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**Judicial Merry-Go-Round**  
**ABI Southeast Bankruptcy Workshop**  
**Amelia Island, July 29, 2018**

**Judicial Estoppel Update: The Eleventh Circuit's  
En Banc Ruling in *Slater v. U.S. Steel Corp.***

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The Eleventh Circuit established new standards for the application of judicial estoppel when a debtor asserts a claim in a federal court that she failed to disclose as an asset on her bankruptcy schedules in its en banc ruling in *Slater v. U. S. Steel Corp.*, 871 F.3d 1174 (11th Cir. 2017) (en banc).

At the time the debtor filed a Chapter 7 bankruptcy case, her lawsuit against U.S. Steel for race and gender discrimination was pending in the district court. She did not disclose the lawsuit in her schedules or Statement of Financial Affairs. The Chapter 7 trustee filed a report of no distribution.

U.S. Steel moved for summary judgment in the employment discrimination case based on judicial estoppel. The debtor testified by declaration that she did not intentionally misrepresent facts to the bankruptcy court and that she misunderstood the question in the Statement of Financial Affairs. The day after U.S. Steel filed the motion for summary judgment, the debtor filed amended schedules to disclose her claims. The bankruptcy trustee employed attorneys to prosecute the claims, but the debtor later converted the case to chapter 13. After she defaulted on her payments, the case was dismissed.

While the bankruptcy case was still pending, the district court granted U.S. Steel's motion for summary judgment on the ground that judicial estoppel barred her claims. The district court rejected the debtor's argument that judicial estoppel should not apply because her failure to list the claims in the lawsuit in her initial filings was an inadvertent mistake such that she had not intended to make a mockery of the judicial system.

The district court rejected the debtor's argument under the standards for application of judicial estoppel that the Eleventh Circuit had established in *Barger v. City of Cartersville*, 348 F.3d 1289 (11th Cir. 2003) and *Burnes v. Pemco Aeroplex, Inc.*, 291 F.3d 1282 (11th Cir. 2002). Under those cases, the district court reasoned, a failure to disclose is "inadvertent" only when the debtor either lacks knowledge of the undisclosed claim or has no motive for its concealment. The district court drew an inference that the debtor intended to make a mockery of the judicial system because she had knowledge of the undisclosed claims and a motive to conceal them.

On appeal, a panel of the Eleventh Circuit affirmed. 820 F.3d 1329 (11<sup>th</sup> Cir. 2016). In a concurring opinion, Judge Tjoflat called for an en banc review. The Eleventh Circuit agreed to rehear the case en banc and vacated the panel opinion.

## 2018 SOUTHEAST BANKRUPTCY WORKSHOP

The en banc court on rehearing reaffirmed the principles that a district court may apply judicial estoppel when (1) the plaintiff took a position under oath in the bankruptcy proceeding that was inconsistent with the plaintiff's pursuit of the civil lawsuit; and (2) the plaintiff intended to make a mockery of the judicial system.

The precise issue on rehearing en banc was how a district court should analyze the second prong. The Circuit clarified its prior precedent to hold that "the district court must consider all the facts and circumstances in determining whether the plaintiff acted with the intent to make a mockery of the judicial system."

The en banc court explicitly overruled the portions of *Burnes* and *Barger* that permitted an inference that a plaintiff intended to make a mockery of the judicial system simply because she failed to disclose a claim. Instead, the court stated, "When the plaintiff's inconsistent statement comes in the form of an omission in bankruptcy disclosures, the court may consider such factors as the plaintiff's level of sophistication, whether and under what circumstances the plaintiff corrected the disclosures, whether the plaintiff told his bankruptcy attorney about the civil claims before filing the bankruptcy disclosures, whether the trustee or creditors were aware of the civil lawsuit or claims before the plaintiff amended the disclosures, whether the plaintiff identified other lawsuits to which he was party, and any findings or actions by the bankruptcy court after the omission was discovered."

The en banc court also overruled *Barger* to the extent that it ruled that judicial estoppel based on the debtor's conduct would bar a bankruptcy trustee from asserting the debtor's claim as property of the estate. Thus, *Parker v. Wendy's International, Inc.*, 365 F.3d 1268 (11<sup>th</sup> Cir. 2004), which had ruled that judicial estoppel cannot bar a trustee's assertion of the claims, is controlling on this issue.

The en banc court remanded the matter to the panel for further consideration in light of its opinion. Noting that the district court had not considered any of the factors that the en banc court identified as relevant to application of judicial estoppel, the panel vacated the district court's summary judgment order and remanded to the district court for further proceedings. 891 F.3d 1329 (11<sup>th</sup> Cir. 2018).

# Litigator's Perspective

BY JEREMY L. RETHERFORD AND JONATHAN P. HOFFMANN

## 11th Circuit Addresses Judicial Estoppel, Unscheduled Litigation



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Think of first-year civil procedure: Remember the doctrine of judicial estoppel? In short, the doctrine “precludes a party from asserting a ... position that contradicts or is inconsistent with a prior position taken by the same party.”<sup>1</sup> Judicial estoppel arises in the bankruptcy context when a debtor fails to disclose a potential claim or pending litigation as a contingent or unliquidated claim in its Schedule B.

When litigation is already pending, the non-debtor defendant may move to dismiss the case, claiming that the debtor is judicially estopped from proceeding in the litigation due to the debtor’s contrary position in the bankruptcy court (essentially stating that the nonbankruptcy case does not exist). Each circuit addresses such arguments in a similar but somewhat unique fashion, as judicial estoppel (assuming that the federal court sits in federal question jurisdiction over the nonbankruptcy case) proceeds under federal, not state, law — a point with notable significance explored below.

For some circuits, whether omitting pending litigation in the schedules proves fatal depends on the intent behind the omission, with good-faith omissions receiving a pass.<sup>2</sup> Since judicial estoppel focuses on the integrity of the judicial system, these circuits’ reasoning holds that no harm to the judiciary’s integrity exists when a party inadvertently makes inconsistent statements before a tribunal.<sup>3</sup> However, *Slater v. U.S. Steel* moves the Eleventh Circuit into a new camp that no longer seeks to uncover the intent of a party’s omission, but rather holds that nondisclosure to a bankruptcy court forecloses the pending litigation from proceeding as a matter of law, regardless of why the omission occurred.

