UTILIZING THE FOURTH OPTION: EXAMINING THE PERMISSIBILITY OF STRUCTURED DISMISSALS THAT DO NOT DEVIATE FROM THE BANKRUPTCY CODE'S PRIORITY SCHEME

ABSTRACT

Following a § 363 asset sale, the Bankruptcy Code provides a debtor with three options to close its chapter 11 case: (1) request confirmation of a liquidation plan; (2) convert the chapter 11 case to a chapter 7 case; or (3) request dismissal of the case. There is a fourth option, however: a structured dismissal. Structured dismissals are controversial because the Code does not expressly provide for them. Opponents thus equate structured dismissals with impermissible sub rosa plans. Existing caselaw does not provide a clear answer as to whether courts have the discretionary authority, under the Code, to authorize structured dismissals. In 2015, the Third Circuit was the first Court of Appeals to grant a structured dismissal settlement. In approving the structured dismissal, the court also held that, in rare instances, a structured dismissal can deviate from the priority scheme in § 507. Through the structured dismissal, the Third Circuit engineered a mechanism for parties to evade the mandatory priority scheme.

This Comment argues that while the Third Circuit had the statutory authority to grant a structured dismissal, the court did not have the authority, statutory or otherwise, to approve a dismissal that deviated from § 507. This Comment takes the position that the Code's priority scheme applies to all estate distributions in a chapter 11 proceeding, including a structured dismissal.

INTRODUCTION

Like most legal proceedings, a number of administrative fees encumber bankruptcy filings.[1] To circumvent costly proceedings that do not maximize the value of a bankruptcy estate, select bankruptcy courts have approved structured dismissals in chapter 11 cases.[2] A structured dismissal is a cross between a dismissal and a confirmation order, which dismisses a chapter 11 case with additional pre-determined provisions.[3] Structured dismissals are typically consensual agreements between the debtor and some, if not all, of the creditors.[4]

In a standard chapter 11 proceeding, the parties first propose a plan of reorganization.[5] The plan must meet certain requirements under § 1129 of the Bankruptcy Code (the "Code").[6] If the plan satisfies § 1129, the bankruptcy court will approve the plan.[7] When the plan is substantially fulfilled, the court closes the case with no additional strings attached.[8] This dismissal returns the debtor to its pre-bankruptcy status.[9]

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1 *See* 28 U.S.C. § 1930 (2012). Specifically under § 1930(a)(3), "[t]he parties commencing a case under title 11 shall pay to the clerk of the district court or the clerk of the bankruptcy court, if one has been certified pursuant to section 156(b) of this title, the following filing fees: . . . (3) For a case commenced under chapter 11 of title 11 . . . $1,167." ADMIN. OFFICE OF THE U.S. COURTS, BANKRUPTCY BASICS (2011), http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics ("The courts are required to charge a $1,167 case filing fee and a $550 miscellaneous administrative fee.").

2 *See, e.g.*, *In re* Felda Plantation, LLC, No. 9:11-bk-14614-BSS., 2012 WL 1071671 (Bankr. M.D. Fla. Mar. 26, 2012) (granting a structured dismissal because of consensual agreement between debtor and creditors); *see also* Norman L. Pernick & G. David Dean, *Structured Chapter 11 Dismissals: A Viable and Growing Alternative After Asset Sales*, AM. BANKR. INST. J. 1 (June 2010) http://www.coleschotz.com/2B7963/assets/files/News/293.pdf (noting that, as late as 2010, "cases involving structured dismissals ha[d] not yet resulted in memorandum decisions (published or unpublished), [but] there ha[d] been a number of rulings that are useful to understanding how structured dismissals have been . . . viewed by courts").

3 COMM'N TO STUDY THE REFORM OF CHAPTER 11, AM. BANKR. INST., FINAL REPORT AND RECOMMENDATIONS 270 (2014).

4 *See In re Felda Plantation*, 2012 WL 1071671 (granting a structured dismissal because of a consensual agreement between debtor and creditors). All parties were placed on notice of the structured dismissal motion and no one objected. *Id.*; *see also* Charles M. Ollerman & Mark G. Douglas, *Taking a Stand Where Few Have Trodden: Structured Dismissal Held Clearly Authorized by the Bankruptcy Code*, JONES DAY, Sept./Oct. 2014, http://www.jonesday.com/taking-a-stand-where-few-have-trodden-structured-dismissal-held-clearly-authorized-by-the-bankruptcy-code-10-01-2014/.

