

The Changing Landscape of Consensual Third-Party Releases in Chapter 11 Plans:

Does Silence = Consent?

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This article examines the statutory framework underlying consensual third-party releases and then discusses recent cases in which consensual releases have been challenged by the Office of the United States Trustee (“U.S. Trustee”) and by courts *sua sponte*. We conclude with practice pointers to support the case for confirmation of chapter 11 plans containing consensual third-party releases.²

Statutory and Legal Framework

Although debtors obtain a discharge of their liabilities upon confirmation of a plan of reorganization, section 524(e) of the Bankruptcy Code specifically provides that the discharge “does not affect the liability of any other entity on, or the property of any other entity for, such [pre-confirmation] debt.”³ Accordingly, the discharge of the debtor’s pre-confirmation debts under the Bankruptcy Code in no way affects the liability of any other entity, such as a non-debtor guarantor, for example. A third-party release in a plan, however, has an effect similar to the discharge by releasing non-debtor entities from liabilities related to a debtor.

Some courts, specifically the Ninth⁴ and Tenth Circuits,⁵ have expressly rejected any third-party releases in a plan of reorganization, regardless of the factual context, based on section 524(e). Under section 105(a) of the Bankruptcy Code, however, the bankruptcy court has broad equitable powers to issue any order, process or judgment necessary or appropriate to carry out the provisions of the Bankruptcy Code.⁶ Many other courts have concluded that section 105(a) provides the requisite statutory authority for approval of a release of claims against non-debtor third parties in a plan.

With section 105(a) serving as the statutory predicate, these courts⁷ analyze first whether parties explicitly or implicitly consented to the release and then weigh multiple other factors,

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² The more rigorous standards for approval of non-consensual third-party releases will not be addressed in this article.

³ 11 U.S.C. § 524(e).

⁴ *In re Am. Hardwoods, Inc.*, 885 F.2d 621, 626 (9th Cir. 1989) (holding that section 524(e) limits the court’s equitable power under section 105 to order the discharge of the liabilities of nondebtors); *Resorts Int’l, Inc. v. Lowenschuss (In re Lowenschuss)*, 67 F.3d 1394, 1401 (9th Cir. 1995) (“This court has repeatedly held, without exception, that § 524(e) precludes bankruptcy courts from discharging the liabilities of non-debtors”); *Underhill v. Royal*, 769 F.2d 1426, 1432 (9th Cir. 1985) (“[T]he bankruptcy court has no power to discharge the liabilities of a nondebtor pursuant to the consent of creditors as part of a reorganization plan.”).

⁵ *In re W. Real Estate Fund, Inc.*, 922 F.2d 592, 600-02 (10th Cir. 1990) (concluding “obviously it is the debtor, who has invoked and submitted to the bankruptcy process, that is entitled to its protections; Congress did not intend to extend such benefits to third-party bystanders”).

⁶ 11 U.S.C. § 105(a).

⁷ See, e.g., *Deutsche Bank AG v. Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005); *In re Specialty Equip. Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1992). See *In re Continental Airlines*, 203 F.3d 203, 214, n.11 (3d Cir. 2000); *In re Spansion, Inc.*, 426 B.R. 114, 144 (Bankr. D. Del. 2010), discussing *Continental*, 203 F.3d at 213-214.

including whether the provisions (1) are integral to the agreement among the various parties in interest and are essential to the formulation and implementation of the plan, (2) confer substantial benefits on the debtor's estate, (3) are fair, equitable and reasonable and (4) are in the best interests of the debtor, its estate and parties in interest.⁸ In essence, when these courts are satisfied that there is either explicit or implicit consent, they use their broad equitable powers under section 105(a) "for the greater good" of protecting third-parties and approve the consensual release.

An Analysis of Recent Decisions and Challenges to Third-Party Releases

The clearest case of a consensual release occurs when a party votes in favor of the plan and does not exercise an express option on the ballot to opt out of the release. Courts typically have also found implicit consent in broader circumstances, such as: (1) holders of unimpaired claims not timely objecting to the releases, (2) holders of impaired claims not voting or not opting out of or otherwise objecting to the releases, and (3) holders of impaired claims voting to reject the plan but not opting out of or otherwise objecting to the releases.⁹ In several recent cases, however, the scope of implicit consent to third-party releases has been challenged.

