Exploring the Debate Regarding Nondebtor, Third-Party Releases

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INTRODUCTION

In an August 8, 2021 episode of HBO's *Last Week Tonight*, host John Oliver took issue with Purdue Pharma's proposed chapter 11 plan, decrying the plan's nonconsensual, third-party releases as "insidious" and opining that "if it sounds weird to you that a company can declare bankruptcy and then a bunch of individuals get shielded from liability, that's because it is. It's really [expletive] weird." He went on, "[i]t might well be true that this is the best deal we can get under our current system, but the fact that that's the case doesn't speak well to this deal or indeed, the system itself."

Nondebtor, third-party releases have been utilized in bankruptcy for more than 35 years, and, therefore, such releases likely do not strike seasoned bankruptcy practitioners as particularly "weird." Both entities with and without large mass tort exposure utilize nondebtor, third-party releases in circuits where such releases are permitted.[2] However, recent efforts to secure nondebtor, third-party releases in high-profile bankruptcies (e.g., Purdue Pharma, Boy Scouts of America, and USA Gymnastics) have generated significant public controversy (as illustrated by the above anecdote). It is perhaps unsurprising, then, that hostility towards nondebtor, third-party releases in bankruptcy is growing.

This paper is not intended as a comprehensive examination of issues surrounding nondebtor, third-party releases, nor does it seek to take sides in the debate on the viability of third-party releases in bankruptcy. Instead, this paper explores three questions at the center of the debate—(1) does the Bankruptcy Code authorize nondebtor, third-party releases in chapter 11 cases, other than under 11 U.S.C. § 524(g); (2) does a district court, and by reference, a bankruptcy court have subject matter jurisdiction, under 28 U.S.C. § 1334, to release or enjoin third-party

[2] There is a split of authority regarding the permissibility of nondebtor, third-party releases. Generally speaking, the Fifth, Ninth, and Tenth Circuits have held that bankruptcy courts lack authority to grant third-party releases in non-asbestos cases. *See, e.g.*, *In re Pac. Lumber Co.*, 584 F.3d 229, 252 (5th Cir. 2009); *In re Lowenschuss*, 67 F.3d 1394, 1401-02 (9th Cir. 1995), *cert. denied*, 517 U.S. 1243 (1996); *In re W. Real Est. Fund, Inc.*, 922 F.2d 592, 600 (10th Cir. 1990), *modified sub nom. Abel v. West*, 932 F.2d 898 (10th Cir. 1991). The current majority view, held by the First, Third, Fourth, Sixth, Seventh, and Eleventh Circuits, currently permits third-party releases in some form, though courts generally agree that such releases should be used only in exceptional circumstances. *See, e.g.*, *In re Millennium Lab Holdings II, LLC*, 945 F.3d 126, 133-40 (3d Cir. 2019), *cert. denied*, 140 S.Ct. 2805 (2020); *In re Seaside Eng'g & Surveying, Inc.*, 780 F.3d 1070, 1076-79 (11th Cir. 2015), *cert. denied*, 577 U.S. 823 (2015); *Nat'l Heritage Found., Inc. v. Highbourne Found.*, 760 F.3d 344, 350 (4th Cir. 2014), *cert. denied*, 574 U.S. 1076 (2015); *In re Airadigm Commc'ns, Inc.*, 519 F.3d 640, 657 (7th Cir. 2008); *In re Dow Corning Corp.*, 280 F.3d 648, 661 (6th Cir. 2002), *cert. denied*, 537 U.S. 816 (2002). At present, the First, Eighth, and D.C. Circuits have yet to weigh in on the question, and the state of the law in the Second Circuit is unsettled. *See In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 141 (2d Cir. 2005) (permitting third-party releases). *Cf. 605 Fifth Prop. Owner, LLC v. Abasic, S.A.*, No. 21cv811(DLC), 2022 WL 683746, at *1, 4 (S.D.N.Y. Mar. 8, 2022) (permitting third-party releases only in "rare cases" in which the release is "essential to the reorganization plan"); *In re Purdue Pharma, L.P.*, 635 B.R. 26 (S.D.N.Y. Dec. 16, 2021), *appeal filed sub nom., Purdue Pharma, L.P. v. State of Washington, et al.*, Case No. 22-85, ECF No. 220 (2d Cir. Jan. 27, 2022) (finding that nonconsensual releases of nondebtor third-parties were not permitted under the Bankruptcy Code).

claims; and (3) does a bankruptcy court have the requisite authority (under the Constitution and 28 U.S.C. § 157) to permanently enjoin or release nondebtor, third-party claims.

PART I—THE "GREAT UNSETTLED QUESTION"[3]

A. *The Current Landscape*

In December 2021, the United States District Court for the Southern District of New York issued an opinion in *In re Purdue Pharma, L.P.* that casts doubt on the viability of nondebtor, third-party releases in the Second Circuit.[4] Reversing the bankruptcy court's order confirming the debtor's chapter 11 plan (which contained such a release), Judge Colleen McMahon concluded that the bankruptcy court lacked authority to order the nonconsensual release of third-party direct claims against nondebtors—a conclusion that has been characterized as a "seismic shift" in the development of the law.[5]

The Bankruptcy Code does not explicitly authorize third-party releases or injunctions outside of the asbestos liability context. *See* 11 U.S.C. §§ 524(g), (h).[6] Yet, "some of the busiest venues for large corporate reorganizations, including the Southern District of New York and Delaware, have long included third-party releases . . . typically in favor of the debtors' officers, directors, professionals and equity sponsors" in confirmed chapter 11 plans.[7] Third-party releases have been used to enjoin prosecution of both direct and indirect, nondebtor, third-party claims that otherwise would be prosecuted in courts of general jurisdiction, often in state court or before a jury.[8] Third-party releases also have been linked to a rise in companies using the permissive venue provisions of the Bankruptcy Code to select a bankruptcy venue likely to issue such releases/injunctions.[9]

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[3] *See Purdue Pharma, L.P.*, 635 B.R. at 37.
[4] *See id*.
[5] *See* Thomas J. Salerno & Clarissa C. Brady, *In Defense of Third-Party Releases in Chapter 11 Cases: Part II*, ABI JOURNAL, Apr. 2022, at 30. While the Second Circuit is routinely cited as following the majority view permitting nonconsensual, third-party releases, the district court in *Purdue Pharma* stated that Second Circuit opinions addressing the issue have been decided on non-statutory grounds, with the only clear statement by the Court of Appeals being that "Section 105(a), standing alone, does not confer such authority on the bankruptcy court outside the asbestos context." *See Purdue Pharma, L.P.*, 635 B.R. at 104.
[6] *See* Michael Legge et al., *Recent Rulings on 3rd-Party Releases, Texas 2-Step Cases Paint Mixed Picture: Is Bankruptcy More Equitable Path to Compensation than 'Lottery' of Tort System or Are Nondebtor Protections 'Abuse' of Process?,* Reorg.com: Bankruptcy Industry Update (Feb. 28, 2022 2:03PM), https://reorg.com/bankruptcy-analysis-protections/.
[7] *Id.*
[8] *Id.*
[9] *See Patterson v. Mahwah Bergen Retail Grp., Inc.*, 636 B.R. 641, 654-55 (E.D. Va. Jan. 13, 2022) ("Ascena Retail") ("[A]ccording to the Trustee, the Richmond Division . . . joins the District of Delaware, the Southern District of New York, and the Houston Division of the Southern District of Texas as the venue choice for 91% of the 'mega' bankruptcy cases.")