5 Ollerman & Douglas, *supra* note 4.

6 11 U.S.C. § 1129 (2012). The court will only confirm a consensual plan that meets all of the requirements prescribed in part (a) of § 1129. *Id.* § 1129(a).

7 Ollerman & Douglas, *supra* note 4.

8 *Id.*

9 11 U.S.C. § 349.

Pre-negotiated asset sales under § 363 serve as an alternative to the standard chapter 11 process.[10] A § 363 sale allows a debtor to liquidate most, if not all, of its assets free of existing liens and interests.[11] Following a § 363 sale, a debtor has a handful of options to finalize its chapter 11 case.[12] Debtors most commonly utilize one of the following three options: (1) request confirmation of a liquidation plan; (2) convert the chapter 11 case to a chapter 7 case; or (3) request a dismissal of the case.[13]

More recently, courts have allowed debtors and creditors to utilize structured dismissals as a fourth option.[14] Structured dismissals are particularly appealing to debtors that have disposed of assets through a sale because the dismissals are less costly and typically more expeditious than proposing and confirming a reorganization plan.[15] Structured dismissals are controversial, however, because they are not expressly provided for under the Code.[16]

Two notable opponents of structured dismissal are the United States Trustee ("UST") and the American Bankruptcy Institute.[17] In the wake of the growing popularity of structured dismissals, the UST co-authored and published an article that delineated several objections to such dismissals.[18] The UST primarily argued that structured dismissals fail to afford parties with the protections provided in a standard confirmation process and therefore "strongly resemble impermissible *sub rosa* plans."[19] Additionally, the American

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> A dismissal of a case – (2) vacates any order, judgment, or transfer ordered, under section 522(i)(1), 542, 550, or 553 of this title; and (3) revests the property of the estate in the entity in which such property was vested immediately before the commencement of the case under this title.

10 Ollerman & Douglas, *supra* note 4.

11 Douglas E. Deutsch & Michael G. Distefano, *The Mechanics of a* § *363 Sale*, AM. BANKR. INST. J. 1 (Feb. 2011), http://www.chadbourne.com/files/Publication/4dbdca20-38ed-4d4c-bc04-a637b7a6997d/Presentation/PublicationAttachment/962b73fc-20b1-4652-88a3-a8b84134f4b8/blocks%202-11.pdf.

12 Ollerman & Douglas, *supra* note 4.

13 *Id.*; Pernick & Dean, *supra* note 2.

14 Pernick & Dean, *supra* note 2.

15 *In re* Petersburg Regency LLC, 540 B.R. 508, 532 (Bankr. D.N.J. 2015) (noting that granting the structured dismissal would prevent more "expensive litigation . . . .").

16 COMM'N TO STUDY THE REFORM OF CHAPTER 11, *supra* note 3, at 270.

17 Amir Shachmurove, *Another Way Out: Structured Dismissals in* Jevic*'s Wake*, NORTON BANKR. L. ADVISER 1 (Thomson Reuters, Saint Paul, Minn.), Nov. 2015, Westlaw, 2015 No. 11 Norton Bankr. L. Adviser NL 1.

18 Lisa L. Lambert, Nan Roberts Eitel & T. Patrick Tinker, *Structured Dismissals, or Cases Dismissed Outside of Code's Structure?*, AM. BANKR. INST. J. 20 (Mar. 2011), http://www.justice.gov/sites/default/files/ust/legacy/2011/07/13/abi_201103.pdf; Shachmurove, *supra* note 17.

19 Lambert, Eitel & Tinker, *supra* note 18, at 20.

Bankruptcy Institute's Commission to Study the Reform of Chapter 11 released a lengthy report suggesting that Congress amend the Code to clarify that structured dismissals are impermissible.[20]

In 2015, the Third Circuit was the first Court of Appeals to approve structured dismissals in *Official Committee of Unsecured Creditors v. CIT Group/Business Credit Inc. (In re Jevic Holding Corp.)*.[21] Prior to the appeal, a New Jersey trucking company filed for bankruptcy.[22] Following the debtor's § 363 sale, the trucking company and select creditors agreed upon a settlement that dictated how they would disperse the remaining assets of the company.[23] The bankruptcy court approved the settlement and dismissed the case, even though the agreement intentionally left out a class of priority claimants.[24] The neglected claimants appealed.[25]