A. Delaware Decisions

Orchard

In *In re Orchard Acquisition Company, LLC*,¹⁰ the U.S. Trustee objected to the debtors' prepackaged plan of reorganization, which deemed unimpaired creditors to have consented to third-party releases, on the basis that such releases were non-consensual and accordingly impaired the legal, equitable and contractual rights of unimpaired creditors in contravention of section 1124 of the Bankruptcy Code.¹¹ The U.S. Trustee argued that the releases were not consensual because unimpaired creditors would have been required to file an objection to confirmation to avoid granting the releases,¹² and the cost and effort of hiring an attorney to object might dissuade creditors from raising objections. The U.S. Trustee also argued that the debtors described the release and procedures to object in a confusing manner, and as a result, it was plausible that the unimpaired creditors remained silent because they did not understand the notice and their obligations thereunder.¹³

Another prong of the U.S. Trustee's objection was that the third-party releases impaired the unimpaired creditors because the releases were effective immediately upon the effective date of the plan, rather than when the creditors later received full payment of their claims in the

⁸ See *In re Paragon Offshore PLC, et al.*, 2016 Bankr. LEXIS 3967, at 26 (Bankr. D. Del. Nov. 15, 2016).

⁹ *Paragon*, 2016 Bankr. LEXIS 3967, at *26-27.

¹⁰ *In re Orchard Acquisition Co., et al.*, No. 17-12914 (Bankr. D. Del. 2018) (KG). Simpson Thacher & Bartlett LLP was counsel to the debtors in these chapter 11 cases.

¹¹ United States Trustee's Objection to Confirmation of the Joint Pre-Packaged Plan of Reorganization of Orchard Acquisition Company, LLC and its Debtor Affiliates at 2, *In re Orchard Acquisition Co., et al.*, No. 17-12914 (Bankr. D. Del. 2018) [Docket No. 126].

¹² *Id.* at 7.

¹³ Transcript of Hearing at 25-26, *In re Orchard Acquisition Co., et al.*, No. 17-12914 (Bankr. D. Del. Jan. 17, 2018).

ordinary course from the reorganized debtors.¹⁴ According to the U.S. Trustee, an immediately effective release of a third-party granted by unimpaired creditors “affected the liability” of another entity on the debtor’s debt and therefore violated section 524(e) of the Bankruptcy Code.¹⁵ The U.S. Trustee maintained this objection even after the debtors amended the plan of reorganization to make clear that the unimpaired creditors’ claims would not be released *vis-à-vis the reorganized debtors* until paid in full and to preserve expressly any rights against non-debtor affiliates to the extent such affiliates were contractually liable to the unimpaired creditors along with the reorganized debtors.¹⁶

The bankruptcy court ultimately sided with the debtors and determined that the third-party releases were indeed consensual and properly effective *vis-à-vis third-parties* as of the effective date of the plan with the narrow modification described above. The bankruptcy court found that the form of the notice that was distributed to all known unimpaired creditors was clear regarding the scope of the releases and the means by which a creditor could object. Because there was not a single objection, formal or informal, to the plan or the releases (apart from the U.S. Trustee’s) and the claims of unimpaired creditors would be paid in full in the ordinary course, the bankruptcy court concluded that it was appropriate on the facts to find that silence signified consent.

Regarding the U.S. Trustee’s objection to the timing of the effectiveness of the releases, the bankruptcy court was persuaded by the debtors and their secured lenders that it would be unfair for the secured lenders to equitize their debt as of the effective date but not obtain at the same time the benefit of releases from unimpaired creditors whose unimpaired treatment the secured lenders had made possible by agreement with the debtors.¹⁷ The bankruptcy court also concluded that the releases were essential to the plan, and that if the releases were not approved, the entire restructuring that the parties had negotiated for months might unravel.¹⁸

Orchard Acquisition presented fairly unique facts, and Judge Gross might have reached a different conclusion under different circumstances. Significantly, the plan in *Orchard Acquisition* had unanimous support from all voting creditors and voting equity holders at a partnership debtor below the public company, and the U.S. Trustee’s objection was confined to unimpaired claims. Notably, Judge Gross remarked that his thinking on third-party releases has “evolved.”¹⁹ He explained that “on most of the cases cited in support of releases, my initials

¹⁴ United States Trustee’s Objection, *supra* note 11, at 5.

¹⁵ *Id.* at 6.

¹⁶ Notice of Filing of Amended Joint Pre-Packaged Plan of Reorganization of Orchard Acquisition Company, LLC and its Debtor Affiliates at 23, *In re Orchard Acquisition Co., et al.*, No. 17-12914 (Bankr. D. Del. 2018) [Docket No. 135].

¹⁷ Because the secured lenders were fully equitizing their debt under the plan, they advocated strongly for the debtors to emerge from bankruptcy with a clean slate. Transcript of Hearing, *supra* note 13, at 46-47. The shareholders in the public company debtor were deemed to have rejected the plan and were removed as both releasing parties and released parties in the final version of the plan. Amended Joint Pre-Packaged Plan of Reorganization of Orchard Acquisition Company, LLC and its Debtor Affiliates, dated January 18, 2018 [Docket No. 154].