### Background

*Slater* begins with a recitation of the doctrine of judicial estoppel as it exists in the Eleventh Circuit. Pre-*Slater*, judicial estoppel did not vary largely from the norm, although notably, “[t]he doctrine may be invoked by a third party: that is, someone who was not a party in the adversary’s prior proceeding and therefore would suffer no prejudice

were the adversary permitted to go forward with the inconsistent position.”<sup>4</sup> Moreover, of paramount importance is “protect[ing] the integrity of the judicial system[;] ... detrimental reliance” by the litigants, though often present, is “not required.”<sup>5</sup> Put more poetically, the Eleventh Circuit seeks to determine whether a litigant intended “to make a mockery of the judicial system.”<sup>6</sup>

After setting forth the state of judicial estoppel in the Eleventh Circuit, the court proceeded to address the facts at bar: Nearly two years after filing an employment-discrimination suit against her employer, Sandra Slater filed a chapter 7 petition, but failed to disclose the pending suit on her Schedule B.<sup>7</sup> U.S. Steel, who was Slater’s employer, moved to dismiss the case for lack of standing, arguing only that the panel trustee could proceed, or, in the alternative, moved for summary judgment under the doctrine of judicial estoppel, citing *Burnes v. Pemco Aeroplex Inc.*, a case on all fours with *Slater* and the ultimate death knell for Slater’s case.<sup>8</sup> As the *Slater* court recounted, “*Burnes* was an employment-discrimination case like Slater’s that was dismissed because the plaintiff, who was in bankruptcy, failed to disclose the pendency of federal-district-court litigation to the Bankruptcy Court.”<sup>9</sup>

Curing misstatements and omissions in schedules can occur easily, though, and Rule 1009(a) of the Federal Rules of Bankruptcy Procedure allows debtors to voluntarily amend schedules “as a matter of course at any time before the case is closed.” Upon receiving U.S. Steel’s motion, that is exactly what Slater did.

She responded to U.S. Steel’s motion arguing that judicial estoppel did not apply because (1) she had not yet received a discharge, (2) no unfair advantage would result from allowing her employment-discrimination case to proceed, and (3) she inadvertently omitted the case from her

4 *Slater*, No. 12-15548, slip op. at 2, n.1 (citing *Moore*, supra, at ¶ 131.33[1] (“The majority rule is that a party is not required to have been a party to the prior proceeding to be able to invoke judicial estoppel.”)).

5 *Id.* (citing *Burnes v. Pemco Aeroplex Inc.*, 291 F.3d 1282, 1286 (quotation marks omitted) (quoting *Ryan Operations GP v. Santiam-Midwest Lumber Co.*, 81 F.3d 355, 360 (3d Cir. 1996))).

6 *Id.* at 8 (quoting *Burnes*, 291 F.3d at 1285 (quoting *Salomon Smith Barney Inc. v. Harvey*, 260 F.3d 1302, 1308 (11th Cir. 2001)); see also *Robinson v. Tyson Foods Inc.*, 595 F.3d 1269, 1275 (11th Cir. 2010) (“When considering a party’s intent[,] ... the debtor’s failure to satisfy its statutory disclosure duty is ‘inadvertent’ only when, in general, the debtor either lacks knowledge of the undisclosed claims or has no motive for their concealment.”).

7 *Id.* at 3-4.

8 291 F.3d 1282 (11th Cir. 2002).

9 *Slater*, No. 12-15548, slip op. at 5.

1 *Slater v. U.S. Steel Corp.*, No. 12-15548, slip op. at 2 (11th Cir. Feb. 24, 2016) (quoting 18 James Wm. Moore, et al., *Moore’s Federal Practice* ¶ 131.13[6][a] (3d ed. 2015)), available at [media.ca11.uscourts.gov/opinions/pub/files/201215548.pdf](http://media.ca11.uscourts.gov/opinions/pub/files/201215548.pdf) (last visited March 25, 2016).

2 See, e.g., *Ah Quin v. County of Kauai DOT*, 733 F.3d 267 (9th Cir. 2013).

3 *Id.* at 271-72.

Schedule B.<sup>10</sup> The district court deemed U.S. Steel's motion to dismiss as moot because, during the pendency of the district court case, the bankruptcy court converted Slater's chapter 7 to a chapter 13 — effectively removing the panel trustee. However, the court granted summary judgment for U.S. Steel over Slater's three arguments, following *Burnes*.<sup>11</sup>

In short, the district court's inquiry came down to analyzing Slater's intent "because [generally] the Eleventh Circuit requires intentional contradictions, not [a] simple error or inadvertence."<sup>12</sup> To determine whether the district court properly answered that question, the *Slater* court engaged in a lengthy discussion of binding authority, ultimately looking to *Barger v. City of Cartersville*,<sup>13</sup> where the court stated that a "debtor's failure to satisfy [her] statutory [Bankruptcy Code] disclosure duty is 'inadvertent' only when ... the debtor either lacks knowledge of the undisclosed claims or has no motive for their concealment."<sup>14</sup> In *Barger*, the court determined that the debtor had such motive because "by omitting the claims, she could keep any proceeds for herself and not have them become part of the bankruptcy estate. Thus, [her] knowledge of her discrimination claims and motive to conceal them [were] sufficient evidence from which to infer her intentional manipulation."<sup>15</sup> In other words, because proceeds of the nonbankruptcy litigation would flow to the debtor and not the estate, not listing known litigation is never inadvertent.<sup>16</sup>

This reasoning allowed the *Slater* court to make its ultimate ruling, which boiled down as follows: "The factors that trigger the application of [judicial estoppel] are (1) an inconsistent position taken under oath in the Bankruptcy Court, and (2) advancing an inconsistent position in the District Court with the intent to make a mockery of justice."<sup>17</sup> Any actions taken by the debtor after discovering its omission do not matter because consideration of remedial measures "only diminish[es] the necessary incentive to provide the bankruptcy court with a truthful disclosure of the debtor's assets."<sup>18</sup> In addition, given the *Slater* court's reading of *Barger* and *Robinson*, "intent to make a mockery" of the court is now inferred as a matter of law by simply making an inconsistent statement. The *Slater* court held that to allow debtors to double back and not make initially complete and truthful disclosures "would be undermining the administration of the bankruptcy law and the integrity of the judicial process."<sup>19</sup>

<sup>10</sup> *Id.* at 6-7. *Slater* rooted these arguments in a U.S. Supreme Court case, *New Hampshire v. Maine*, 532 U.S. 742, 121 S. Ct. 1808, 149 Ed. 2d 968 (2001). *New Hampshire* speaks directly to judicial estoppel and provides a set of analytical factors that the *Burnes* and *Slater* courts noted were not "inflexible prerequisites or an exhaustive formula for determining the applicability of judicial estoppel," as "[a]dditional considerations may inform the doctrine's application in specific factual contexts." *Slater*, No. 12-15548, at 21-22 (quoting *Burnes*, 291 F.3d at 1285 (quoting *New Hampshire*, 532 U.S. at 750-51)). Indeed, the *Burnes* court specifically noted that Eleventh Circuit law conformed with *New Hampshire*. *Id.* (citing *Burnes*, 291 F.3d at 1285-86).