Two issues were presented on appeal in *In re Jevic*.[26] First, does a chapter 11 case dismissal always amount to a "hard reset"?[27] In other words, does a dismissal always return the debtor to its prebankruptcy status, or does the court have discretion to issue any additional requirements or provisions attached to a chapter 11 case dismissal?[28] In approving structured dismissals, the court reasoned that a dismissal does not have to amount to a hard reset.[29]

Second, is it permissible for a structured dismissal settlement to deviate from the Code's priority scheme under § 507?[30] The court held that structured dismissals may deviate, but only in rare instances.[31]

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[20] COMM'N TO STUDY THE REFORM OF CHAPTER 11, *supra* note 3, at 272–73; *see also* Shachmurove, *supra* note 17.
[21] 787 F.3d 173 (3d Cir. 2015).
[22] *Id.* at 176.
[23] *Id.*
[24] *Id.*
[25] *Id.* at 179.
[26] *Id.* at 175.
[27] *Id.* at 181.
[28] *Id.*
[29] *Id.*
[30] *Id.* at 175.
[31] *Id.* The "rare instances" the Third Circuit noted will depend on the facts of each case. In *In re Jevic*, for example, the court found that the structured dismissal was the "least bad alternative" because there was "no prospect" of a plan being confirmed and conversion to chapter 7 would have resulted in the secured creditors taking their collateral "in short order." *Id.* at 185. In *In re Petersburg Regency LLC*, the Bankruptcy Court for the District of New Jersey found "the instant case is stronger than *Jevic* because all creditors, except the Harmons, are receiving a distribution and the 'class-skipping' issue which figured in *Jevic* is not present here." 540 B.R. 508, 532 (Bankr. D.N.J. 2015). The court also noted four other factors that constituted the requisite "rare instances": (1) no classes are being skipped; (2) dismissing the case now would prevent "many more

Keeping in mind that one of the Code's core goals is to maximize the value of an estate, bankruptcy parties must seek creative options to resolve chapter 11 cases.[32] This Comment proceeds in two parts and examines the permissibility and necessity of structured dismissals that do not deviate from the Code's priority scheme. First, this Comment defends the proposition that structured dismissals are permissible under the Code. Second, this Comment addresses the current split between the Third and Fifth Circuits regarding the applicability of §§ 507 and 1129 of the Code to settlement agreements.[33] After careful analysis, this Comment contends that §§ 507 and 1129 apply to settlement agreements in the context of structured dismissals.

I. FRAMEWORK

This section of the Comment provides an overview of the seminal *In re Jevic* case and structured dismissals in four parts. First, it recounts the facts and Third Circuit's holding in *In re Jevic*. Next, it describes what structured dismissals are and how they work by outlining the types of remedies that derive from structured dismissals. Then, this section explains the three standard options to finalize a chapter 11 case provided by the Code. Finally, this section concludes by explaining the Code's priority scheme.

A. Highlighting the Case: In re Jevic Holding Corp.

In 2006, Sun Capital Partners acquired Jevic Transportation, Inc., a New Jersey trucking company, in a leveraged buyout.[34] A group of lenders, led by CIT Group, funded the acquisition.[35] CIT gave Jevic an $85 million line of

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months or years of continuing and expensive litigation . . .;" (3) the secured claims "far exceeded" the value of the collateral; and (4) no realistic possibility of a reorganization or conversion to chapter 7 existed. *Id.*

32 *See* Toibb v. Radloff, 501 U.S. 157, 163 (1991); *In re Jevic*, 787 F.3d at 186.

33 *Compare In re Jevic*, 787 F.3d at 186 (permitting a structured dismissal that deviated from the Code's priority scheme), *with In re* AWECO, Inc., 725 F.2d 293, 298 (5th Cir. 1984) (determining the settlement was not "fair and equitable" for two reasons: (1) it placed a junior creditor's interest before that of the government's senior interest; and (2) the approval was not "informed" because the value of the estate was based on "guesses and conjecture"), *and* Motorola, Inc. v. Official Comm. of Unsecured Creditors (*In re* Iridium Operating LLC), 478 F.3d 452, 466–67 (2d Cir. 2007) (holding the settlement agreement was not an impermissible *sub rosa* plan of reorganization because the agreement was in the best interest of the estate).