¹⁸ Transcript of Hearing, *In re Orchard Acquisition Co., LLC, et al.*, *supra* note 13, at 67.

¹⁹ *Id.* at 66.

appear.... And my thinking on the matter has evolved to the point that I don't recognize all releases at this point...."²⁰ His remarks are consistent with the increasing scrutiny of implicit consent in the context of third-party releases.

Rand Logistics

The Department of Justice ("DOJ") on behalf of the United States and the U.S. Trustee were the only parties objecting to confirmation in the recent prepackaged case of *In re Rand Logistics, Inc.*,²¹ a case with only one class of creditors entitled to vote and only one creditor in that class.²² While both objectors raised some of the same arguments, the DOJ focused on aspects of the plan that could adversely affect the rights and potential claims of the United States and its agencies,²³ and the U.S. Trustee challenged the third-party releases as non-consensual and contended that unimpaired creditors were in fact impaired by the plan releases, injunctions, discharge and asset vesting provisions that would take effect on the effective date, similar to the arguments raised in *Orchard*.²⁴ Under the plan, the third-party releases were provided by (i) holders of claims voting to accept the plan, (ii) holders of unimpaired claims and (iii) holders of claims entitled to vote that did not submit a ballot and timely object to the releases.²⁵ Judge Shannon found that the third-party releases were consensual and overruled the U.S. Trustee's objection with the addition of clarifying language in the confirmation order that allowance of a claim could be determined by a court of competent jurisdiction other than the bankruptcy court and that the re-vesting of assets in the reorganized debtors, discharge, plan releases and injunction provisions would not affect or modify the requirement that the reorganized debtors provide holders of allowed claims with their specified plan treatment.²⁶ Judge Shannon also directed that customary reservation of rights language for the United States and the states be included in the confirmation order.²⁷

B. Southern District of New York Decisions

Walter Investment

In *In re Walter Investment Management Corp.*,²⁸ the U.S. Trustee also objected to the proposed third-party releases in the prepackaged plan of reorganization. The plan originally

²⁰ *Id.*

²¹ *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018).

²² Certification of Andres A. Estrada With Respect to the Tabulation of Votes on the Debtors' Joint Prepackaged Chapter 11 Plan of Reorganization at 2-3, *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018) [Docket No. 83].

²³ Objection of the United States to the Disclosure Statement and the Debtors' Joint Prepackaged Chapter 11 Plan of Reorganization, *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018) [Docket No. 107].

²⁴ United States Trustee's Confirmation Objection at 9-12, *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018) [Docket No. 106].

²⁵ Debtors' Joint Prepackaged Chapter 11 Plan of Reorganization at 29, *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018) [Docket No. 13].

²⁶ Order Approving Debtors' Disclosure Statement for, and Confirming, the Debtors' Joint Prepackaged Chapter 11 Plan of Reorganization, at 49, 36, *In re Rand Logistics, Inc., et al.*, No. 18-10175 (Bankr. D. Del. 2018) [Docket No. 156].

²⁷ *Id.* at 50-51.

²⁸ *In re Walter Inv. Mgmt. Corp.*, No. 17-13448 (Bankr. S.D.N.Y. 2017) (JLG).

provided for third-party releases to be given by: (1) holders of impaired claims voting to accept the plan, (2) holders of impaired claims abstaining from voting on the plan or not opting out of granting the releases, (3) consenting term lenders and consenting senior noteholders under a prepetition restructuring support agreement, (4) significant equity holders²⁹ and (5) certain affiliates of the entities described in (1) through (4).³⁰ The U.S. Trustee argued that two categories of proposed releasing parties could not be deemed to consent to the releases: (i) creditors that did not vote and (ii) creditors that voted to reject but did not separately opt out of the releases.³¹ However, before the bankruptcy court could rule on the issue, debtors' counsel revised the plan so that it no longer included a release of third-party claims by holders of impaired claims that either did not vote on the plan or voted to reject the plan, whether or not they opted out of the release.³² The remaining consensual third-party releases were approved in the confirmation order.³³

Global Brokerage

The U.S. Trustee objected yet again to the third-party releases in the prepackaged plan in *In re Global Brokerage, Inc.*³⁴ The U.S. Trustee noted that, although it appeared that the definition of "releasing parties" was tailored so that only holders of claims that voted to accept the plan would be deemed to have consented, "any confirmation order should make crystal clear that the only parties bound by the Third-Party Releases are named parties and holders of claims that have voted in favor of the plan."³⁵ No modifications were made to the original plan with respect to the third-party releases in the confirmation order, and the bankruptcy court determined that the releases were fair, equitable, reasonable, supported by good consideration and in the best interests of the debtor, the reorganized debtor, the estate and other parties in interest.³⁶ The scope

²⁹ The significant equity holders had executed voluntary releases in favor of the released parties prior to the commencement of the bankruptcy case. Prepackaged Chapter 11 Plan of Reorganization of Walter Investment Management Corp. and The Affiliate Co-Plan Proponents at 12, *In re Walter Inv. Mgmt. Corp.*, No. 17-13448 (Bankr. S.D.N.Y. 2017) [Docket No. 11].