<sup>11</sup> The district court also rested its decision upon a sister case to *Burnes*: *Robinson*, 595 F.3d 1269.

<sup>12</sup> *Slater*, No. 12-15548, *slip op.* at 10.

<sup>13</sup> 348 F.3d 1289 (11th Cir. 2003).

<sup>14</sup> *Id.* at 1296.

<sup>15</sup> *Id.*

<sup>16</sup> This inference deviates partially from *Burnes*. As *Slater* discusses, the debtor in *Burnes* "intentionally concealed from the Bankruptcy Court his claim against Pemco, thereby depriving the chapter 7 trustee of the ability to intervene and prosecute his claim for the benefit of the bankruptcy estate and his creditors." *Slater*, No. 12-15548, *slip op.* at 24. In *Burnes*, the debtor — once found out — attempted to reopen his bankruptcy case in order to list the pending litigation. *Burnes*, 291 F.3d at 1288. However, as the court in *Slater* noted, allowing the debtor to remedy his concealment "would be condoning his behavior, and, to the extent that such behavior would be noised about, it would be encouraging future debtors to follow suit." *Slater*, No. 12-15548, *slip op.* at 24.

<sup>17</sup> *Slater*, No. 12-15548, *slip op.* at 31.

<sup>18</sup> *Id.* at 31-32 (quoting *Burnes*, 291 F.3d at 1288).

<sup>19</sup> *Id.* at 24.

## The Opened Door

Although the Eleventh Circuit issued *Slater* as a *per curiam* opinion, Hon. Gerald Tjoflat wrote a special concurrence. At more than twice the length of the opinion itself, Judge Tjoflat's special concurrence contains a meticulous analysis and presentation of the genesis of judicial estoppel in the Eleventh Circuit.

Since *Slater* was issued as a *per curiam*, it stands as the law of the Eleventh Circuit. However, Judge Tjoflat in no uncertain terms "call[ed] for *en banc* review to set straight the doctrine of judicial estoppel."<sup>20</sup> In other words, he asked practitioners to challenge *Slater* and the cases it relies on, providing them and his fellow judges a remarkably thorough argument complete with all the possible cases necessary to make such a challenge.<sup>21</sup>

At the risk of oversimplifying, Judge Tjoflat's discussion shows that at some point in the Eleventh Circuit's history, judicial estoppel cases citing state-based standards were adopted by courts sitting in federal-question jurisdiction. The Eleventh Circuit Court of Appeals and the district courts within the Eleventh Circuit have not always recognized or respected that distinction. Judge Tjoflat admitted to adding to the confusion by partaking in a decision that was "directly contrary" to binding precedent, despite the case "presenting a set of facts [that were] materially indistinguishable" from that binding precedent.<sup>22</sup> The full nuance and depth of Judge Tjoflat's special concurrence falls outside the scope — and, indeed, length — of this article. However, suffice it to say, it opens wide the door for challenges — or, at bottom, clarification — to *Slater*, *Burnes*, and the great body of cases making up the doctrine of judicial estoppel in the Eleventh Circuit. Indeed, as Judge Tjoflat makes clear, that was his stated purpose in drafting the concurrence.

Despite the special concurrence calling into question the longevity and basis for *Slater*, the case presents a remarkably administrable rule for practitioners within the Eleventh Circuit: Not listing pending litigation on a Schedule B gives grounds for dismissal of that pending litigation under the judicial estoppel doctrine. Very little wiggle room exists for debtors to avoid the results of *Slater*, as the intent required to "make a mockery of the judicial system" is now inferred as a matter of law by the simple act of not listing a pending action.

*Slater* gives no indication that its holding is limited to the employment-discrimination arena, opening up the use of this argument for litigants of other walks of life. Thus, it now is more important than ever for debtor attorneys to counsel clients on the importance of full disclosure. Equally important, attorneys defending cases must periodically check to see whether a plaintiff has filed for bankruptcy and failed to disclose pending litigation. [abi](#)

<sup>20</sup> *Id.* at 36 (Tjoflat, J., concurring).

<sup>21</sup> The special concurrence ends with a set of appendices containing charts that categorize and analyze each and every germane Eleventh Circuit judicial estoppel case. *Id.* at 106-12. Appendix I provides a timeline specifically addressing the oath requirement of the doctrine and a timeline of key judicial estoppel cases that were most relevant to that analysis. Appendix II contains a "list of court of appeals, district court, and bankruptcy court decisions within the Eleventh Circuit that cite [*Burnes* or *Barger*] or both as of February 22, 2016." *Id.* at 108.

<sup>22</sup> *Id.* at p. 68. Judge Tjoflat went so far as to plea, "*Mea culpa*." *Id.*

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# Last in Line

BY HON. DEBORAH L. THORNE AND BRETT NEWMAN<sup>1</sup>

## What's Next After *Husky v. Ritz*: Has Pandora's Box Been Opened?

The U.S. Supreme Court granted *certiorari* in *Husky International Electronics Inc. v. Ritz* to resolve a circuit split, but the decision left many more questions in its aftermath. The full scope of *Husky*'s impact is unknown, but several issues that are likely to follow the Supreme Court's decision stand out.

### Background

The facts in *Husky* are unique but relatively straightforward.<sup>2</sup> For a number of years, Husky International Electronics sold electronic device components to Chrysalis Manufacturing Corp., a company controlled by Daniel Ritz (the debtor).<sup>3</sup> Chrysalis did not pay for all of the goods it received, and Ritz transferred Chrysalis' assets to other entities controlled by him.<sup>4</sup> Husky then sued Ritz, attempting to hold him personally liable for Chrysalis' debt. The suit eventually led to Ritz filing a chapter 7 petition. Husky responded with an adversary complaint, claiming Ritz was liable for Chrysalis' debt and that the debt owed to it was not dischargeable under § 523 of the Bankruptcy Code.<sup>5</sup> The graphic illustrates the relationship among Husky, Ritz and Ritz's entities.