In *Purdue Pharma*, the district court issued a 142-page opinion, detailing the unsettled state of the law regarding third-party releases and surveying the positions taken in the circuit court split.[10] Judge McMahon noted that the courts that prohibit third-party releases are united in their reasoning, but the courts that permit such releases "offer various justifications for their conclusions."[11] Frustrated by dearth of clear authority, Judge McMahon wrote, "[t]his will no longer do. Either statutory authority exists or it does not. There is no principled basis for acting on questionable authority in 'rare' or 'unique' cases" and further, "[w]hen every case is unique, none is unique."[12]

Because Purdue was "[e]ngulfed in a veritable tsunami of litigation," it filed for chapter 11 protection in September 2019 with the intention of resolving "both existing and future claims against the company arising from the prescription of OxyContin."[13] The plan of reorganization proposed broad releases of direct claims against nondebtors, including a variety of state law claims "arising under various unfair trade practices and consumer protection laws that make officers, directors and managers who are responsible for corporate misconduct personally liable for their actions."[14] Over ninety-five percent of the voting creditors voted to accept the plan.[15]

With "obvious reluctance," the Bankruptcy Court for the Southern District of New York confirmed the plan because the court applied the traditional rubric for approving settlements in bankruptcy and concluded that there was simply no other means to achieve a similar result.[16] On appeal to the district court, a coalition of appellants argued that the plan's broad, nonconsensual third-party releases impermissibly expanded bankruptcy court protection to members of the Sackler family and their affiliates, none of whom had filed for bankruptcy themselves.[17]

To the district court, "[t]he great unsettled question" was "whether the Bankruptcy Court—or any court—is statutorily authorized to grant such releases."[18] Siding with the minority view, the district court concluded that the Bankruptcy Code does not provide statutory authorization to approve nonconsensual nondebtor releases, outside of section 524(g).[19] The district court acknowledged that invalidating the third-party releases would most likely lead to the undoing of Purdue Pharma's carefully crafted plan, which would fund desperately needed programs to counteract opioid addiction, but concluded that a bankruptcy court's "power to grant relief to a

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[10] *See Purdue Pharma, L.P.*, 635 B.R. at 37, 104-06.
[11] *Id.* at 37.
[12] *Id*.
[13] *Id.* at 35.
[14] *Id.* at 70.
[15] *See id.* at 71; Paul R. Hage, *"The Great Unsettled Question": Nonconsensual Third-Party Releases Deemed Impermissible in Purdue*, ABI JOURNAL, Feb. 2022, at 12.
[16] *See Purdue Pharma, L.P.*, 635 B.R. at 73-74; Hage, *supra* note 15, at 12.
[17] Hage, *supra* note 15, at 13.
[18] *Purdue Pharma, L.P.*, 635 B.R. at 37.
[19] *Id*. at 106-15.

non-debtor from non-derivative third-party claims 'can only be exercised within the confines of the Bankruptcy Code.'"[20]

The district court further concluded that the bankruptcy court lacked constitutional authority to enter a final order approving such releases under *Stern v. Marshall* because "nothing in *Stern* or any other case suggests that a party otherwise entitled to have a matter adjudicated by an Article III court forfeits that constitutional right if the matter is disposed of as part of a plan of reorganization in bankruptcy."[21] Purdue appealed the district court's decision, and since Judge McMahon's opinion entered, the bankruptcy court approved a mediated settlement resulting in an additional $1 billion contribution from the Sackler family, the "rocket docket" appeal of the district court decision to the Second Circuit is expected to resolve in summer 2022, and commentators widely expect a potential appeal of any Second Circuit ruling to the United States Supreme Court.[22]

Following the *Purdue Pharma* decision, courts have been increasingly hostile to nondebtor third-party releases in chapter 11 plans. In the *Ascena Retail* decision issued in January 2022, the District Court for the Eastern District of Virginia roundly criticized its bankruptcy court colleagues for regularly approving third-party releases, where it concluded that the bankruptcy court plainly lacked constitutional authority to adjudicate claims covered by the releases proposed in the plan.[23] The court made its current skepticism toward third-party releases perfectly clear: "Third-party releases, such as those at issue here, carry much controversy, for they are a 'device that lends itself to abuse.'"[24] The *Ascena Retail* opinion also reversed the bankruptcy court's approval of the manner of the releases—an opt-out mechanism, as opposed to a consensual release—because the third-parties' silence could not constitute consent to the bankruptcy court's jurisdiction for *Stern v. Marshall* purposes or to the releases themselves.[25]

In March 2022, another district judge in the Southern District of New York issued an opinion that struck down a third-party release in a confirmed and consummated chapter 11 plan.[26] In *Abasic*, the debtor signed a commercial lease, guaranteed by the debtor's corporate parent in favor of the landlord.[27] Due to the pandemic, the debtor filed for chapter 11 protection, rejected the lease, and confirmed a plan that included a third-party release extending to the debtor's "affiliates."[28] After the plan was consummated, the landlord sued the parent on the guarantee, and

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[20] *Id*. at 115.
[21] *Id*. at 79-82 (citing *Stern v. Marshall*, 564 U.S. 462 (2011)).
[22] *See* Salerno & Brady, *supra* note 5, at 30; *see also Purdue Pharma, L.P. v. State of Washington, et al.*, Case No. 22-85, ECF No. 220 (2d Cir. Jan. 27, 2022).
[23] *See Ascena Retail*, 636 B.R. at 655, 702-03 ("The ubiquity of third-party releases in the Richmond Division demands even greater scrutiny of the propriety of such releases.").
[24] *Id*. at 654.
[25] *See id*. at 672-88.
[26] *See Abasic, S.A.*, 2022 WL 683746, at *1.
[27] *Id*.
[28] *Id.* at * 1, 3.

the parent contended it had been released by the plan as an affiliate of the debtor.[29] The district court held that the landlord was entitled to enforce the guarantee against the parent because the parent had not explained why the plan "should be read to extinguish all of its obligations to anyone who happened to do business with its American subsidiary—the organization that actually declared bankruptcy," nor had it explained the exceptional circumstances which made the nondebtor release "essential to the reorganization plan."[30]

The pendulum may, however, be swinging back. Seeing that certain venues were increasingly hostile to nondebtor third-party releases, the Bankruptcy Court for the District of Delaware claimed its spot as a favorable venue for debtors seeking such relief.[31] In a February 2022 opinion, the Delaware Bankruptcy Court opined, "[t]here can be no debate over the proposition that a bankruptcy court can approve a plan that includes third-party releases."[32] In *Mallinckrodt*, the court examined a chapter 11 plan for a pharmaceutical company that produced and sold opioids and other specialty pharmaceutical products.[33] Stating that he was aware of the *Purdue Pharma* and *Ascena Retail* precedents but bound by the law of the Third Circuit, Judge Dorsey confirmed the debtors' plan, which included a nonconsensual, third-party release of opioid and non-opioid claims.[34] The court also found the opt-out mechanism proposed in the plan to be a valid method of obtaining consent to the releases.[35] One interesting wrinkle in the *Mallinckrodt* opinion is that Judge Dorsey offered that he "disagree[s] with the notion that releases are the equivalent of a discharge," a departure from the *Purdue Pharma* and *Ascena Retail* rulings which held that such releases effectively extinguish third-party claims.[36]

B. Rationales for the Minority and Majority Views

A confirmed chapter 11 plan generally "discharges the debtor from any debt that arose before the date of such confirmation . . . ."[37] The effect of a chapter 11 discharge is governed by 11 U.S.C. § 524(a) which states, in part, that discharge "voids any judgment at any time obtained, to the extent that such judgment is a determination of the *personal liability of the debtor* with respect to any debt discharged under [applicable Bankruptcy Code sections] . . . [and] operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a *personal liability of the debtor* . . . ."[38]

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[29] *Id.* at * 1-3.
[30] *Id.* at * 3-4.
[31] *See In re Mallinckrodt PLC*, No. 20-12522 (JTD), 2022 WL 404323 (Bankr. D. Del. Feb. 8, 2022).
[32] *Id.* at *23.
[33] *Id.* at *1.
[34] *Id.* at *1, 16, n.70.
[35] *Id.* *25-26.
[36] *See id.* at *16, n.70. *Cf. Ascena Retail*, 636 B.R. at 702-03; *Purdue Pharma, L.P.*, 635 B.R. at 95-98.
[37] 11 U.S.C. § 1141(d)(1)(A).
[38] *Id.* §§ 524(a)(1)-(2) (emphasis added).

While expansive, the discharge injunction "does not extinguish the debt itself but merely releases the debtor from personal liability. . . . The debt still exists, however, and can be collected from any other entity that may be liable"[39] for the debt pursuant to section 524(e) of the Bankruptcy Code, which states that "discharge of a debt of the debtor *does not affect the liability of any other entity on*, or the property of any other entity for, such debt."[40]

Courts agree, pursuant to section 524(e), that "the discharge of the debtor's debt does not itself affect the liability of a third-party."[41] Yet, there is substantial disagreement regarding whether section 524(e) constitutes an absolute bar prohibiting nonconsensual, third-party releases and/or whether a bankruptcy court has statutory authority to approve the nonconsensual release of third-party claims against nondebtors in connection with confirmation of a chapter 11 plan.[42]

A minority of courts hold that section 524(e) constitutes a statutory impediment to a bankruptcy court's approval of third-party releases of non-asbestos related claims and that bankruptcy courts do not have authority under the Bankruptcy Code to approve such releases.[43] These courts do not permit third-party releases and interpret section 524(e) as being a specific provision such that bankruptcy courts may not expand its scope using section 105(a) to discharge claims against nondebtors.[44] These courts "emphasize that § 524(e) discharges the debtor only, not third parties."[45]

The (present) majority view is that nonconsensual, third-party releases are legally permissible under certain limited or unique circumstances.[46] These courts generally hold that section 524(e) cannot be construed as an *absolute* or *per se* proscription which limits a bankruptcy court's equitable powers under section 105(a) to "issue any order . . . that is necessary or appropriate to carry out the provisions . . . " of the Code, coupled with a bankruptcy court's