³⁰ *Id.* at 42-44.

³¹ Objection of United States Trustee to Debtor's Disclosure Statement and Confirmation of the Prepackaged Chapter 11 Plan of Reorganization of Walter Investment Management Corp. and the Affiliate Co-Plan Proponents at 10-11, *In re Walter Inv. Mgmt. Corp.*, No. 17-13448 (Bankr. S.D.N.Y. 2017) [Docket No. 130].

³² Debtor's Memorandum of Law and Response to Objections in Support of (I) Approval of (A) Disclosure Statement, (B) Solicitation of Votes and Voting Procedures, and (C) Form of Ballots and (II) Confirmation of Amended Prepackaged Chapter 11 Plan of Reorganization of Walter Investment Management Corp. and the Affiliate Co-Plan Proponents at 34, n.13, *In re Walter Inv. Mgmt. Corp.*, No. 17-13448 (Bankr. S.D.N.Y. 2017) [Docket No. 136].

³³ Findings of Fact, Conclusions of Law and Order (I) Approving Debtor's (A) Disclosure Statement, (B) Solicitation of Votes and Voting Procedures and (C) Form of Ballots, and (II) Confirming Amended Prepackaged Chapter 11 Plan of Reorganization of Walter Investment Management Corp. and the Affiliate Co-Plan Proponents, *In re Walter Inv. Mgmt. Corp.*, No. 17-13446 (Bankr. S.D.N.Y. 2017).

³⁴ *In re Global Brokerage, Inc.*, No. 17-13532 (Bankr. S.D.N.Y. 2017) (MEW).

³⁵ Objection of the United States Trustee to Confirmation of the Prepackaged Plan of Reorganization of Global Brokerage, Inc. Pursuant to Chapter 11 of the Bankruptcy Code at 24, *In re Global Brokerage, Inc.*, No. 17-13532 (Bankr. S.D.N.Y. 2017) [Docket No. 49].

³⁶ Findings of Fact, Conclusions of Law, and Order (I) Approving Debtor's (A) Disclosure Statement, (B) Solicitation of Votes and Voting Procedures and (C) Form of Ballots, and (II) Confirming Prepackaged Chapter 11 Plan of Reorganization of Global Brokerage, Inc. at 24, *In re Global Brokerage, Inc.*, No. 17-13532 (Bankr. S.D.N.Y. 2017) [Docket No. 67].

of the debtor release was narrowed, however, to exclude any claims of the debtor against its current or former officers, directors and employees so that potential shareholder claims against such persons would not be indirectly released.³⁷

SunEdison

In *In re SunEdison, Inc.*,³⁸ Judge Bernstein *sua sponte* challenged whether the third-party releases provided in the plan were consensual.³⁹ The plan of reorganization contained a broad third-party release in favor of the debtors' non-debtor affiliates and specified released parties,⁴⁰ and the releasing parties included all holders of claims entitled to vote for or against the plan that did not vote to reject the plan.⁴¹ Although neither the U.S. Trustee nor any other party objected to the third-party release at confirmation, Judge Bernstein conducted an independent evaluation with respect to the non-voting releasors.⁴² He ruled that the non-voting releasors had not implicitly consented to the release because, absent a duty to speak, silence does not constitute consent.⁴³ He found that the debtors did not identify the source of the duty to speak and that the warning in the disclosure statement and the ballots regarding the effect of silence did not give rise to a duty to speak by the non-voting releasors.⁴⁴ He granted the debtors leave to propose a modified form of release provided that they (1) specify each releasee by name or identifiable group and the claims to be released, (2) demonstrate how each of the claims, if not released, might have a conceivable effect on the reorganized debtors, and (3) show that the releases met the standards for a non-consensual release under *Metromedia*.⁴⁵

An important distinguishing feature of the *SunEdison* plan was the failure to include an opt-out provision in the ballot. Judge Bernstein rejected the debtors' argument that their plan was analogous to the plan ultimately approved in *In re Conseco, Inc.*⁴⁶ Judge Bernstein found that the debtors' plan was more analogous to an earlier iteration of the *Conseco* plan that was not confirmed in which all creditors accepting a plan distribution would have been bound to a third-party release even if they had not voted to accept.⁴⁷ The debtors in *Conseco* then revised the plan so that creditors either voting to accept or failing to opt out would be bound by the third-party

³⁷ *Id.* at 5

³⁸ *In re SunEdison, Inc., et al.*, No. 16-10992 (Bankr. S.D.N.Y. 2017) (SMB).