The bankruptcy court rejected these claims.<sup>6</sup> The district court affirmed, holding that Ritz was personally liable but that Husky could still not prevail under § 523(a)(2)(A), which excepts debts from discharge "for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by — false pretenses, a false representation, or actual fraud...."<sup>7</sup> The Fifth Circuit also affirmed and held that a misrepresentation is needed to show actual fraud in § 523(a)(2)(A).<sup>8</sup> In doing so, the Fifth Circuit rejected the Seventh Circuit's decision in *McClellan v. Cantrell*, in which Judge Richard Posner found that "actual fraud" in § 523(a)(2)(A) does not require a misrepresenta-

tion.<sup>9</sup> After the Fifth Circuit decided *Husky*, the First Circuit sided with the Seventh Circuit,<sup>10</sup> deepening the circuit split.

The Supreme Court granted *certiorari* in *Husky International Electronics Inc. v. Ritz* to resolve whether "actual fraud" in § 523(a)(2)(A) of the Bankruptcy Code requires a misrepresentation, and thus resolve the circuit split. On May 16, 2016, the Court ruled by a 7-1 vote<sup>11</sup> that fraudulent conveyances, like Ritz's alleged scheme, are within the scope of "actual fraud" in § 523(a)(2)(A).<sup>12</sup>

Justice Sonia Sotomayor delivered the opinion of the Court, which focused on two main points to justify its reversal of the Fifth Circuit's decision. First, the addition of "actual fraud" to § 523(a)(2)(A) in 1978 suggests that the phrase must include actions other than just false pretenses or false representations.<sup>13</sup> Second, the Court reasoned that the common law understanding of fraud, going all the way back to the *Statute of 13 Elizabeth*, included fraudulent conveyances.<sup>14</sup> The Court reversed the Fifth Circuit and remanded to decide, among other issues, "whether the debt to Husky was 'obtained by' Ritz'[s] asset-transfer scheme."<sup>15</sup>

Justice Clarence Thomas wrote a dissent that focused heavily on the "obtained by" issue, specifically that § 523(a)(2)(A) applies only at the *inception* of a debt, which was not the case in *Husky*.<sup>16</sup> He followed that reliance on the debtor's misrepresentation was required to satisfy § 523(a)(2)(A).<sup>17</sup> Because Ritz did not fraudulently induce Husky to sell goods to Chrysalis, Husky could not support a claim under § 523(a)(2)(A).<sup>18</sup>

### Implications

While *Husky* answers the question of whether "actual fraud" requires a misrepresentation, several other questions are left in *Husky*'s wake.

<sup>9</sup> *Id.*; see *McClellan v. Cantrell*, 217 F.3d 890 (7th Cir. 2000). In *McClellan*, the creditor sold assets to the debtor's brother, who subsequently transferred them to his sister (the debtor) for only \$10. *Id.* at 892. The debtor then sold the assets for \$160,000. *Id.* Then she filed a chapter 7 petition. *Id.* The Seventh Circuit found that a misrepresentation was not required to except a debt from discharge under § 523(a)(2)(A). *Id.* at 893. Judge Posner wrote that by participating in the fraudulent-transfer scheme, the debtor "obtained" assets by fraud and incurred a debt. *Id.* at 895.

<sup>10</sup> *Sauer Inc. v. Lawson (In re Lawson)*, 791 F.3d 214 (1st Cir. 2015).

<sup>11</sup> Only eight justices participated in the decision due to Justice Antonin Scalia's death in February 2016.

<sup>12</sup> *Husky Int'l Elecs. Inc. v. Ritz*, 136 S. Ct. 1581 (2016).

<sup>13</sup> *Id.* at 1586.

<sup>14</sup> *Id.* at 1586-88.

<sup>15</sup> *Id.* at 1589, n.3.

<sup>16</sup> *Id.* at 1591 (Thomas, J., dissenting).

<sup>17</sup> *Id.* (Thomas, J., dissenting).

<sup>18</sup> *Id.* at 1592 (Thomas, J., dissenting).



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<sup>1</sup> Disclaimer: None of the statements contained in this article constitute the official policy of any judge, court, agency or government official or quasi-governmental agency. The authors express their gratitude to Prof. Charles J. Tabb of the University of Illinois College of Law and Jasmine Reed, a law clerk to Hon. Pamela Pepper of the U.S. District Court for the Eastern District of Wisconsin, for their suggestions and insights.

<sup>2</sup> See *Husky Int'l Elecs. Inc. v. Ritz (In re Ritz)*, 787 F.3d 312, 314 (5th Cir. 2015).

<sup>3</sup> *Id.*

<sup>4</sup> *Id.* Ritz had varying degrees of ownership in the transferee entities.

<sup>5</sup> *Id.* Husky's § 523 actions rest on a veil-piercing theory, where Husky attempted to hold Ritz liable for the companies that he controlled. This issue will need to be decided on remand for a § 523 claim to be successful.

<sup>6</sup> *Husky Int'l Elecs. Inc. v. Ritz (In re Ritz)*, 459 B.R. 623 (Bankr. S.D. Tex. 2011).

<sup>7</sup> *Husky Int'l Elecs. Inc. v. Ritz (In re Ritz)*, 513 B.R. 510 (S.D. Tex. 2014).

<sup>8</sup> *Husky*, 787 F.3d at 321. The Fifth Circuit did not discuss, however, whether Ritz was personally liable.

Some of these issues may be particularly troublesome for bankruptcy courts. Most notably, the inclusion of fraudulent transfers under “actual fraud” significantly expands the scope of potential § 523(a)(2)(A) actions, leaving bankruptcy courts to deal with an influx of § 523(a)(2)(A) adversary proceedings. Given the peculiar factual situation in *Husky* and the unresolved “obtained-by” issue, the scope of *Husky*’s effects is unclear. Below are some of the issues that may follow from the increase in § 523(a)(2)(A) actions.

**Unresolved Questions**

The Supreme Court’s decision was a narrow one, limited to the finding that “actual fraud” under § 523(a)(2)(A) *does not* require a misrepresentation. The question of whether the debt owed to *Husky* was “obtained by” Ritz’s transfer scheme remains open.<sup>19</sup>

In its limited discussion on the issue, the Court stated that a transferor does not “obtain[n]” debt via a fraudulent conveyance, but a transferee *can* “obtain[n]” assets “by” participating in a fraud with the requisite intent.<sup>20</sup> If the transferee then files for bankruptcy, the debts that are “traceable to” the fraud are nondischargeable.<sup>21</sup> Despite its commentary on the issue, the Court stopped short of determining whether Ritz’s debt was “obtained by” the transfer scheme. This might not stop creditors, however, from latching onto what appears to be the majority’s *dicta* when trying to satisfy the “obtained by” requirement.