34 *In re Jevic*, 787 F.3d at 175. "A leveraged buyout (LBO) is the acquisition of another company using a significant amount of borrowed money (bonds or loans) to meet the cost of acquisition. The assets of the company being acquired are often used as collateral for the loans, along with the assets of the acquiring company." *Leveraged Buyout–LBO*, INVESTOPEDIA, http://www.investopedia.com/terms/l/leveragedbuyout.asp (last visited March 11, 2016).

35 *In re Jevic*, 787 F.3d at 175.

credit, conditioned upon Jevic maintaining at least $5 million in assets and collateral.[36] In the following years, Jevic's business continued to plummet; by May 2008, Jevic's board of directors agreed to file for chapter 11.[37] Jevic ceased operations and notified its employees of their immediate termination.[38]

At the time of filing, Jevic owed over $73 million to both its first priority secured creditors (CIT and Sun Capital) and its general unsecured creditors.[39] An official committee was developed to represent the unsecured creditors.[40] The committee sued the secured creditors for fraudulent conveyance, claiming that Sun Capital, with funds from CIT, acquired Jevic with improper projections of profitability.[41] Additionally, a group of terminated Jevic employees filed a class action suit against the secured creditors and Jevic because Jevic did not provide its employees with the requisite sixty-day notice of termination prior to layoffs, as required by the New Jersey Worker Adjustment and Retraining Notification Act ("WARN Act").[42]

The United States Bankruptcy Court for the District of Delaware partially granted and partially denied Jevic's motion to dismiss the fraudulent transfer suit. The court held that the secured creditors' acquisition of Jevic constituted both a fraudulent transfer and preferential transfer under §§ 547 and 548;[43] however, the secured creditors' actions did not constitute a fraudulent transfer under § 544.[44] The ex-employees obtained a similar mixed result in their WARN Act suit.[45] The court entered a ruling against Jevic because it determined that Jevic fell within the WARN Act's definition of "employer."[46] The court granted the secured creditors' summary judgment motion, however, because it determined that the secured creditors did not fall within this same definition.[47]

Following the court's ruling, the committee, secured creditors, terminated employees, and Jevic's board of directors met to negotiate a settlement for the

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36 *Id.*
37 *Id.*
38 *Id.* at 175–76.
39 *Id.* at 176.
40 *Id.*
41 *Id.*
42 *Id.*
43 *Id.*
44 *Id.*
45 *Id.*
46 *Id.*
47 *Id.*

fraudulent conveyance suit.[48] The committee concluded that a settlement was a more desirable solution in light of Jevic's limited remaining assets ($1.7 million in cash).[49] In the interim between the original bankruptcy filing date and the settlement agreement meeting, Jevic liquidated its assets.[50] The final terms of the settlement agreement allocated Jevic's remaining $1.7 million to taxes, administrative creditors, and unsecured creditors.[51] Specifically, the settlement accomplished four things:

> (1) The involved parties would exchange releases of their claims against each other, and the fraudulent conveyance action would be dismissed with prejudice;
> (2) CIT would pay $2 million into an account earmarked to pay Jevic's and the committee's legal fees and other administrative expenses;
> (3) Sun Capital would assign its lien on Jevic's remaining $1.7 million to a trust, which would pay tax and administrative creditors first and then the general unsecured creditors on a pro rata basis; and
> (4) Jevic's chapter 11 case would be dismissed.[52]

Notably, the agreement did not provide for any distribution to the drivers (Jevic's ex-employees), even though they had an uncontested WARN Act claim.[53] The drivers argued that a portion of the claim was a priority wage claim under § 507(a)(4), and their claim was entitled to a higher priority than the tax and unsecured creditors' claims.[54]

The ex-employees rejected the settlement because creditors of a lower priority received the remaining Jevic assets.[55] The court ignored the employees' objection and approved the settlement agreement.[56] The court dismissed the case as a structured dismissal, conditioned on the parties' execution of the terms of the settlement agreement.[57]

48 *Id.*
49 *Id.*
50 *Id.*
51 *Id.* at 177.
52 *Id.*
53 *Id.*
54 *Id.*
55 *Id.* at 178.
56 *Id.*
57 *Id.*