³⁹ Memorandum Decision and Order Regarding Third-Party Releases under the Debtor's Joint Plan at 1, *In re SunEdison, Inc., et al.*, No. 16-10992 (Bankr. S.D.N.Y. 2017) [Docket No. 4253]

⁴⁰ The released parties included debtors' financial advisors, directors, officers, employees, DIP agents and other lenders, as well as such entities' affiliates and advisors. Findings of Fact, Conclusions of Law and Order Confirming Second Amended Plan of Reorganization of SunEdison, Inc. and Its Debtor Affiliates, dated July 28, 2017, No. 16-10992 (Bankr. S.D.N.Y. 2017) [Docket No. 3735].

⁴¹ *SunEdison*, *supra* note 39, at 1.

⁴² This evaluation occurred after the plan was confirmed, in the absence of objection from the debtors and certain beneficiaries of the release. The court also considered whether it had subject matter jurisdiction to approve the third-party releases. The jurisdictional debate regarding third-party releases is beyond the scope of this article.

⁴³ *SunEdison*, *supra* note 39, at 7.

⁴⁴ *Id.* at 10-11.

⁴⁵ *Id.* at 16-17.

⁴⁶ 301 B.R. 525 (Bankr. N.D. Ill. 2003).

⁴⁷ *SunEdison*, *supra* note 39, at 9, n.8.

release.⁴⁸ Judge Bernstein observed that “[w]hile one may question the curative effect of an opt-out provision, the *Plan* does not allow creditors to opt out of the Release.”⁴⁹

The debtors emerged from bankruptcy shortly after Judge Bernstein’s decision was issued. The previously-confirmed plan was not amended to incorporate the modified release described by Judge Bernstein.

Cumulus

In the context of approval of the disclosure statement in *In re Cumulus Media Inc.*,⁵⁰ Judge Chapman recently signaled an opposing viewpoint to Judge Bernstein’s holding in *SunEdison*. The debtors proposed to use an opt-out mechanism for the releases, including for creditors and equity holders deemed to reject the plan and unimpaired classes.⁵¹ Accordingly, voting creditors, unimpaired creditors and deemed rejecting creditors/equity holders would all have the ability to opt-out of the releases, whether on a ballot or on a notice of non-voting status. The U. S. Trustee objected to this proposal, citing *In re Chassix Holdings*,⁵² in which the court held that compelling a rejecting creditor to affirmatively opt out is effectively a “trap” for the careless or inattentive creditor.⁵³

In response, Judge Chapman disagreed with the characterization as a trap, stating that “[i]naction is action under appropriate circumstances. When someone is clearly and squarely told if you fail to act your rights will be affected, that person is then given information that puts them on notice that they need to do something or else. That’s not a trap.”⁵⁴ In addition to the important due process considerations with respect to those deemed to provide a third-party release, Judge Chapman added that “it’s also important to think about the reorganizing entity. Because in my view a reorganization is supposed to be exactly that, a reorganization and a fresh start for the debtor.”⁵⁵ Although Judge Chapman noted that the proper scope of the releases, the U.S. Trustee’s position that rejecting creditors should have to opt in to the release, and the extent to which the releases “would be still characterized as non-consensual” would be issues for confirmation, her “philosophical view” is supportive of consensual third-party releases provided that the notice is clear about the release and the effect of inaction on the first page and then clearly directs the recipient to the opt-out section of the form.⁵⁶

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *In re Cumulus Media Inc., et al.*, No. 17-13381 (Bankr. S.D.N.Y 2017) (SCC).

⁵¹ Transcript of Hearing at 27-28, *In re Cumulus Media Inc., et al.*, No. 17-13381 (Bankr. S.D.N.Y Feb. 1, 2018).

⁵² *In re Chassix Holdings, Inc.*, 533 B.R. 64, 79 (Bankr. S.D.N.Y 2015).

⁵³ Objection of United States Trustee to Disclosure Statement for Joint Plan of Reorganization of Cumulus Media Inc. and its Debtor Affiliates at 8, *In re Cumulus Media Inc., et al.*, No. 17-13381 (Bankr. S.D.N.Y 2017) [Docket No. 182].