This open issue is likely to spawn similar litigation, with lower courts left to decide whether a specific transferee “obtain[s]” a debt “by” receiving a fraudulent convey-

ance.<sup>22</sup> On remand, the Fifth Circuit may very well deny *Husky*’s § 523(a)(2)(A) claim again — this time on the basis that Ritz’s alleged debt to *Husky* was not “obtained by” the fraudulent-transfer scheme.

Does this mean that bankruptcy courts can continue to deny § 523(a)(2)(A) claims similar to *Husky*’s if the debt was not “obtained by” actual fraud? Bankruptcy courts will need to examine whether the nexus between the debtor and the offended creditor is sufficient to support a § 523(a)(2)(A) action. Despite the Court answering the question that “actual fraud” in § 523(a)(2)(A) does not require a misrepresentation, the “obtained by” issue is likely to leave lower courts split on what to do with *Husky*-type cases.

**Two Bites at the Apple**

Section 727(a)(2)(A) of the Bankruptcy Code provides a remedy for all creditors when there are fraudulent transfers, but those actions are limited to transfers occurring within a year before filing the petition.<sup>23</sup> Section 523(a)(2)(A), which covers fraudulent transfers post-*Husky*, contains no such limitation. This gives creditors a possible second bite at the apple in preventing the discharge of debts owed to them. In addition, it could erode the protection of the one-year reach-back period in § 727(a)(2)(A).

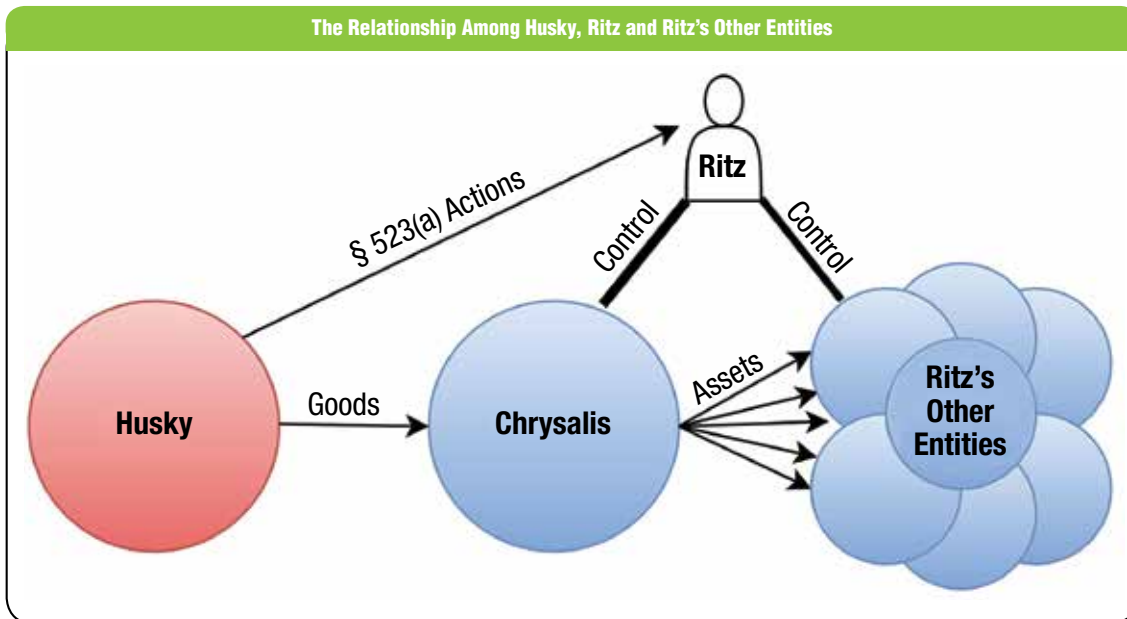
Will this result in many more § 523(a)(2)(A) actions when § 727(a)(2)(A) is the more appropriate option? Section

<sup>22</sup> For example, the Seventh Circuit has already addressed this question in *McClellan v. Cantrell*. In *McClellan*, the court acknowledged that a knowing recipient of a fraudulent transfer may obtain assets by fraud, and a debt “arises by operation of law” from the transferee’s fraud. 217 F.3d at 895. The court determined that this debt would not be dischargeable under § 523(a)(2)(A). *Id.*

<sup>23</sup> “The court shall grant the debtor a discharge, unless ... the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed ... property of the debtor, within one year before the date of the filing of the petition.”

<sup>19</sup> *Id.* at 1589 n.3. Whether *Husky* could pierce the corporate veil and hold Ritz individually liable was also an open question that would need to be decided on remand.  
<sup>20</sup> *Id.* at 1589.  
<sup>21</sup> *Id.*

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## ***Last in Line: What's Next After Husky: Has Pandora's Box Been Opened?***

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727(a)(2)(A) was clearly drafted to respond to fraudulent transfers,<sup>24</sup> but it is not so clear for § 523(a)(2)(A).

### **Organizing § 523(a)(2)(A) Actions**

Section § 523(a)(2)(A) is meant to except specific debts owed to individual creditors from discharge. When the fraud at issue is related to the inception of the debt, it is not difficult to tie the debt to the fraud. The same cannot be said for subsequent fraudulent transfers that are far removed from the inception of a debt. Given the decision in *Husky*, however, there will likely be many § 523(a)(2)(A) actions that are not easily tied to a particular debt owed to one creditor. Some likely issues that will follow are best shown by a hypothetical.

For example, consider a situation similar to *Husky*.<sup>25</sup> An individual (the transferor) owes three creditors \$1,000 each. The transferor realizes that he is unable to pay his debts, and he transfers his last \$300 to his niece (the transferee). Assume, as will likely be the case in these types of actions, that the \$300 is not easily attributed to any one of the three individual creditors.<sup>26</sup> The transferee files a chapter 7 petition, and all of the transferor's creditors want to prevent the transferee from discharging her debt. Because the transferee received only \$300 in fraudulent transfers, does only the winner of the proverbial "race to the courthouse" get to except its debt from discharge? If not, which seems to be the only fair answer, how does a bankruptcy court organize competing § 523(a)(2)(A) actions? What happens if one of the creditors does not show up?<sup>27</sup> If the creditors are successful, how much of the debts owed to them can be excepted from discharge?<sup>28</sup> The questions do

not end here, and bankruptcy courts will be left to determine an equitable way to deal with these issues.