B. *How Structured Dismissals Work*

Generally, before a party may file a motion for a structured dismissal to conclude its bankruptcy case, a § 363 sale occurs.[58] Section 363 sales are increasingly used by debtors that wish to sell substantially all of their assets instead of attempting to restructure through the chapter 11 process.[59] Under § 363, the debtor or a court appointed trustee may sell any asset in which the debtor has a legal or equitable ownership interest at the beginning of the bankruptcy case.[60] Anyone except the trustee or an officer of the court may purchase assets from the sale.[61]

There are two types of § 363 sales: those made (1) in the ordinary course of business; or (2) outside the ordinary course of business.[62] Allowing the sale of property conducted in the ordinary course of business enables the debtor to continue operations while in bankruptcy as long as the court approves the sale.[63] In contrast, the sale of property conducted outside the ordinary course of business requires notice and hearing.[64] Notice and hearing is a prerequisite to the sale's approval because it provides creditors the opportunity to object.[65] If there are no timely objections, the § 363 sale may proceed.[66] If there are objections to the sale, the court will conduct a hearing and determine whether the sale is appropriate.[67]

Debtors generally utilize structured dismissals if one of three scenarios occurs following a § 363 asset sale: (1) the debtor is unable to pay administrative debts or fund a chapter 11 plan; (2) the debtor has sufficient funds from the asset sale to fund a chapter 11 plan, but doing so would significantly drain the available funds for creditor distribution; or (3) the debtor has remaining assets after a § 363 sale and creditors agree to negotiate an out-

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58 John Kane, *Structured Dismissals – How They Work Part I: Court Authority for Alternative Ending*, INSOLVENCY INSIGHTS BLOG (Sept. 22. 2014), http://insolvencyinsights.com/2014/09/22/structured-dismissals-how-they-work-part-i-court-authority-for-an-alternative-ending/.

59 Pernick & Dean, *supra* note 2.

60 Philip A. Schovanec, Comment, *The Sale of Property Under Section 363: The Validity of Sales Conducted Without Proper Notice*, 46 OKLA. L. REV. 489, 495 (1993).

61 *Id.* at 494.

62 *Id.* at 496.

63 *Id.* at 496–97.

64 *Id.* at 496.

65 *Id.* at 498.

66 *Id.* at 499.

67 *Id.*

of-court agreement to administer the remaining assets.[68] The purpose of each scenario is to demonstrate that there are insufficient post-363 sale assets to make necessary payment distributions to creditors and fulfill a chapter 11 reorganization plan.[69]

For the court to grant a structured dismissal, the movant must demonstrate a cause for dismissal.[70] The three aforementioned scenarios are sufficient reasons to establish cause.[71] A structured dismissal goes beyond a standard chapter 11 dismissal.[72] While a standard chapter 11 dismissal will simply end all court proceedings,[73] a structured dismissal will end all court proceedings *and* contain varying "bells and whistles," such as the orders, settlements, and provisions that continue to govern the dismissal.[74]

1. *Structured Dismissal Remedies*

The facts and desired outcome of a case will determine what bells and whistles are included in a structured dismissal. As previously discussed, a structured dismissal does not simply dismiss a bankruptcy case. Instead, courts utilizing structured dismissals will dismiss cases and mandate additional requirements for the parties to fulfill—i.e., bells and whistles. Typically, bells and whistles fall into at least one of four categories: (1) release and exculpation provisions; (2) claims reconciliation processes and distribution procedures; (3) carve-outs and "gift" trusts; and (4) enforceability of prior orders and retention of jurisdiction.[75]

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68 Peter M. Sweeney, *Delaware Views from the Bench–Structured Dismissals*, 4 BLAKELY & BLAKELY Q. (Winter 2014), http://www.bandblaw.com/newsletter/archived/2014WinterBBQuarterly.pdf; *see also* JAY R. INDYKE, ET AL., STRAFFORD, CHAPTER 11 STRUCTURED DISMISSALS: VIABLE EXIT STRATEGY OR IMPERMISSIBLE UNDER BANKRUPTCY CODE? (2014), http://media.straffordpub.com/products/chapter-11-structured-dismissals-viable-exit-strategy-or-impermissible-under-bankruptcy-code-2014-10-28/presentation.pdf.

69 JAY R. INDYKE, ET AL., *supra* note 68.

70 Kane, *supra* note 58.

71 Pernick & Dean, *supra* note 2, at 2.

72 Kane, *supra* note 58.

73 U.S. BANKR. COURT CENT. DIST. OF CAL., *Dismissal, Conversion & Closing of A Bankruptcy Case, What are the Differences Between Them?*, http://www.cacb.uscourts.gov/faq/dismissal-conversion-closing-bankruptcy-case-what-are-differences-between-them (last visited Feb. 26, 2016).