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[39] *W. Real Est. Fund, Inc.,* 922 F.2d at 600 (quoting *In re Lembke*, 93 B.R. 701, 702 (Bankr. D.N.D. 1988)).
[40] 11 U.S.C. § 524(e)(emphasis added); *see also Owaski v. Jet Florida Sys., Inc. (In re Jet Florida Sys., Inc.)*, 883 F.2d 970, 973 (11th Cir. 1989)(stating the "discharge will not act to enjoin a creditor from taking action against another who also might be liable to the creditor").
[41] *Seaside Eng'g & Surveying*, 780 F.3d at 1078.
[42] *See Purdue Pharma, L.P.*, 635 B.R. at 89 (stating that whether section 524(e) constitutes a statutory impediment to the nonconsensual, third-party releases "is entirely a function of where the debtor files for bankruptcy.").
[43] *See id.*; *Pac. Lumber Co.,* 584 F.3d at 229; *Lowenschuss,* 67 F.3d at 1394; *W. Real Est. Fund, Inc.,* 922 F.2d at 592.
[44] *In re HWA Props., Inc.*, 544 B.R 231, 238-39 (Bankr. M.D. Fla. 2016).
[45] *In re Master Mortg. Inv. Fund, Inc.,* 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994).
[46] *Millennium Lab Holdings, II,* 945 F.3d at 129 (finding third-party releases were "integral to the restructuring of the debtor-creditor relationship"); *Seaside Eng'g & Surveying, Inc.,* 780 F.3d at 1070; *Behrmann v. Nat'l Heritage Found., Inc. (In re Behrmann),* 663 F.3d 704, 710 (4th Cir. 2011)(rejecting "the notion that 11 U.S.C. § 524(e) forecloses bankruptcy courts from releasing and enjoining causes of action against nondebtors"); *Airadigm Commc'ns, Inc.* 519 F.3d at 640; *Metromedia Fiber Network, Inc.,* 416 F.3d at 136; *Dow Corning Corp.,* 280 F.3d at 648; *In re Drexel Burnham Lambert Grp., Inc.,* 960 F.2d 285, 293 (2d Cir. 1992)(stating that a bankruptcy "court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtor's reorganization plan."); *In re Cont'l Airlines,* 203 F.3d 203, 211 (3d Cir. 2000*); Menard-Sanford v. Mabey (In re A.H. Robins Co., Inc.),* 880 F.2d 694 (4th Cir. 1989)(finding that the bankruptcy court had the power to enjoin suits against certain third-party entities that involved the Dalkon Shield).

authority to approve a plan under 11 U.S.C. § 1123(b)(6) which includes "any other appropriate provision not inconsistent with the applicable provisions" of the Bankruptcy Code.[47] Accordingly, these courts interpret section 524(e) to be consistent with section 105(a) because 524(e) does not specifically prohibit third-party releases, so the bankruptcy court has the power to approve such provisions under section 105(a) "as long as the circumstances justify such extraordinary relief."[48]

In *Purdue Pharma*, the proposed plan included nonconsensual releases of direct third-party claims against nondebtors, the Sackler family shareholders who had served as officers, directors, and managers of the drug manufacturer.[49] In exchange for the release of current and future opioid lawsuits, the Sacklers have now agreed to contribute $6 billion to fund Purdue Pharma's restructuring plan.

The bankruptcy court explained that a "clear majority" of circuits that have addressed the issue have found that bankruptcy courts have statutory or "residual" authority under the Bankruptcy Code to approve third-party releases "in appropriate, narrow circumstances."[50] As explained by the Seventh Circuit in the case of *In re Airadigm Commc'ns,* a bankruptcy court's "residual authority" to approve nonconsensual, third-party releases is derived from sections 105(a) and 1123(b)(6) of the Bankruptcy Code:

> A bankruptcy court "appl[ies] the principles and rules of equity jurisprudence," *Pepper v. Litton*, 308 U.S. 295, 304, 60 S.Ct. 238, 84 L.Ed. 281 (1939), and its equitable powers are traditionally broad, *United States v. Energy Resources Co., Inc.,* 495 U.S. 545, 549, 110 S.Ct. 2139, 109 L.Ed.2d 580 (1990). Section 105(a) codifies this understanding of the bankruptcy court's powers by giving it the authority to effect any "necessary or appropriate" order to carry out the provisions of the bankruptcy code. *Id.* at 549; 11 U.S.C. § 105(a). And a bankruptcy court is also able to exercise these broad equitable powers within the plans of reorganization themselves. Section 1123(b)(6) permits a court to "include any other appropriate provision not inconsistent with the applicable provisions of this title." 11 U.S.C. § 1123(b)(6). In light of these provisions, we hold that this "***residual authority***" permits the bankruptcy court to release third parties from liability to participating creditors if the release is "appropriate" and not inconsistent with any provision of the bankruptcy code.[51]

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[47] *See* 11 U.S.C. §§ 105(a), 1123(b)(6).
[48] *HWA Props., Inc.*, 544 B.R. at 239.
[49] *In re Purdue Pharma, L.P.,* 633 B.R. 53 (Bankr. S.D.N.Y. 2021), *vacated*, 635 B.R. 26 (S.D.N.Y. 2021), *appeal filed sub nom.*, *Purdue Pharma, L.P. v. State of Washington, et al.*, Case No. 22-85, ECF No. 220 (2d Cir. Jan. 27, 2022).
[50] *Id.* at 100.
[51] *Airadigm Commc'ns, Inc.*, 519 F.3d at 657 (emphasis added).

"In other words," the *Purdue Pharma* bankruptcy court explained that third-party "releases flow from a federal statutory scheme . . . [which] reflects Congress's exercise of its preemption powers, which permit the abolition of [rights] to attain a permissible legislative object."[52] Accordingly, the bankruptcy court concluded that it had statutory authority "to authorize the release of non-derivative—direct or particularized—claims because the third party claims to be released . . . . were 'premised as a legal matter on a meaningful overlap with the debtor's conduct.'"[53]

The district court reversed, concluding that the Bankruptcy Code does not, even in rare or unique cases, authorize the nonconsensual release of direct claims against nondebtors, stating emphatically:

> No. The Bankruptcy Code does not authorize a bankruptcy court to order the non-consensual release of third-party claims against non-debtors in connection with the confirmation of a chapter 11 plan . . . Sections 105(a) and 1123(a)(5) & (b)(6), whether read individually or together, do not provide a bankruptcy court with such authority; and there is no such thing as "equitable authority" or "residual authority" in a bankruptcy court untethered to some specific, substantive grant of authority in the Bankruptcy Code.[54]

The Second Circuit approved Purdue Pharma's request to expedite its interlocutory appeal, and oral arguments were scheduled for the week of April 25, 2022.[55]

C. The History of Nondebtor, Third-Party Releases in Bankruptcy

Section 524(g), added by the Bankruptcy Reform Act of 1994, authorized bankruptcy courts to issue an injunction in asbestos-related cases "against any entity taking legal action to collect a claim or demand that it is to be paid in whole or in part by a trust created through a qualifying plan of reorganization."[56] Congress enacted section 524(g) after the Second Circuit affirmed the use of a similar injunction in the landmark asbestos-related bankruptcy case of Johns-Manville Corporation ("Johns-Manville"),[57] which provided a reorganization blueprint for entities crippled by mass tort litigation.

In its chapter 11 case, Johns-Manville, an asbestos-manufacturing company, proposed a plan which established a trust designed to compensate both current and unknown future personal

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[52] *Purdue Pharma, L.P.,* 633 B.R. at 103 (quoting *Lynch v. Lapidem Ltd. (In re Kirwan Offices S.A.R.L.),* 592 B.R. 489, 511 (S.D.N.Y. 2018)).
[53] *Purdue Pharma, L.P.*, 635 B.R. at 75.
[54] *Id.* at 78.
[55] *See supra* note 22.
[56] 4 COLLIER ON BANKRUPTCY ¶ 524.07 (Richard Levin & Henry J. Sommer eds., 16th ed. 2022).
[57] *See generally Kane v. Johns-Manville Corp. (In re Johns-Manville Corp.)*, 843 F.2d 636 (2d Cir. 1988).

injury claimants.[58] The purpose of the trust, which was funded in part by stock of the reorganized debtor, was to provide a means for Manville to reorganize while satisfying future/unknown asbestos claims.[59] The plan included an injunction channeling all future asbestos claims to the trust which barred claimants from suing Manville and other third-parties.[60] Relying on its equitable powers under section 105(a), the bankruptcy court overruled objections filed on behalf of personal injury claimants and confirmed the plan.[61]