Changing the facts slightly, consider that there are now 100 creditors, most of which have considerable resources and are willing to file § 523 adversary complaints. Given that the fraudulent transfers cannot be specifically tied to the debt of any of the 100 creditors, all of them seek to file § 523(a)(2)(A) actions to prevent the transferee from discharging the debt that is owed to them. Surely it would not be economical or practical for 100 separate adversary proceedings to be initiated, seeking to except each separate debt from discharge. How will bankruptcy courts deal with this situation? Because the fraudulent transfers are not specifically tied to any of the 100 creditors, it would make sense for one action to be brought on behalf of all of the creditors.

The Bankruptcy Code incorporates provisions to allow one action to be brought on behalf of all the creditors, specifically §§ 548 and 727(a). In contrast, an action under § 523(a) benefits only the creditor that pursues it. The collective remedies in §§ 548 and 727(a) would surely be the more economical, equitable and practical approach for creditors to recover in the above example. These collective remedies provide a remedy for the benefit of all when the fraudulent transfers at issue are not directly attributable to any one single creditor. If the trustee does not pursue the above options, however, it leaves the door open for individual creditors to use § 523(a) for fraudulent transfers.

### **What Now?**

Creditors will quickly respond to the Supreme Court's expansive reading of § 523(a)(2)(A), and it will be up to bankruptcy courts (absent further decisions from the courts of appeals) to respond to the increased use of the exception to discharge. The scope of the impact is unknown, but one thing is for sure: "Actual fraud" in § 523(a)(2)(A) includes receiving fraudulent transfers. Will this open Pandora's box, or is it much ado about nothing? **abi**

<sup>24</sup> *Id.*

<sup>25</sup> A similar hypothetical was posed by Hon. Eugene R. Wedoff (ret.), ABI's President-Elect, in a recent webinar. See "Experts Discuss Supreme Court's Ruling in *Husky International Electronics Inc. v. Ritz* and Its Impact on Fraudulent Conveyance Litigation," ABI Media Webinar (May 18, 2016), available at [abi.org/educational-brief/experts-discuss-supreme-courts-ruling-in-husky-international-electronics-inc-v-](http://abi.org/educational-brief/experts-discuss-supreme-courts-ruling-in-husky-international-electronics-inc-v-)

<sup>26</sup> This may not be the case if, for example, if the transferor conveyed one of the creditor's goods to the transferee. In that case, the affected creditor may be the only one with a viable § 523(a)(2)(A) action.

<sup>27</sup> See ABI Media Webinar, *supra* n.25. In his answer to Judge Wedoff's question, Prof. Anthony Casey of the University of Chicago Law School asked what would happen if only one creditor shows up.

<sup>28</sup> *Id.* In this type of hypothetical situation, Judge Wedoff asked how much of the debt owed to each creditor would be nondischargeable.

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# Feature

BY ANUPAMA YERRAMALLI AND ALEXANDER NICAS<sup>1</sup>

## “Per Plan” or “Per Debtor”?

### *Transwest Reignites the § 1129(a)(10) Debate*

As a matter of first impression among circuit courts, the U.S. Court of Appeals for the Ninth Circuit recently held in *Transwest* that 11 U.S.C. § 1129(a)(10) should be interpreted on a “per-plan” basis, meaning that only one impaired accepting class at one debtor is required for a multi-debtor joint chapter 11 plan.<sup>2</sup> In adopting the “per-plan” interpretation, the Ninth Circuit dismissed the alternative “per-debtor” interpretation of § 1129(a)(10), which requires an impaired accepting class at every debtor participating in a multi-debtor joint chapter 11 plan.

*Transwest* resolves, at least in the Ninth Circuit, an issue that has produced conflicting lower court decisions in the Second and Third Circuits, and it reignites a debate as to proper interpretation of § 1129(a)(10).<sup>3</sup> As § 1129(a)(10) has been called the “statutory gatekeeper” to cramdown, the per-plan interpretation alters the balance of power between debtors and creditors in plan negotiations, and it directly affects any chapter 11 case where jointly administered — but not substantively consolidated — debtors seek to cram down a joint plan over creditor objections.<sup>4</sup>

ership interests in the OpCo debtors, and the OpCo debtors’ loan was secured by the two hotels.

In 2010, the debtors filed for chapter 11, and the court approved joint administration of the five bankruptcy cases.<sup>6</sup> Thereafter, the debtors filed a chapter 11 plan predicated upon a third-party investor acquiring the OpCo debtors for \$30 million, thereby extinguishing the MezzCo debtors’ ownership interest in the OpCo debtors.<sup>7</sup> The chapter 11 plan did not seek to substantively consolidate the debtors.<sup>8</sup>

JPMCC objected to the chapter 11 plan and argued that § 1129(a)(10) applies on a per-debtor, not per-plan, basis.<sup>9</sup> JPMCC’s per-debtor interpretation would have blocked confirmation of the chapter 11 plan because (1) JPMCC, after purchasing the MezzCo debtors’ loan from Ashford, was the only impaired class of creditors at the MezzCo debtors; and (2) JPMCC voted to reject the chapter 11 plan, meaning that the MezzCo debtors did not have an impaired accepting class to satisfy § 1129(a)(10). The bankruptcy court confirmed the chapter 11 plan over JPMCC’s objection, and the district court affirmed.<sup>10</sup>

### The Ninth Circuit’s Decision

On appeal, a unanimous panel of Ninth Circuit judges held that the plain language of § 1129(a)(10) necessitates the per-plan approach because “once a single impaired class accepts a plan, section 1129(a)(10) is satisfied as to the entire plan.”<sup>11</sup> According to the court, this interpretation was persuasive because § 1129(a)(10) “makes no distinction concerning or reference to the creditors of different debtors under ‘the plan,’ nor does it distinguish between single-debtor and multi-debtor plans.”<sup>12</sup> Having determined that “the plan” in § 1129(a)(10) meant the joint chapter 11 plan for all five debtors, it was not the Ninth Circuit’s job “to modify the plain language of a statute by interpretation.”<sup>13</sup>

The Ninth Circuit also dismissed JPMCC’s argument that statutory context supported the per-debtor



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### Facts

The *Transwest* debtors’ corporate structure consisted of one holding company (the “HoldCo debtor”), two intermediate holding companies (the “MezzCo debtors”) and two operating companies (the “OpCo debtors,” together with the HoldCo debtor and MezzCo debtors, the “debtors”).<sup>5</sup> In 2008, Ashford Hospitality Financing, LP provided financing to the MezzCo debtors, and JPMCC 2007-C1 Grasslawn Lodging LLC provided financing to the OpCo debtors, to finance the purchase of two hotels — one in Hilton Head, S.C., and a second in Tucson, Ariz. The MezzCo debtors’ loan was secured by the MezzCo debtors’ 100 percent own-

<sup>1</sup> The authors thank Adam Rogoff for his valuable input on this article.