74 Kane, *supra* note 58; Sweeney, *supra* note 68.

75 Pernick & Dean, *supra* note 2, at 2.

a. Release and Exculpation Provisions

The first category of relief that courts provide through structured dismissals eliminates the debtor's risk of potential future obligations by adding either release provisions or exculpatory provisions to the final court order.[76] Both provisions relieve parties from liability on a claim.[77] These provisions are either specific to one or more certain, identified claims or apply more broadly to cover potential claims.[78]

Release provisions discharge a party within a suit from another related or non-related pending course of action.[79] They are commonly found in settlement agreements where parties mutually agree to settle one claim in exchange for a release from another pending suit.[80] The following boilerplate release provision of a settlement agreement illustrates how comprehensive these provisions can be:

> Each Party hereby fully, finally, and forever releases and discharges the other Party, and any and all of its respective past, present, and future affiliates from any and all actions, causes of action, claims, demands, damages, debts, losses, costs, expenses, attorney fees or other liabilities of every kind and nature whatsoever; whether legal or equitable and whether known or unknown, arising out of, resulting from, or relating to, in any manner, the Action, the claims and causes of action that were or could have been asserted relating to the Action, or any facts or circumstances related to the Action.[81]

Exculpatory provisions prevent a party from pursuing a legal claim against another party that it otherwise could assert.[82] Though parties are generally free to devise their own terms of a release or exculpatory provision, parties cannot

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76 *In re* Naartjie Custom Kids, Inc., 534 B.R. 416, 419 (Bankr. D. Utah 2015) ("The Settlement Agreement also provided that customary release and exculpation provisions will be included in the order resolving the case.").

77 *See, e.g.*, *In re* Biolitec, Inc., 528 B.R. 261, 266 (Bankr. D.N.J. 2014) (outlining the provisions of the structured dismissal, which included releasing the trustee from any liability connected to the chapter 11 case); *In re* Strategic Labor, Inc., 467 B.R. 11, 17 n.10 (Bankr. D. Mass. 2012) (listing provisions commonly found in structured dismissal agreements and the controversy associated with them).

78 Pernick & Dean, *supra* note 2, at 3.

79 *See In re Biolitec*, 528 B.R. at 266.

80 *See* Federal Deposit Insurance Corp., *Settlement Agreement Between FDIC and PCMG*, April 2011, https://www.fdic.gov/about/freedom/plsa/oh_amtrust_bank_cleveland_1.pdf.

81 *Id.*

82 *See In re* Century Elecs. Mfg., Inc., 345 B.R. 33, 34 (Bankr. D. Mass. 2006); Neal J Suit, *Understanding the Differences Between Indemnity and Exculpatory Clauses*, CAPITAL (2013), http://www.ccsb.com/pdf/Publications/RealEstate/Differences_Between_Indemnity_and_Exculpatory_Clauses.pdf.

create provisions that will limit their liability in a manner that violates the law or is against public policy.[83]

b. Reconciliation Process

In a structured dismissal order that contains reconciliation provisions, a party's objective is to reconcile claims in a speedy and cost-effective fashion.[84] The reconciliation orders will often contain provisions similar to those found in chapter 11 confirmation plans.[85] The reconciliation process requires the debtor to compare creditors' claims with its own records to confirm or reject inconsistencies between claims filed by creditors and the debtor's schedule of liabilities.[86] This process is necessary because some creditors will file invalid or inflated claims.[87]

After a debtor files a bankruptcy petition, the debtor is required to submit a schedule of assets and liabilities.[88] The schedule outlines the debtor's current assets and debts owed to creditors. If the debtor did not list an obligation owed to a creditor, that creditor must file a proof of claim to participate in a distribution.[89] Although the Code is silent about the time period within which a party should file its proof of claim, a court will typically set a filing deadline, known as the "bar date."[90]

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83 *See* Bisso v. Inland Waterways Corp., 349 U.S. 85, 90 (1955). The California Supreme Court devised an effective six criteria test to determine when contractual agreements affect public policy. Tunkl v. Regents of Univ. of Cal., 60 Cal. 2d 92, 102 (1963).