⁵⁴ Transcript of Hearing, *In re Cumulus Media Inc., et al.*, *supra* note 51, at 27-28.

⁵⁵ *Id.* at 28.

⁵⁶ *Id.* at 27-28, 30, 36.

The confirmation hearing began on April 12, 2018 and concluded on May 1, 2018.⁵⁷ In a bench decision read at the conclusion of the hearing, Judge Chapman confirmed the plan and overruled the objections to the third-party releases. She agreed with the debtors that inaction constituted action in this case, and she held that the third-party releases were appropriate and consensual. She also found that the standards for non-consensual releases had been satisfied.

ARO Liquidation (Aéropostale)

In *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*,⁵⁸ Judge Lane recently confirmed the plan of liquidation and overruled objections from the Securities and Exchange Commission and the U.S. Trustee to the non-consensual and consensual releases included in the plan.⁵⁹ Judge Lane found that the non-consensual release in favor of the term lenders met the standards of *Metromedia* and was justified under the circumstances because concessions by the term lenders enabled most of the Aéropostale business to be sold as a going concern and funded unpaid administrative costs of the case and the wind-down to permit a plan of liquidation to be confirmed.⁶⁰ The unsecured creditors' committee supported the non-consensual release, even though unsecured claims received nothing under the plan, because the term lenders' concessions preserved many jobs, numerous store leases and ongoing relationships with suppliers and trade creditors and eliminated potential preference claims against general unsecured creditors.⁶¹ Judge Lane also approved the consensual third-party releases provided by (i) the unimpaired classes of other priority claims and other secured claims and (ii) the impaired and deemed rejecting classes of general unsecured claims and equity interests.⁶² Consent was evidenced by an opt-out box on the notice of non-voting status for the two unimpaired classes and the class of equity interests.⁶³ The consent mechanism for the class of general unsecured claims was changed from an opt-out

⁵⁷ The U.S. Securities and Exchange Commission objected to confirmation of the plan and argued that the third-party releases should be deleted from the plan, or alternatively, the plan should be amended to provide that the third-party releases would not bind deemed rejecting shareholders or unsecured creditors that did not return a ballot, notwithstanding that both classes were provided an opt-out option on the notice of non-voting status or ballot, respectively. Objection of the U.S. Securities and Exchange Commission to Confirmation of the Debtors' First Amended Joint Plan of Reorganization, *In re Cumulus Media Inc., et al.*, No. 17-13381 (Bankr. S.D.N.Y. 2017) [Docket No. 582]. The Official Committee of Unsecured Creditors also objected to the broad scope of the plan releases and contended that the releases were non-consensual because an opt-out mechanism was used rather than an opt-in mechanism. Objection of the Official Committee to Confirmation of the First Amended Joint Plan of Reorganization of Cumulus Media, Inc., *In re Cumulus Media Inc., et al.*, No. 17-13381 (Bankr. S.D.N.Y. 2017) [Docket No. 653]. The U.S. Trustee did not object to confirmation.

⁵⁸ *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. 2016) (SHL).

⁵⁹ Findings of Fact, Conclusions of Law, and Order Pursuant to Sections 1129(a) and (b) of the Bankruptcy Court and Rule 3020 of the Federal Rules of Bankruptcy Procedure Confirming Debtors' Second Revised Third Amended Joint Chapter 11 Plan, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. 2016) [Docket No. 1732].

⁶⁰ Transcript of Bench Decision at 20-23, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. Mar. 28, 2018); Transcript of Confirmation Hearing at 42-45, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. Mar. 19, 2018); Transcript of Continued Disclosure Statement Hearing at 10, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. Feb. 7, 2018).

⁶¹ Transcript of Confirmation Hearing, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 34-37.

⁶² Transcript of Bench Decision, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 30-31.

⁶³ Second Revised Third Amended Joint Chapter 11 Plan of ARO Liquidation, Inc. and Its Affiliated Debtors at 7, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. 2016) [Docket No. 1710].

box to an opt-in box under the final plan because the class treatment had changed from impaired with possible recovery and voting under prior versions of the plan to impaired and deemed to reject under the final plan.⁶⁴ Judge Lane concluded that an opt-in mechanic was the proper approach in this case for the class of general unsecured claims, as opposed to an affirmative obligation to opt out, because the plan treatment had changed “dramatically” to provide no recovery to the class.⁶⁵ Judge Lane concluded that in the future, he expects “more fulsome briefing” on consent procedures and “analysis in the context of the case and these precedents and analogous circumstances in other areas of the law” and not regurgitation “of the same boilerplate that [he had] seen over and over again.”⁶⁶