<sup>2</sup> *JPMCC 2007-C1 Grasslawn Lodging LLC v. Transwest Resort Props. Inc.* (In re *Transwest Resort Props. Inc.*), 881 F.3d 724, No. 16-16221, 2018 WL 615431 (9th Cir. Jan. 25, 2018). See 11 U.S.C. § 1129(a)(10) (“If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.”).

<sup>3</sup> Compare *In re Tribune Co.*, 464 B.R. 126, 180-84 (Bankr. D. Del. 2011) (“*Tribune*”) (adopting “per-debtor” interpretation of § 1129(a)(10)), and *In re JER/Jameson Mezz Borrower II LLC*, 461 B.R. 293, 302-03 (Bankr. D. Del. 2011) (same), with *In re Enron Corp.*, 2004 Bankr. LEXIS 2549, at \*234-36 (Bankr. S.D.N.Y. July 15, 2004) (adopting “per-plan” interpretation of § 1129(a)(10)), *In re Charter Commc’ns*, 419 B.R. 221, 229-30 (Bankr. S.D.N.Y. 2009) (same), and *In re SGPA Inc.*, 2001 Bankr. LEXIS 2291, at \*12-22 (Bankr. M.D. Pa. Sept. 28, 2001) (same).

<sup>4</sup> *In re 266 Washington Assocs.*, 141 B.R. 275, 287 (Bankr. E.D.N.Y. 1992).

<sup>5</sup> *Transwest*, 2018 WL 615431, at \*1.

<sup>6</sup> *Id.* at \*2.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* JPMCC also advanced a second chapter 11 plan objection regarding § 1111(b), which is not addressed in this article.

<sup>10</sup> See also David M. Neff and Eric E. Walker, “*Transwest*: How Many Impaired Classes Are Required for a Joint Plan Under § 1129(a)(10)?,” XXXVI *ABI Journal* 5, 16-17, 60, May 2017, available at [abi.org/abi-journal](http://abi.org/abi-journal).

<sup>11</sup> *Transwest*, 2018 WL 615431, at \*4.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

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**“Per Plan” or “Per Debtor”? Transwest Reignites the § 1129(a)(10) Debate**

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interpretation, thus disagreeing with *Tribune*.<sup>14</sup> In *Tribune*, the bankruptcy court held, in part, that § 1129(a)(10) should be interpreted as “per debtor” because § 102(7) provides that the “singular includes the plural” throughout title 11, and other subsections of § 1129(a) support a per-debtor interpretation.<sup>15</sup> Regarding § 102(7), the Ninth Circuit stated that applying it to the text of § 1129(a)(10) revises the statute to read “at least one class of claims that is impaired under the plans has accepted the plans,” which the court found to be consistent with the per-plan approach.<sup>16</sup>

As for other subsections of § 1129(a), the Ninth Circuit noted that, for example, § 1129(a)(3) (the good-faith requirement) does not need to be interpreted as “per debtor” because nothing in the plain text of the statute indicates that it applies in this manner.<sup>17</sup> Finally, the panel dismissed JPMCC’s objection that the chapter 11 plan substantively consolidated the debtors because this issue was not properly before the court on appeal and, to the extent that the per-plan approach would result in a “parade of horrors” for lenders, such “policy considerations [are] best left for Congress to resolve.”<sup>18</sup>

In her concurrence, Circuit Judge Michelle Friedland noted that the “better reading” of § 1129(a)(10) is that it applies on a per-plan basis, despite the statutory language being “somewhat ambiguous.”<sup>19</sup> Judge Friedland instead focused on JPMCC’s substantive consolidation argument and she agreed that the chapter 11 plan treated the debtors as a single entity, meaning that JPMCC’s claims were satisfied from the debtors’ substantively consolidated pool of assets.<sup>20</sup> This “*de facto*” substantive consolidation, rather than the court’s per-plan interpretation of § 1129(a)(10), was the root of JPMCC’s objection, because absent consensus, “there should have been an evaluation of whether substantive consolidation was appropriate before it (effectively) occurred.”<sup>21</sup> To allay the creditor’s concerns, Judge Friedland proposed that a court assess, on a case-by-case basis, whether the requirements of substantive consolidation have been met “if a creditor believes that a reorganization improperly intermingles different estates.”<sup>22</sup>

**Section 1129(a)(10)’s Legislative History**

Although the Ninth Circuit held that “the plain language of section 1129(a)(10) indicates that Congress intended a ‘per-plan’ approach,” the legislative history is not so clear.<sup>23</sup> The 1978 version of § 1129(a)(10) required that “at least one [non-insider] class of claims has accepted the plan.”<sup>24</sup> Commentators and courts agree that the accepting-class requirement was intended to address *In re Pine Gate*, a pre-

Bankruptcy Code single-asset real estate case in which the plan was crammed down on the debtor’s sole secured creditor by providing that creditor with a payment in cash equal to the fair market value of the real property.<sup>25</sup>

**A benefit to evaluating § 1129(a)(10) in the context of good faith is that it counters plan-related manipulation inherent in adopting one golden rule and furthers the reorganization goal of chapter 11. Such manipulation was at the core of the recommendation to remove § 1129(a)(10) from the Bankruptcy Code by the ABI Commission....**

After § 1129(a)(10) was enacted, confusion arose as to whether an unimpaired class deemed to have accepted a plan satisfied the accepting-class requirement.<sup>26</sup> “Impaired” was added to the statute in 1984 in order to address this issue, and a congressional report indicated that this change was intended to ensure that a class of creditors affected by the plan voted in its favor.<sup>27</sup>

Not all commentators agree with this conclusion. The final report published by the ABI Commission to Study the Reform of Chapter 11 concluded that “[a]lthough some courts and commentators suggest that section 1129(a)(10) was intended to ensure that a plan had some creditor support, neither the legislative history nor the Bankruptcy Code indicate such a purpose.”<sup>28</sup>

**Conclusion and Implications**

*Transwest* will likely reignite the debate as to the proper interpretation of § 1129(a)(10), one that has been dormant for more than five years.<sup>29</sup> Should a circuit split continue, debtors

14 *Id.* at \*5.15 *Id.*16 *Id.*17 *Id.*18 *Id.*19 *Id.* at \*6.20 *Id.*21 *Id.* at \*6-7.22 *Id.* at \*8.23 *Id.* at \*5.