The Second Circuit affirmed, finding in part that the holder of an asbestos-related personal injury claim lacked third-party standing to challenge the confirmation order.[62] The Second Circuit stated that "[t]he Bankruptcy Code provides statutory authority for the channeling orders," citing section 363(f), and noted that free and clear sales of property in the debtor's estate are permitted under certain circumstances, including situations where the third-party interest is "in *bona fide* dispute."[63] Because such a dispute existed in the Johns-Manville bankruptcy proceeding, given that "the product liability limits on the policies to which the vendor endorsements attach ha[d] been exhausted," the Second Circuit viewed the channeling orders "were necessary to . . . make sure that claims to Manville's insurance proceeds were, in fact, channeled to the settlement fund and could not be asserted directly against the insurers."[64] In effect, the Second Circuit found that because the bankruptcy court had jurisdiction over property of the debtor's estate, section 363(f) provided authority for the bankruptcy court to "enjoin a lien-holder from attempting to assert his lien against property [of the estate] in the hands of a purchaser who has acquired from the Bankruptcy Court a title free and clear of liens and encumbrances."[65]

To the extent the claimant argued that the injunction effectively granted a discharge to nondebtor third-parties such as Manville's insurers, the Second Circuit noted that it had previously determined that the bankruptcy court did not exceed its jurisdiction or authority when it enjoined third-party suits in conjunction with the settlement of Manville's claims against its insurers because the insurance policies constituted "property of the debtor's estate."[66]

Thereafter, Congress enacted section 524(g), utilizing the trust/injunction mechanisms established in *Manville* as a guideline.[67] Subsection 524(g)(4)(A)(ii) states that "*[n]otwithstanding*

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[58] *Id.* at 639-40.
[59] *Id*. at 640.
[60] *Id.*
[61] *See generally In re Johns-Manville Corp.*, 68 B.R. 618, 624-27, 638.
[62] *See generally Kane*, 843 F.2d 636 (2d Cir. 1988).
[63] *MacArthur Co. v. Johns–Manville Corp. (In re Johns– Manville Corp.)*, 837 F.2d 89, 93 (2d Cir. 1988).
[64] *Id.*
[65] *Id.* (internal citation omitted).
[66] *Kane*, 843 F.2d at 643, n.4 (citing *MacArthur Co.*, 837 F.2d at 90, and finding any rights that the distributor of Manville's asbestos products, which claimed to be coinsured under some of the policies, might have in the policies were derivative of and inseparable from the debtor's own rights, so as to fall within the bankruptcy court's *in rem* subject matter jurisdiction over property of the debtor's estate).
[67] *See* H.R. Rep. No. 103-835, 103rd Cong., 2d Sess. (1994), *reprinted in* 1994 U.S.C.C.A.N. 3340.

the provisions of section 524(e), such an injunction may bar any action directed against a third party who is identifiable from the terms of such injunction (by name or as part of an identifiable group) and is alleged to be directly or indirectly liable for the conduct of, claims against, or demands on the debtor . . . . "[68]

In another mass tort litigation case involving Dalkon Shield-related injuries, *Menard-Sanford v. Mabey (In re A.H. Robins Co., Inc.),*[69] the debtor sought confirmation of a plan that enjoined suits against third-parties on the basis that the third-parties were joint tortfeasors of the debtor. After the bankruptcy court and district court jointly confirmed the plan, the Fourth Circuit affirmed, rejecting arguments that section 524(e) prohibited the injunction, stating:

> Some courts have held that § 524(e) and its predecessor, § 16 of the 1898 Bankruptcy Act, results in the bankruptcy court having no power to discharge liabilities of a nondebtor pursuant to the consent of creditors as a part of a reorganization plan. *See Underhill v. Royal*, 769 F.2d 1426, 1432 (9th Cir. 1985); *Union Carbide Corp. v. Newboles,* 686 F.2d 593 (7th Cir. 1982). However, the Fifth Circuit has stated that "[a]lthough section 524 has generally been interpreted to preclude release of guarantors by a bankruptcy court, the statute does not by its specific words preclude the discharge of a guaranty when it has been accepted and confirmed as an integral part of reorganization." *Republic Supply Co. v. Shoaf*, 815 F.2d 1046, 1050 (5th Cir. 1987).[70]

The Fourth Circuit has declined to construe section 524(e) as a prohibition on the power of bankruptcy courts where a plan has been "overwhelmingly approved" and "where the entire reorganization hinges on the debtor being free from indirect claims such as suits against parties who would have indemnity or contribution claims against the debtor . . ."[71] Relying in part on the bankruptcy court's equitable powers under section 105(a), as well as the analogous doctrine of marshalling of assets, the Fourth Circuit further stated that "[a] creditor has no right to choose which of two funds will pay his claim. The bankruptcy court has the power to order a creditor who has two funds to satisfy his debt to resort to the fund that will not defeat other creditors."[72]

In *SEC v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Grp., Inc.*), directors and officers received a release from liability for certain securities actions in the debtor's plan. The Second Circuit adopted the view expressed by the Fourth Circuit in *A.H. Robins,*

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[68] 11 U.S.C. § 524(g)(4)(A)(ii)(emphasis added).
[69] *A.H. Robins Co.*, 880 F.2d at 694. For a discussion specific to third-party releases of tort claims, *see* Anne Hardiman, *Toxic Torts and Chapter 11 Reorganization: The Problem of Future Claims*, 38 VAND. L. REV. 5, 1369 (1985).
[70] *A.H. Robins Co.*, 880 F.2d. at 702.
[71] *Id*.
[72] *Id.* at 701.

stating that "a court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtor's reorganization plan."[73]

Another seminal case in the area of nonconsensual, third-party releases involving mass tort litigation is the case of *In re Dow Corning*,[74] in which the Sixth Circuit adopted a seven-factor test to determine whether a bankruptcy court has authority to enjoin a nonconsenting creditor's claims against a nondebtor to facilitate a reorganization plan. Although "[t]he Bankruptcy Code does not explicitly prohibit or authorize a bankruptcy court to enjoin" third-party claims, the Sixth Circuit stated that bankruptcy courts enjoy broad authority under 11 U.S.C. § 105(a) "to issue 'any order, process, or judgment that is necessary or appropriate to carry out the provisions'" of the Code.[75] Consistent with section 105(a)'s broad grant of equitable power, the Sixth Circuit explained that section 1123(b)(6) is the provision of the Bankruptcy Code that grants a bankruptcy court affirmative power to use its equitable powers to approve third-party releases.[76] "Thus, the bankruptcy court, as a forum for resolving large and complex mass litigations, has substantial power to reorder creditor-debtor relations needed to achieve a successful reorganization."[77] The Sixth Circuit further opined that section 524(e) merely "explains the effect of a debtor's discharge. It does not prohibit the release of a non-debtor."[78]

Having concluded that enjoining third-party claims against a nondebtor is "not inconsistent" with the Code, the Sixth Circuit set out the following factors for courts to considering when determining whether sufficient "unusual circumstances" are present in a case to approve third-party releases:

> (1) There is an identity of interests between the debtor and the third party, usually an indemnity relationship, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete the assets of the estate;
>
> (2) The non-debtor has contributed substantial assets to the reorganization;
>
> (3) The injunction is essential to reorganization, namely, the reorganization hinges on the debtor being free from indirect suits against parties who would have indemnity or contribution claims against the debtor;
>
> (4) The impacted class, or classes, has overwhelmingly voted to accept the plan;

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[73] *Drexel Burnham Lambert Grp., Inc.*, 960 F.2d at 293 (citing *A.H. Robins Co.*, 880 F.2d at 701).
[74] *Dow Corning Corp.,* 280 F.3d at 648.
[75] *Id.* at 656.
[76] *Id*.
[77] *Id*.
[78] *Id.* at 657.