Westinghouse

In *In re Westinghouse Electric Company LLC*,⁶⁷ Judge Wiles recently confirmed the modified second amended plan of reorganization and approved the third-party releases as consensual.⁶⁸ Earlier versions of the plan provided that all holders of claims or interests would be Releasing Parties and grant third-party releases except for (i) those entitled to vote that did not vote and (ii) those voting to reject and not also checking a box on the ballot to opt to grant the releases.⁶⁹ Following discussion at the confirmation hearing, the debtors modified the definition such that third-party releases would be provided only by holders of claims or interests (i) entitled to vote and voting to accept or (ii) entitled to vote, abstaining from voting and affirmatively opting to grant the release on the ballot.⁷⁰ Only the class of general unsecured claims was impaired and entitled to vote. Two classes of non-intercompany equity interests were deemed to

⁶⁴ Second Amended Joint Plan of Reorganization of Aéropostale, Inc. and Its Affiliated Debtors at 8, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. 2016) [Docket No. 525]; Second Revised Third Amended Joint Chapter 11 Plan, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 63, at 7; Revised Disclosure Statement for Revised Third Amended Joint Chapter 11 Plan of ARO Liquidation, Inc. and Its Affiliated Debtors at 5, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, No. 16-11275 (Bankr. S.D.N.Y. 2016) [Docket No. 1658]. See Transcript of Continued Disclosure Statement Hearing at 16, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 16 (“[T]o the extent that there’s an argument that an unimpaired party doesn’t need to be asked at all about a third party release based on consent, I disagree.”).

⁶⁵ Transcript of Bench Decision, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 30. See Transcript of Continued Disclosure Statement Hearing, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 59, at 14-15.

⁶⁶ Transcript of Bench Decision, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 33, 34. At the continued hearing on the disclosure statement, Judge Lane “urge[d] the U.S. Trustee program to give their attorneys assigned to cases the needed prosecutorial discretion to assess the facts and circumstances of each case in determining when and when not to object to releases and when and how to fashion such objections that fit the cases—each case in question because that’s I think how the analysis should be done.” Transcript of Continued Disclosure Statement Hearing, *In re ARO Liquidation, Inc. (f/k/a Aéropostale, Inc.)*, *supra* note 60, at 11.

⁶⁷ *In re Westinghouse Electric Company LLC*, No. 17-10751 (Bankr. S.D.N.Y. 2017) (MEW).

⁶⁸ Findings of Fact, Conclusions of Law, and Order Confirming Modified Second Amended Joint Plan of Reorganization at 21-22, *In re Westinghouse Electric Company LLC*, No. 17-10751 (Bankr. S.D.N.Y. 2017) [Docket No. 2988].

⁶⁹ See Joint Chapter 11 Plan of Reorganization, First Amended Joint Chapter 11 Plan of Reorganization, Modified First Amended Joint Chapter 11 Plan of Reorganization and Second Amended Joint Plan of Reorganization, *In re Westinghouse Electric Company LLC*, No. 17-10751 (Bankr. S.D.N.Y. 2017) [Docket Nos. 2325, 2593, 2622 and 2954, respectively].

⁷⁰ Modified Second Amended Joint Plan of Reorganization, *In re Westinghouse Electric Company LLC*, No. 17-10751 (Bankr. S.D.N.Y. 2017) [Docket No. 2986].

reject the plan because no recovery was provided. There were two classes of unimpaired claims: other priority claims and secured claims. The U.S. Trustee did not file an objection to confirmation.

C. Other Jurisdictions

The Eastern District of Virginia and the Southern District of Texas have also been popular venues in recent years for larger chapter 11 cases. A review of a number of recent cases reveals that customary forms of consensual third-party releases have been approved and that the U.S. Trustee in the Southern District of Texas has not always objected to such releases. A chart summarizing the consensual third-party release language in selected cases is attached as Exhibit A.

Practice Pointers for Structuring Consensual Third-Party Releases

In recent cases, the U.S. Trustee has become increasingly active in challenging third-party releases in plans of reorganization when the affected creditor or equity holder has not expressly consented, and courts have scrutinized such releases more closely. Although courts often conclude that third-party releases are consensual and appropriate notwithstanding an objection by the U.S. Trustee, counsel for future debtors should consider steps that may be taken to bolster the likelihood of approval of third-party releases as consensual.

