelled to act as a tax collector, focused on increasing the coffers of the U.S. Treasury, perhaps, at times, in derogation of its original mission." *Id.* at *1.

- Section 1930(a)(6) requires payment of quarterly fees to the OUST on "disbursements," "commonly understood in this context to apply to payments made with the funds generated from the liquidation of the debtor's assets." *Id.* at *3. The bankruptcy court noted that there are different interpretations of section 1930(a)(6), but "the common thread that appears to bind many of those decisions together is the fact that the debtor had some interest in, or control over, the money disbursed." *Id.*

- Here, the litigation trust's transfer of the trust corpus to the trust's beneficiaries did not trigger any obligation to pay the statutory fees required by section 1930 because the litigation trust was not paying expenses on behalf of any debtors and the debtors transferred any interests in the trust, free and clear of all liens and in consideration for the benefit of certain agreed releases, as part of its plan of reorganization. *Id.* at *3-4. Because the trust assets vested free and clear in the trust several years prior to the Trustee's motion to compel, the bankruptcy court held that the final distribution could not be construed as a "disbursement" on behalf of the debtors. *Id.* at *4.