(5) The plan provides a mechanism to pay for all, or substantially all, of the class or classes affected by the injunction;

(6) The plan provides an opportunity for those claimants who choose not to settle to recover in full and;

(7) The bankruptcy court made a record of specific factual findings that support its conclusions.[79]

The Eleventh Circuit has also upheld such releases over objections during the confirmation process.[80] In *Seaside Engineering & Surveying*, the bankruptcy court confirmed a plan under which the original principal guarantors became equity members in a new company, Gulf Atlantic, and the plan included a release of any claims against the debtor, Gulf Atlantic, and any of their respective representatives for "any act, omission, transaction or other occurrence in connection with, relating to, or arising out of the Chapter 11 Case . . . except and solely to the extent such liability is based on fraud, gross negligence or willful misconduct."[81]

The Eleventh Circuit reviewed its prior precedent finding that 11 U.S.C. § 105(a) provided authority for the bankruptcy court to issue a bar order in favor of a defendant who provided funds for the bankruptcy estate and would not have done so in the absence of such a release.[82] Noting that the discharge of the debtor's debt "does not itself affect the liability of a third-party" under 11 U.S.C. § 524(e), the Eleventh Circuit interpreted section 524(e) to not foreclose the bankruptcy courts' ability to approve a third-party release because "if Congress had meant to limit the powers of bankruptcy courts, it would have done so clearly, as it did in other instances."[83] Accordingly, the court stated that section 105(a) "codifies the established law that a bankruptcy court 'applies the principles and rules of equity jurisprudence.'"[84]

To approve the proposed release, the Eleventh Circuit adopted the seven-factor *Dow Corning* test and found that the factors were satisfied under these particular circumstances.[85] Specifically, the court stated that the "releases [were] fair and equitable, and wholly necessary to ensure that [the reorganized debtor] may continue to operate as an entity. This case has been a death struggle, and the non-debtor releases are a valid tool to halt the fight."[86]

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[79] *Id.* at 658 (citing *A.H. Robins Co.*, 880 F.2d at 701-02; *MacArthur Corp.*, 837 F.2d at 92-94; *Cont'l Airlines,* 203 F.3d at 214).
[80] *Seaside Eng'g & Surveying*, 780 F.3d at 1079; *see also Matter of Munford*, 97 F.3d 449, 453-54 (11th Cir. 1996).
[81] *Seaside Eng'g & Surveying*, 780 F.3d 1076.
[82] *See id.* at 1078.
[83] *Id.* (internal quotation omitted).
[84] *Id.* at 1078-79.
[85] *Id.* at 1079 (citing *Dow Corning Corp.*, 280 F.3d at 658).
[86] *Id.* at 1081.

While the Eleventh Circuit has generally approved third-party releases when the *Dow Corning* factors are satisfied, courts within the Eleventh Circuit have had occasion to find a proposed release too broad. In *HWA Properties*, the bankruptcy court declined to enter the requested bar order because it viewed the third-party release of the debtor's principal as granting the principal "what is, in effect, a Chapter 7 discharge when that party has not made full disclosure of his assets and liabilities" in the course of his own bankruptcy proceeding.[87] The bankruptcy court concluded that this proposed release was not fair and equitable, but rather, "a step too far."[88]

D. Bankruptcy Rule 2002(c)(3)

While the Bankruptcy Code does not expressly provide for non-asbestos related third-party releases, Bankruptcy Rule 2002(c)(3) appears to assume that a release may be included in a plan even if the Bankruptcy Code does not expressly provide for such a release. Rule 2002(c)(3) states as follows:

> (3) *Notice of Hearing on Confirmation When Plan Provides for an Injunction.* If a plan provides for an injunction against conduct not otherwise enjoined under the Code, the notice required under Rule 2002(b)(2) shall:
>
> (A) include in conspicuous language (bold, italic, or underlined text) a statement that the plan proposes an injunction;
>
> (B) describe briefly the nature of the injunction; and
>
> (C) identify the entities that would be subject to the injunction.[89]

The Eleventh Circuit recently held that the failure to give notice of a nondebtor, third-party release as required by Bankruptcy Rule 2002(c)(3) was not fatal where the release information was contained in the debtor's plan and disclosure statement.[90] In *In re Le Centre on Fourth, LLC,* the creditor was injured while staying at a hotel which the debtor owned but leased to another company.[91] After the debtor filed for relief under chapter 11, the creditor filed a motion for relief from the stay for the sole purpose of pursuing any liability insurance the debtor had related to the hotel in a pending state court action filed against the lessee, and other related parties.[92] After the bankruptcy court lifted the stay, the debtor filed a disclosure statement which explained that the debtor's proposed plan provided for the release of certain nondebtor entities

[87] *HWA Props., Inc.*, 544 B.R. at 240-43.
[88] *Id.* at 243.
[89] Fed. R. Bankr. P. 2002(c)(3)(A)-(C).
[90] *Jackson v. Le Ctr. on Fourth, LLC (In re Le Ctr. on Fourth, LLC)*, 17 F.4th 1326 (11th Cir. 2021).
[91] *Id*.
[92] *Id.* at 1330.

affiliated with the debtor. The debtor served creditor's counsel with the disclosure statement but did not serve the creditor with notice as required by Rule 2002(c)(3). The debtor's First Amended Disclosure Statement stated that section 105(a) "provided the bankruptcy court with the authority to release non-debtor parties" and made it clear that released parties "would receive a discharge injunction in their favor."[93] The day of the confirmation hearing, the debtor filed a Third Amended Plan, expanding the definition of released parties to include additional parties.[94]

The creditor did not oppose the debtor's plan and the bankruptcy court confirmed the plan, finding that it could approve the third-party releases because they were "integral" to the debtor's reorganization.[95] Then the affiliated nondebtor parties filed a motion to dismiss the creditor's state court tort action on the grounds that the terms of the confirmed plan released them from liability.[96] The creditor responded that he had not received appropriate notice of the plan terms related to the scope of the release in accordance with the Bankruptcy Rules.[97] The bankruptcy court disagreed and approved the motion to dismiss, finding that failure to comply with procedural rules was not necessarily tantamount to a violation of due process.[98] The bankruptcy court also denied the creditor's request to proceed nominally against the nondebtor parties in state court to reach their insurers.[99]

The district court affirmed, explaining that "11 U.S.C. § 105(a) granted the bankruptcy court the power to release non-debtors to further the bankruptcy plan."[100] On appeal to the Eleventh Circuit, the creditor argued that it did not receive notice reasonably calculated to inform him of the third-party releases in the debtor's plan in violation of his due process rights. Pursuant to Rule 2002(c)(3), a "creditor must receive notice that includes a conspicuous statement that the plan proposes a discharge injunction, a brief description of the injunction, and the identity of the entities subject to the injunction."[101] "[T]his notice must be supplied 28 days before the confirmation hearing so that a party can file objections."[102]

There was no dispute that the debtor failed to provide the required procedural notice.[103] Nevertheless, the Eleventh Circuit rejected the creditor's due process arguments, explaining that the creditor's counsel had both actual knowledge of the case as well as the release language contained in the plan.[104] The Court of Appeals found the Supreme Court's *Espinosa* opinion

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[93] *Id.* at 1331.
[94] *Id.*
[95] *Id.*
[96] *Id.* at 1332.
[97] *Id.*
[98] *Id.*
[99] *Id.* at 1332-33.
[100] *Id.* at 1333.
[101] *Id.* at 1334.
[102] *Id.*
[103] *Id.*
[104] *Id.* at 1334-36.

instructive given that both cases deal with procedural notice requirements.[105] The Eleventh Circuit noted that the creditor's position differed slightly from *Espinosa*, which involved the discharge of a student loan debt in a chapter 13 plan, in that the creditor in this case waived any claim against the bankruptcy estate when the bankruptcy court lifted the stay to allow the creditor to proceed in state court.[106] The creditor argued that this gave his attorney less incentive to read the debtor's disclosure statement, but the Eleventh Circuit stated that the "law is clear that a bankruptcy court can issue non-debtor releases in bankruptcy restructuring plans."[107] Thus, "the bankruptcy court retained the authority to impact [the creditor's] rights against third parties despite his waiver of claims against the bankruptcy estate."[108]

PART II—THE QUESTION OF SUBJECT MATTER JURISDICTION

Assuming a court finds that a bankruptcy (or district) court has statutory or residual authority to issue nondebtor, third-party releases under the Bankruptcy Code, the court must still consider whether the subject injunction or release is a proper exercise of federal subject matter jurisdiction. Conceptually, this is the first question a court must address, not the second, but it is somewhat less controversial—i.e., most courts acknowledge that bankruptcy courts have subject matter jurisdiction to enjoin third-party claims provided the claims will impact the bankruptcy estate. However, it is difficult to define the outer limits of a bankruptcy court's subject matter jurisdiction to enjoin third-party claims with precision, as the inquiry is both fact specific and circuit specific. Importantly, section 105 is not an independent source of federal jurisdiction, and the exercise of a bankruptcy court's equitable powers under section 105 cannot exceed the scope of the bankruptcy court's subject matter jurisdiction. Of course, factors considered by courts, like those enumerated in *Dow Corning*, often bear on whether the issuance of the injunction is an appropriate exercise of federal subject matter jurisdiction.[109]

Federal courts' bankruptcy subject matter jurisdiction derives from 28 U.S.C. § 1334. Section 1334(a) gives district courts original and exclusive jurisdiction of all cases under title 11. Section 1334(e) gives the district court in which a case under title 11 is commenced or is pending "exclusive jurisdiction . . . of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate." Section 1334(b) outlines three categories of proceedings over which district courts have "original but not exclusive jurisdiction," including: (1) civil proceedings "arising under title 11;" (2) civil proceedings "arising in . . . cases under title 11;" and (3) civil proceedings "related to cases under title 11." A district court may refer all cases under title 11, as well as proceedings arising in or under title 11 or related to a case