It is important to note that the facts of the case may also influence the court's views of consensual third-party releases. If the plan is a prepackaged plan that has received unanimous or overwhelming support from voting parties and the releases are an important element in the overall construct of the negotiated deal reflected in the plan, a court may be more likely to find that implicit consent has been provided, particularly if the class at issue is unimpaired. If impaired creditors are becoming the new equity holders of the reorganized debtor, the court may also focus on the importance of giving the reorganized debtor, as well as directors, officers and employees whose services may be important to the future success of the reorganized debtor, a complete fresh start, free of any potential claims by third-party releasing parties. Although these factual circumstances are important considerations, recent case law also illustrates that debtor's counsel can preemptively address many of the concerns raised by the U.S. Trustee and others by taking the following steps, as applicable:

- Include a release opt-out box on both ballots for voting classes and notices to non-voting creditors and equity holders (whether unimpaired or deemed to reject);
- Make the notice regarding the opt-out option clear and describe the option in bold on the first page of the ballot/notice to non-voting classes. If the opt-out box is not located on the first page, state on the first page where the opt-out box is. Clearly describe the necessary steps to be taken in order to opt out. Finally, expressly state on the first page that a failure to opt out on the returned ballot or to return the notice of non-voting status with the opt-out box checked will be deemed a consent to the release;
- Describe the claims being released as specifically as possible;
- Consider whether a more narrowly-tailored release will satisfy the goals of the debtor and other constituents supporting the plan;

May 7, 2018

- Consider whether an opt-in structure will satisfy the goals of the debtor and other constituents supporting the plan; and
- File a declaration from the claims/voting agent confirming that no solicitation materials/notices of non-voting status were returned undelivered.

Finally, counsel for the debtor should create the evidentiary record that demonstrates why the consensual third-party releases are fair, appropriate and essential to the plan and the reorganized debtor and its constituents.

**Consensual Third-Party Release Provisions in Selected Cases in the
Eastern District of Virginia and the Southern District of Texas**

Case Name and Number	Jurisdiction and Judge	Confirmation Date and Effective Date	Releasing Parties	Objections to Third-Party Releases
The Gymboree Corporation, No. 17-32986	E.D. Virginia K. Phillips	September 7, 2017; September 29, 2017	Holder of Claims and Interests voting to accept; holders of Claims and Interests deemed to accept; holders in voting classes abstaining	Yes, by U.S. Trustee
Penn Virginia Corporation, No. 16-32395	E.D. Virginia K. Phillips	August 11, 2016; September 12, 2016	Holder of Claims and Interests deemed to accept; holders of Claims and Interests voting to accept; holders of Claims and Interests abstaining from voting and not opting out	Yes, by U.S. Trustee
Alpha Natural Resources, Inc., No. 15-33896	E.D. Virginia K. Huennekens	July 12, 2016; July 26, 2016	Broad release applicable to any holder of a claim* *Note this release was evaluated on non-consensual basis but court found that holders of claims voting for plan provided consensual release	Yes, by U.S. Trustee
GenOn Energy, Inc., No. 17-33695	S.D. Texas D. Jones	December 12, 2017; Effective Date has not yet occurred	All holders of Claims and Interests except those opting out or otherwise objecting to the releases	Yes, by U.S. Trustee
Linn Energy, LLC, No. 16-60040	S.D. Texas D. Jones	January 27, 2017; February 28, 2017	All holders of Claims and Interests other than (i) holders voting to reject, (ii) holders in a class that	None

Exhibit A

Case Name and Number	Jurisdiction and Judge	Confirmation Date and Effective Date	Releasing Parties	Objections to Third-Party Releases
			is deemed to reject and (iii) holders voting to accept or abstaining from voting and expressly opting out of the release	
Castex Energy Partners, L.P., No. 17-35835	S.D. Texas M. Isgur	February 27, 2018; March 14, 2018	Holders of Claims and Interests voting to accept; holders of Claims and Interests deemed to accept; holders of Claims and Interests that receive a ballot but do not vote for the Plan and do not check the box to opt out of the releases; holders of Claims and Interests voting to reject and not checking the box to opt out; holders of Claims and Interests deemed to reject that do not opt out; all other holders of Claims and Interests to the extent permitted by law	Yes, by the U.S. Trustee
Goodman Networks Incorporated, No. 17-31575	S.D. Texas M. Isgur	May 4, 2017; May 31, 2017	Holders of Claims and Interests that vote to accept; holders of Claims and Interests that do not vote and do not opt out; holders of Claims and Interests that vote to reject and do not opt out	None
Seadrill Limited, No. 17-60079	S.D. Texas D. Jones	April 17, 2018;	All holders of Claims or Interests [an objection to	Yes, by the U.S. Trustee

Exhibit A

Case Name and Number	Jurisdiction and Judge	Confirmation Date and Effective Date	Releasing Parties	Objections to Third-Party Releases
		Expected Effective Date is July 16, 2018	confirmation would have been necessary to avoid granting releases; no such objections filed]	