24 See Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978).

25 See *In re Pine Gate Assocs. Ltd.*, No. B75-4345A, 1976 WL 359641, at \*17 (N.D. Ga. Oct. 20, 1976); *National Bankruptcy Review Commission Final Report, Bankruptcy: The Next 20 Years*, Oct. 20, 1997, at 584, n.1474 (stating that § 1129(a)(10) was enacted as a last-minute reaction to *Pine Gate*); *In re Duval Manor Assocs.*, 191 B.R. 622, 628 (Bankr. E.D. Pa. 1996) (stating that § 1129(a)(10) “was designed to ameliorate a perceived harshness inherent in the cramdown provisions” after *Pine Gate*); *After Pine Gate*, multiple courts construed its holding to allow for “maximum cramdown,” meaning confirmation of a debtor’s plan over the objection of the debtor’s only creditor, once that creditor received the fair-market value of the property. See Bruce A. Markell, “Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification,” 11 *Emory Bankr. J.* 1, 38 (1994-95) (discussing “maximum cramdown”); *In re Hobson Pike Assocs. Ltd.*, No. B76-2124A, 1977 WL 182364, at \*7 (N.D. Ga. Sept. 20, 1977); *In re Marietta Cobb Apartment Co.*, No. 76-B-1523, 1977 WL 182365, at \*4 (Bankr. S.D.N.Y. Sept. 9, 1977).

26 *In re Barrington Oaks Gen. P’ship*, 15 B.R. 952, 967 (Bankr. D. Utah 1981) (discussing contradictory inferences between §§ 1126(f) (deemed acceptance by unimpaired class), 1129(a)(6) (class either accepts plan or is unimpaired) and 1129(a)(10) (accepting class is required), and whether deemed acceptance by an unimpaired class satisfies § 1129(a)(10)).

27 See Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333 (1984); *In re Bloomingdale Partners*, 170 B.R. 984, 994 n.15 (Bankr. N.D. Ill. 1994) (citing 1983 Senate report that stated, “Paragraph (10) makes clear the intent of section 1129(a)(10) that one ‘real’ class of creditors must vote for the plan of reorganization”).

28 See *ABI Commission to Study the Reform of Chapter 11, Final Report and Recommendations* at p. 258, available at [commission.abi.org/full-report](http://commission.abi.org/full-report).

29 See *supra* n.3.

might selectively choose to file in certain jurisdictions, and the prevailing interpretation of § 1129(a)(10) will directly affect how a reorganization plan is formulated.

Although it is common for a joint plan to be filed for a multi-debtor enterprise in chapter 11, debtors should conduct an impaired-accepting-class analysis of each debtor, and thought should be given to including language stating that the plan is a separate plan for each debtor. If any debtor does not have an impaired accepting class, the per-debtor interpretation could require conversion to chapter 7 for those debtors who fail to satisfy § 1129(a)(10), while others pursue reorganization under chapter 11. The per-plan approach counters this result and affords flexibility to achieve a reorganization of the entire enterprise. Creditors aggrieved by the per-plan interpretation will likely focus on whether the joint plan (1) violates notions of corporate separateness (*i.e.*, each corporate entity is a distinct debtor that files a separate bankruptcy petition and has its own bankruptcy estate); (2) is a *de facto* or “deemed” substantive consolidation for plan-voting and distribution purposes;<sup>30</sup> and (3) is fair and equitable and does not unfairly discriminate.<sup>31</sup>

The concurrence’s suggestion that courts pursue a case-by-case analysis might present an alternative approach.

Although not suggested by Judge Friedland, a court could conduct a § 1129(a)(3) good-faith analysis to review a debtor’s plan and its formulation, an inquiry that is supported by analogous precedent in a similar context. In *Village at Camp Bowie I LP*, the Fifth Circuit held that the artificial impairment of claims to create an impaired accepting class in order to satisfy § 1129(a)(10), while not prohibited by the text of this section, must be evaluated through the good-faith lens of § 1129(a)(3).<sup>32</sup> Adopting this reasoning, a court could focus on how a plan is formulated and whether application of either the per-plan or per-debtor approach unduly prejudices debtors or creditors.

A benefit to evaluating § 1129(a)(10) in the context of good faith is that it counters plan-related manipulation inherent in adopting one golden rule and furthers the reorganization goal of chapter 11.<sup>33</sup> Such manipulation was at the core of the recommendation to remove § 1129(a)(10) from the Bankruptcy Code by the ABI Commission to Study the Reform of Chapter 11, a concern that should be addressed by Congress if courts fail to find a workable, practical solution.<sup>34</sup> **abi**

30 William H. Widen, “Corporate Form and Substantive Consolidation,” 75 *Geo. Wash. L. Rev.* 237, 254 (2007) (stating that in “deemed” substantive consolidation, distinct legal entities are not combined. Instead, votes on a plan, plan distribution, or both are computed ‘as if’ legal entities had been combined”). Although not cited in *Transwest*, the Third Circuit has held that for purposes of calculating quarterly U.S. Trustee fees under 11 U.S.C. § 1129(a)(12), such fees should be assessed for each debtor, absent substantive consolidation. See *In re Genesis Health Ventures Inc.*, 402 F.3d 416, 424 (3d Cir. 2005).

31 See 11 U.S.C. § 1129(b).

32 *W. Real Estate Equities LLC v. Vill. at Camp Bowie I LP (In re Vill. at Camp Bowie I LP)*, 710 F.3d 239, 247-48 (5th Cir. 2013).

33 See, e.g., *Bank of Am. Nat’l Trust & Sav. Ass’n v. 203 N. LaSalle St. P’shp.*, 526 U.S. 434, 453 (1999) (stating that policies underlying chapter 11 are preserving going concerns and maximizing property available to satisfy creditors).

34 See *ABI Commission Final Report*, n.28 at p. 260 (“The Commissioners debated the utility of section 1129(a)(10), focusing on whether the provision protected creditor interests or simply allowed creditors to hold up the confirmation process. For example, the Commissioners discussed cases with a limited number of impaired creditor classes and a lender or other large creditor who purchases a sufficient number of claims in each class to control the plan vote. By voting against the plan in each of these classes, that single creditor can block a cramdown because there will be no accepting impaired class of creditors for purposes of section 1129(a)(10).”).

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