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[105] *Id.* at 1335.
[106] *Id.* at 1334-35.
[107] *Id.* at 1335, n.4.
[108] *Id.*
[109] *See* Joshua M. Silverstein, *Overlooking Tort Claimants' Best Interests: Non-Debtor Releases in Asbestos Bankruptcies*, 78 UMKC L. REV. 1 (2009).

under title 11, to a bankruptcy court, but the bankruptcy court's subject matter jurisdiction in such cases and proceedings is derivative of, and dependent upon, that of the district court.[110]

Broadly speaking, a bankruptcy court must have at least "related to" subject matter jurisdiction under section 1334(b) to enjoin or release suits involving third-parties.[111] The majority view is that "[a]n action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate."[112]

Explaining Second Circuit precedent, the district judge in *Purdue Pharma* concluded that section 1334(b) does not require that "an action's outcome will certainly have, or even that it is likely to have, an effect on the *res* of the estate…It is, rather, whether it *might have any conceivable impact* on the estate."[113] Judge McMahon went on to state, "in this Circuit, it is well settled that the only question a court need ask is whether 'the action's outcome *might have* any conceivable effect on the bankrupt estate.' If the answer to that question is yes, then related to jurisdiction exists—no matter how implausible it is that the action's outcome actually will have an effect on the estate."[114]

Notably, some courts have invoked a bankruptcy court's *in rem* jurisdiction under section 1334(d), not a bankruptcy court's "related to" jurisdiction under section 1334(b), as the source of a bankruptcy court's subject matter jurisdiction to enjoin nondebtor, third-party claims. In a 1988 opinion, the Second Circuit considered the jurisdiction of the Johns-Manville bankruptcy court to enjoin actions by certain third-party distributors of Johns-Manville's asbestos products against

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[110] *See* 28 U.S.C. § 157(a).

[111] *See, e.g.*, *Celotex Corp. v. Edwards*, 514 U.S. 300, 307-09 (1995).

[112] *Id.* at 308, n.6 (quoting *Pacor, Inc. v. Higgins*, 743 F.2d 984 (1984) and collecting cases); *see also Miller v. Kemira, Inc. (Matter of Lemco Gypsum, Inc.)*, 910 F.2d 784, 788 (11th Cir. 1990) (explaining that the test for determining whether a proceeding is "related to bankruptcy" is "whether the outcome of the proceeding could conceivably have an effect on the estate being administered in bankruptcy."). The Second Circuit's "significant connection" test also turns on whether the outcome of a proceeding would have a "conceivable effect" on the bankruptcy estate. *See In re Adelphia Commc'ns Corp.*, 285 B.R. 127, 137 (Bankr. S.D.N.Y. 2002) (citing *In re Cuyahoga Equip. Corp.*, 980 F.2d 110 (2d Cir. 1992)).

[113] *Purdue Pharma, L.P.*, 635 B.R. at 83 (emphasis in original).

[114] *Id.* at 85 (internal citation omitted) (emphasis in original). The District Court ultimately concluded, following a thorough analysis, that the to-be-released claims might have some conceivable effect on the estate (and, in fact, "likely *will* have such an impact") such that the claims fell within the "related to" jurisdiction of the bankruptcy court. *Id.* at 85-89 (emphasis in original). In the case of *Purdue Pharma*, the district court noted that the non-derivative third-party claims were the type of claims that affect distribution of estate property, given that continued litigation against the Sacklers stood to "destroy[] all of the interlocking intercreditor settlements enshrined in the plan." *Id.* at 85 (internal citation omitted). The district court also credited the fact that the claims raised against the Sacklers threatened to affect the amount available to other creditors for distribution. *Id.* at 85-86. The district court discussed the high degree of interconnectedness among the lawsuits against the debtors and the Sacklers and the possibility that the debtor's litigation over the question of its indemnification obligations would further burden the assets of the estate. *Id.* at 86-89. Tallying these factors, Judge MacMahon concluded "I must and I do find that the claims asserted against the Shareholder Released Parties *might have* some conceivable effect on the estate of a debtor . . . and thus fall within the 'related to' jurisdiction of the Bankruptcy Court."). *Id.* at 89 (emphasis in original).

settling insurers.[115] The distributors claimed to be coinsured under the Johns-Manville insurance policies by virtue of "vendor endorsements" contained therein and challenged the bankruptcy court's channeling injunction on jurisdictional grounds (among other things).[116] Invoking the bankruptcy court's *in rem* jurisdiction under section 1334(d)—not the court's section 1334(b) "related to" subject matter jurisdiction—the Second Circuit concluded the subject policies and policy proceeds were property of the estate, and the distributor's rights therein were entirely derivative of the debtor's rights.[117] Thus, by virtue of the bankruptcy court's *in rem* jurisdiction, the circuit court concluded that the bankruptcy court had jurisdiction to approve Johns-Manville's settlement with its insurers and to channel claims arising under the policies to the proceeds of the settlement.[118] It is significant that the court considered the third-party claims against the debtor's insurers as derivative claims to the *res* of the debtor's estate (the policy proceeds), not *in personam* claims against a nondebtor.[119]

More than two decades after the bankruptcy court confirmed the Johns-Manville plan, the Second Circuit again took up the question of whether the channeling injunction in the 1986 Johns-Manville confirmation order constituted an appropriate exercise of federal subject matter jurisdiction.[120] The litigation involved direct claims of third-parties asserted against a Johns-Manville insurer (unrelated to the policy proceeds) for the insurer's own alleged wrong-doing.[121] The claimants challenged a clarifying order entered by the bankruptcy court, which prompted the Second Circuit to consider whether the 1986 confirmation order exceeded the limits of the bankruptcy court's subject matter jurisdiction.[122] The Second Circuit held that the bankruptcy court lacked even "related to" subject matter jurisdiction to enjoin direct, third-party claims against the debtor's insurer for its alleged, independent wrongdoing, reasoning that the subject third-party claimants raised no claims to the debtor's insurance coverage, aimed to proceed against the nondebtor third-party's assets, made no claim against an asset of the bankruptcy estate for the claims, and their actions did not affect the estate.[123] The Second Circuit went on to conclude that neither shared facts between the subject third-party action and the debtor's relationship to the insurer, nor the insurer's financial contribution to the reorganization, were sufficient to give the bankruptcy court subject matter jurisdiction over the subject nondebtor, third-party claims.[124]

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[115] *MacArthur Co.*, 837 F.2d at 89.
[116] *Id.* at 90-91.
[117] *Id.* at 91-93.
[118] *Id.*
[119] *Id.* at 92-93; s*ee also* Ralph Brubaker, *Bankruptcy Injunctions and Complex Litigation: A Critical Reappraisal of Non-Debtor Releases in Chapter 11 Reorganizations*, 1997 U. ILL. L. REV. 959, 1037-38 (1997) (criticizing the notion that section 1334's *in rem* jurisdiction provision gives a bankruptcy court subject matter jurisdiction to enjoin collateral *in personam* actions).
[120] *See In re Johns-Manville Corp.*, 517 F.3d 52, 65 (2d Cir. 2008), *rev'd and remanded on other grounds sub nom. Travelers Indem. Co. v. Bailey*, 557 U.S. 137 (2009).
[121] *Id.* at 63.
[122] *Id.* at 60-61.
[123] *Id.* at 65.
[124] *Id.* at 66-68.

Echoing concerns articulated by the Third Circuit in *Combustion Engineering*,[125] the Second Circuit opined that parties cannot create subject matter jurisdiction by structuring plans in such a way as to depend upon third-party contributions.[126] The United States Supreme Court reversed the Second Circuit, on res judicata grounds, without reaching the jurisdictional question.[127]

In a more recent case, *In re Millennium Lab Holdings II, LLC*, [128] the Third Circuit Court of Appeals took a more expansive view federal bankruptcy jurisdiction, holding the bankruptcy court had "core" jurisdiction (see discussion below), not merely "related to" jurisdiction, to release and enjoin direct claims of the debtors' creditors against certain of the debtors' equity security holders, who had agreed to contribute $375 million to the debtors' reorganization in consideration of the third-party releases.[129] Finding "the deal to avoid corporate destruction would not have been possible without the third-party releases,"[130] the court concluded that the bankruptcy court had jurisdiction (and constitutional authority) to adjudicate the nondebtor claims because the resolution of the claims was a matter "integral to the restructuring of the debtor-creditor relationship." Stated succinctly, the court reasoned that without the third-party contributions there would be no reorganization and, conversely, there would be no third-party contributions (negotiated pre-bankruptcy) without the releases.[131] In other words, third-party funding sources, like insurance policy proceeds, can be an important asset to preserve for ratable distribution in bankruptcy.[132]

Ultimately, is undoubtedly true that "related to" jurisdiction encompasses "suits between third parties which have an effect on the bankruptcy estate. "[133] However, not all third-party suits that implicate a defendant's relationship with a chapter 11 debtor will (necessarily) impact a bankruptcy estate.

PART III—THE ARTICLE III ADJUDICATION QUANDARY

A wholly separate question from that of subject matter jurisdiction is whether a bankruptcy court has authority to enjoin or release a claim over which the bankruptcy court would lack final judgment adjudicatory authority absent litigant consent. As discussed above, in 28 U.S.C. § 157(a), Congress provided that district courts could refer three types of proceedings, echoed in section 1334(b), to bankruptcy courts. District courts retain the authority to withdraw the reference to the bankruptcy court, in whole or in part.[134] Proceedings that "arise under" or "arise in" a title

[125] *See In re Combustion Eng'g, Inc.*, 391 F.3d 190, 228 (3d Cir. 2004).
[126] *In re Johns-Manville Corp.*, 517 F.3d at 66.
[127] *See generally Travelers Indem. Co.*, 557 U.S. at 137.
[128] *See Millennium Lab Holdings, II,* 945 F.3d at 126.
[129] *Id*. at 137-38.
[130] *Id*. at 132.
[131] *Id*. at 133-40.
[132] *See, e.g.*, Brady & Salerno, *supra* n.5, at 30-31.
[133] *See Celotex Corp*., 514 U.S. at 308, n.5.
[134] *See Ascena Retail*, 636 B.R. at 666.

11 case are known as core proceedings, while proceedings that are "related to" a title 11 case are non-core.[135] The distinction of whether a proceeding is core or non-core is important because bankruptcy courts lack statutory authority to enter final judgments in non-core, "related to" proceedings (absent consent), and, even if a matter is statutorily designated as core, the bankruptcy court (as a non-Article III court) may lack final judgment adjudicatory authority (absent litigant consent) if the litigants have a constitutional entitlement to an Article III adjudication.[136]

In examining third-party releases, courts recognize the clash between a bankruptcy court's statutory and constitutional authority to confirm a plan of reorganization—a summary matter of bankruptcy estate and case administration that implicates the non-Article III bankruptcy power (for which Congress can establish uniform laws under Article I of the Constitution)[137]—and a bankruptcy court's lack of final judgment adjudicatory authority in a traditional plenary suit against an adverse claimant (e.g., "a disputed cause of action [for money damages] against a third party or for tangible property held under a substantial claim of right by a third party")[138]—absent the litigants' consent.[139] In many instances, the nondebtor, third-party claims to be released will, by nature, be "the subject of a suit at the common law, or in equity, or admiralty."[140] (Of course, many of the claims against a debtor's bankruptcy estate also would be plenary in nature but for the bankruptcy.)

The *Purdue Pharma* bankruptcy court reasoned that the nonconsensual, third-party releases approved in the plan were an exercise of the court's "constitutionally core" authority under *Stern* because confirmation of a chapter 11 plan is a "fundamentally central aspect of a Chapter 11 case's adjustment of the debtor/creditor relationship."[141] The district court overruled the bankruptcy court on the ground that "nothing in *Stern* or any other case suggests that a party otherwise entitled to have a matter adjudicated by an Article III court forfeits that constitutional right if the matter is disposed of as part of a plan of reorganization in bankruptcy."[142] Taken to

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[135] *Purdue Pharma, L.P.*, 635 B.R. at 79.
[136] *Id.* at 79-80; *see Stern*, 564 U.S.at 462; *Ascena Retail*, 636 B.R. at 666, 668 ("Congress has attempted to align the responsibilities of bankruptcy judges with the boundaries set by the Constitution. However . . . the Supreme Court has found that Congress violated Article III in authorizing bankruptcy judges to decide certain claims for which litigants enjoy an entitlement to an Article III adjudication."). For a discussion of whether the parties' consent to a final judgment adjudication by a non-Article III bankruptcy court cures the constitutional violation, *see* Ralph Brubaker, *Non-Article III Adjudication: Bankruptcy and Nonbankruptcy, with and without Litigant Consent*, 33 EMORY BANKR. DEV. J. 11, 26-28 (2016).
[137] *See generally* Brubaker, *supra* note 136 (discussing "summary" matters historically understood to fall within the non-Article III bankruptcy power and "plenary" suits (in law, equity, or admiralty) historically understood to fall within the Article III judicial power).
[138] *Id.* at 76.
[139] *See id.* at 36.
[140] *Id.* at 15, 58.
[141] *Purdue Pharma L.P.*, 633 B.R. at 99-100.
[142] *Purdue Pharma L.P.*, 635 B.R. at 80.

logical extremes, Judge McMahon worried that parties could manufacture the bankruptcy court's authority to adjudicate non-core matters by simply inserting them into a plan of reorganization.[143]

The *Purdue Pharma* district court construed *Stern v. Marshall* as requiring the court to analyze whether the release/injunction "stem from the bankruptcy itself or would necessarily be resolved in the claims allowance process—not whether the release and injunction are 'integral to the restructuring of the debtor-creditor relationship.'"[144] Judge McMahon went on to conclude that the third-party claims released by the *Purdue Pharma* plan and confirmation order "neither stem from Purdue's bankruptcy nor [could] they be resolved in the claims allowance process," and yet were extinguished without the third-parties' consent and without any payment simply by inclusion of the release of non-core claims in a plan of reorganization.[145] The district court also reasoned that "[a] bankruptcy court's order extinguishing a non-core claim and enjoining its prosecution without an adjudication on the merits 'finally determines' that claim."[146] As such, Judge McMahon determined that, for the bankruptcy court to enter an order releasing a third-party's non-core claim, the parties must consent to the bankruptcy court's jurisdiction.[147] Absent such consent, Judge McMahon concluded that a bankruptcy court lacks constitutional authority to enter an order finally approving such nonconsensual releases and injunctions.[148] Although the *Purdue Pharma* district court struck down the third-party releases as an unconstitutional non-Article III adjudication without litigant consent, the *Purdue Pharma* court left open the possibility that the bankruptcy court could tender proposed findings of fact and conclusions of law, which the district court could review *de novo*.[149]

Issued shortly after the *Purdue Pharma* decision, the *Ascena Retail* court also struck down third-party releases "[t]he sheer breadth of [which] can only be described as shocking," as the proposed provision released claims of "*at least* hundreds of thousands of potential plaintiffs not involved in the bankruptcy, shielding an incalculable number of individuals associated with [the] Debtors in some form, from every conceivable claim—both federal and state claims—for an unspecified time period stretching back to time immemorial."[150] Discussing the bankruptcy court's constitutional authority to approve such a release, the district court cautioned, "*Stern* teaches that courts should focus on the content of the proceeding rather than the category of the proceeding when determining whether a bankruptcy court has acted within its constitutional authority."[151]

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[143] *Id*.
[144] *Id.* at 81 (internal citation omitted).
[145] *Id*.
[146] *Id.* at 82.
[147] *Id.*; *see Stern*, 564 U.S. at 484.
[148] *Purdue Pharma, L.P.*, 635 B.R. at 82.
[149] *Id.*; *see also* 11 U.S.C. §157(c)(1); *Stern*, 564 U.S. at 475.
[150] *Ascena Retail*, 636 B.R. at 655.
[151] *Id.* at 669.

The *Ascena Retail* opinion went on to state that the bankruptcy court must properly classify the claims to be released as statutorily and constitutionally "core" or "non-core" to assess the court's authority to release the claim without consent.[152] The court stressed that this is a claim by claim analysis that asks whether the to-be-released claims stem from the bankruptcy itself or would necessarily be resolved by the claims-allowance process in bankruptcy.[153] The court explained:

> The Bankruptcy Court did not parse the content of the claims that it purported to release to determine if each claim constituted a core claim, a non-core claim or a claim unrelated to the bankruptcy case. The sheer breadth of the Third-Party Releases renders this a herculean undertaking and underscores the constitutional questionability of the Bankruptcy Court's actions. However, the enormity of the task does not absolve the Bankruptcy Court of its responsibility to properly identify the content of the claims before it and ensure that it has jurisdiction to rule on each of them. In fact, because of the constitutional implications of extinguishing these claims, this undertaking carries even greater import. As an appellate court, this Court will not speculate as to the claims released and then parse each purportedly released claim to determine whether the Bankruptcy Court had the power to extinguish that claim—that was the responsibility of the Bankruptcy Court. *In re Continental Airlines*, 203 F.3d 203, 214 (3d Cir. 2000) ("The hallmarks of permissible non-consensual releases—fairness, necessity to the reorganization, and specific factual findings to support these conclusions—are all absent here."). The sheer breadth of the releases and the lack of findings with respect to each released claim renders appellate review virtually impossible and speaks to the impropriety of the approval of the Third-Party Releases.[154]

The district courts' conceptions of "core" jurisdiction in *Purdue Pharma* and *Ascena Retail* are notably narrower than those of other courts. For instance, in *Millennium Lab Holdings*, the Third Circuit expressly rejected the notion that the "*Stern* Court meant its 'integral to the restructuring' language to be limited to the claims-allowance process," explaining that "the reason bankruptcy courts may adjudicate matters arising in the claims-allowance process is because those matters are integral to the restructuring of debtor-creditor relations, not the other way around."[155]

Moreover, a question exists as to whether an injunction or release is the equivalent of a final judgment adjudication implicating the Article III judicial power. At least one court has upheld nonconsensual third-party releases in a proposed plan because the court disagreed with the idea that such releases were "the equivalent of a discharge" or a ruling on the merits of the claim

[152] *Id.* at 668.
[153] *Id.* at 668-69.
[154] *Id.* at 669.
[155] *Millennium Lab Holdings, II*, 945 F.3d at 138.

being released.[156] And, the Second Circuit, in 1988, opined that third-party's derivative claims against a debtor's insurers were not "extinguished," but merely "channeled away from the insurers and redirected to the proceeds" of the debtor's settlement with the insurers.[157] However, with respect to the direct claims of third-parties against the debtor's insurers, the Second Circuit was less sanguine concerning the adjudicatory nature of third-party releases: "In form, it is a release; in effect, it may operate as a bankruptcy discharge arranged without a filing and without the safeguards of the Code."[158]

Consider the dissent of Justice Stevens in the *Celetox* case (joined in by Justice Ginsberg):

> The unambiguous text of § 157(c)(1) requires that the bankruptcy judge's participation in related proceedings be merely advisory rather than adjudicative. In my view, having jurisdiction to grant injunctions over cases that one may not decide is inconsistent with such an advisory role. An injunction is an extraordinary remedy whose impact on private rights may be just as onerous as a final determination. The constitutional concerns that animate the current jurisdictional provisions of the Bankruptcy Code and that deny non-Article III tribunals the power to determine private controversies apply with equal force to the entry of an injunction interfering with the exercise of the admitted jurisdiction of an Article III tribunal.[]
>
> In sum, my view on the sufficiency of "related to" jurisdiction to sustain the injunction in this case can be stated quite simply: If a bankruptcy judge lacks jurisdiction to "determine" a question, the judge also lacks jurisdiction to issue an injunction that prevents an Article III court, which concededly does have jurisdiction, from determining that question.[] Any conclusion to the contrary would trivialize the constitutional imperatives that shaped the Bankruptcy Code's jurisdictional provisions.[][159]

In response to the dissent, the majority emphasized that the subject injunction amounted to an interlocutory stay, not a final order or judgment, and also that the respondents waived any claim that the injunction proceedings were non-core.[160]

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[156] *See Mallinckrodt*, 2022 WL 404323, at *14, n.70 (citing authority from the Bankruptcy Court for the District of Delaware).
[157] *MacArthur Co.*, 837 F.2d at 91.
[158] *Johns-Manville Corp.*, 517 F.3d at 66 (quoting *Metromedia Fiber Network, Inc.*, 416 F.3d at 142).
[159] *Celotex Corp.*, 514 U.S. at 322–24.
[160] *Id.* at 309, n.7. It bears mention that, if a plan proposes to pay nondebtor, third-party claims and conditions the permanence of the injunction of the nondebtor, third-party claims on timely plan completion (leaving open the possibility of recovery against the nondebtor if the debtor fails to satisfy the plan), the injunction is arguably "non-adjudicatory."

One scholar has observed that "jurisdiction to temporarily stay an action is not dependent upon jurisdiction to adjudicate the parties' controversy."[161] Conversely,

> In the case of a permanent non-debtor release and injunction, however, the distinction between jurisdiction to enjoin and jurisdiction to adjudicate disappears, because the injunction *does* adjudicate. A non-debtor release is not a mere status quo injunction; a non-debtor release effectively adjudicates the released non-debtor action. The release operates as an adjudication on the merits, fully binding for res judicata/preclusion purposes.[162]

In other words, if the bankruptcy court's authority to permanently enjoin proceedings on a third-party claim against a nondebtor is dependent on the court's non-core, "related to" subject matter jurisdiction to adjudicate the litigants' controversy, it is certainly arguable that the court's power to permanently enjoin the third-party's claim depends on the claimant's consent to a non-Article III adjudication (i.e., a voluntary relinquishment of the Constitutional right to final adjudication by an Article III tribunal).[163] Where, however, the non-Article III adjudication is a function of the court's "core" jurisdiction, the litigant's consent to a non-Article III adjudication is not necessary.

In sum, where the hallmarks of a permissible nonconsensual release are present—e.g., fairness, necessity to a reorganization, etc.—approval of the release may be subject to characterization as "core," even though the release amounts to a final adjudication of an otherwise "plenary" suit by a non-Article III tribunal. Further, where the concern is that the release is merely an exercise of the bankruptcy court's non-core, "related to" jurisdiction, the bankruptcy court's lack of final judgment adjudicatory authority does not foreclose approval of the release; it simply necessitates evaluation of whether the parties to such "plenary" suit have consented to the non-Article III adjudication (i.e., waived their right to adjudication by an Article III tribunal).

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[161] *See* Ralph Brubaker, *Bankruptcy Injunctions and Complex Litigation: A Critical Reappraisal of Non-Debtor Releases in Chapter 11 Reorganizations*, 1997 U. ILL. L. REV. 959, 1065-67 (1997) ("Under the 1898 Act, status quo injunctions for the preservation of the estate (including protection of a reorganization endeavor) were so intimately connected to administration of the estate that they were within the summary jurisdiction of courts of bankruptcy (including referees), even with respect to actions that could be adjudicated only through a plenary suit.[] Likewise, under the current jurisdictional scheme, a temporary non-debtor stay, premised upon preservation of a debtor's reorganization effort, is properly considered a core 'matter[] concerning the administration of the estate,'[] even though the action being stayed is outside the bankruptcy court's core jurisdiction to adjudicate. Such a status quo injunction could well be considered a proceeding 'arising under' the Bankruptcy Code, because the authority to issue such an injunction comes from section 105 of the Bankruptcy Code. Alternatively, the non-debtor stay is a proceeding uniquely 'arising in' the bankruptcy reorganization case that has no separate existence absent the reorganization proceedings.[] Even though the collateral non-debtor suit is one with an existence independent of the bankruptcy proceedings, a temporary stay of the non-debtor action does not involve the sort of adjudication of an independent action that motivated the *Marathon* holding and the subsequent core/non-core dichotomy.[] The bankruptcy proceeding to stay the non-debtor action is distinct from the collateral non-debtor litigation itself, as is the jurisdictional basis for each proceeding, and a temporary non-debtor stay issued by a bankruptcy court is properly considered a core proceeding.")

[162] *Id.* at 1069–70 (emphasis in original).

[163] Whether and how a bankruptcy court can obtain such consent in connection with a chapter 11 plan confirmation hearing is beyond the scope of this paper.

CONCLUSION

Ultimately, whether third-party releases/injunctions are permitted by the Bankruptcy Code (other than under section 524(g)),whether district courts (and, by reference, bankruptcy courts) have subject matter jurisdiction to issue such injunctions in connection with a bankruptcy case, and whether bankruptcy courts have the requisite statutory and constitutional authority to issue third-party injunctions/releases, are important preliminary questions that are often fact-specific and circuit-specific. Of course, there is always the prospect that future legislation will impact the relief that may be afforded in bankruptcy.[164] Moreover, the aforementioned issues pertaining to nondebtor, third-party releases are the tip of the proverbial iceberg. Due process considerations, determinations as to whether future claimants are "creditors", and other confirmation requirements (like the best interests of creditors test) will inform how the plan is structured, the requisite notice of the plan, and whether the plan is ultimately confirmable. Such issues are beyond the scope of this paper, but they present difficult and, in some jurisdictions, unsettled questions in their own right.

[164] In July 2021, certain members of Congress introduced the Nondebtor Release Prohibition Act of 2021 (the "Act") which would amend the Bankruptcy Code to prohibit the nonconsensual release of a nondebtor's liability to an entity other than the debtor. The proposed legislation would generally prohibit a bankruptcy court from approving nonconsensual, third-party releases in connection with confirmation of a chapter 11 plan or enjoining a judicial proceeding or other act to collect or otherwise enforce such a claim or cause of action against a nondebtor. The bill would, however, permit third-party releases if express consent is given by the third-party. In November 2021, H.R. 4777 was ordered reported by the Committee on the Judiciary with no further activity reported since.