84 Pernick & Dean, *supra* note 2, at 3.

85 *Id.*

86 *See* *Reconciliation*, INVESTOPEDIA (Feb. 26. 2016), http://www.investopedia.com/terms/r/reconciliation.asp?optm=sa_v2.

87 Carriane J. M. Balser & Heather L. Hyde, *Effective Claims Management in Bankruptcy–Planning Teamwork and Documentation*, AM. BANKR. INST. J., Jul./Aug. 1998, http://www.abi.org/abi-journal/effective-claims-management-in-bankruptcy-planning-teamwork-and-documentation.

88 ADMIN. OFFICE OF THE U.S. COURTS, *supra* note 1.

89 11 U.S.C. § 501(a) (2012). Filing a proof of claim is permissive, but a creditor cannot participate in a distribution if it does not have a claim. FED. R. BANKR. P. 3002(a), (c). Furthermore, certain claims are excepted from the claim filing requirement. *See* 4 COLLIER ON BANKRUPTCY ¶ 501.01[3] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.).

90 The Federal Rules of Bankruptcy Procedure control the timely filing of proofs of claims. *See* FED. R. BANKR. P. 3003(a). Subsection (c)(3) gives the bankruptcy court the authority to set the "bar date," which courts strictly enforce. *See id.* 3003(c)(3); *In re* Analytical Sys., Inc., 933 F.2d 939, 942 n.5 (11th Cir. 1991).

c. Gifting

Creditor classes utilize gifting as a mechanism to obtain consensual structured dismissals.[91] Gifting is best illustrated by the First Circuit's decision in *In re SPM Manufacturing Corp.*[92] In that case, the debtor sold all of its assets in a § 363 sale because a chapter 11 reorganization was not feasible.[93] The secured creditor maintained a lien on substantially all of the debtor's assets.[94] Under the Code's priority scheme, the secured creditor would receive all of the proceeds from the asset sale, leaving the unsecured creditors empty handed.[95]

In an out-of-court negotiation, the secured creditor and the unsecured creditors' committee agreed to cooperate in both crafting a reorganization plan and the remaining bankruptcy proceedings in exchange for a portion of the secured creditor's proceeds.[96] The agreement was beneficial to the secured creditor who wanted to end the costly and time-consuming bankruptcy proceedings without interference from the unsecured creditors.[97] The debtor objected to the secured creditor's motion seeking approval to distribute a portion of the sale proceeds to the unsecured creditors.[98] The debtor argued that the proposed distribution improperly paid unsecured creditors before administrative creditors with a higher priority under § 507.[99] The court reasoned that the secured creditor was guaranteed all available proceeds from the sale.[100] No chance existed that the unsecured creditors or other administrative creditors would receive any distribution from the sale.[101] Therefore, the court concluded that creditors were free to distribute their bankruptcy dividends however they chose.[102]

In *In re SPM Manufacturing*, the creditor was free to distribute a portion of its proceeds in consideration for the unsecured creditors' cooperation because

91 Pernick & Dean, *supra* note 2, at 1.
92 984 F.2d 1305 (1st Cir. 1993).
93 *Id.* at 1307.
94 *Id.*
95 *Id.* at 1308.
96 *Id.*
97 *Id.*
98 *Id.* at 1309.
99 *Id.*
100 *Id.* at 1308.
101 *Id.*
102 *Id.* at 1313.

the proceeds belonged exclusively to the secured creditor.[103] In the context of structured dismissals, a secured creditor may include gifting provisions in the dismissal agreement to induce other parties to consent to the dismissal.[104]

d. Enforceability of Prior Orders and Retention of Jurisdiction

The fourth type of relief in structured dismissal orders is retention orders. Notwithstanding § 349, bankruptcy courts will retain jurisdiction over matters even after they dismiss a case.[105] Retention provisions are useful in structured dismissals because they authorize a specific court to implement the dismissal order, resolve any subsequent matters, or both.[106] If the court adds a retention order, the court will retain jurisdiction over the matter even after it has dismissed the case. Without retention provisions, the previous orders and judgments in the bankruptcy case are vacated under § 349.[107]

C. Exit Strategies

The Code expressly provides three options for a debtor to exit a chapter 11 case: (1) confirming a reorganization plan; (2) converting the case from chapter 11 to chapter 7; or (3) dismissing the case with no additional bells and whistles. Each option is briefly discussed in the following subsections.

1. Confirmation of a Reorganization Plan

A debtor's chapter 11 plan details its reorganization strategy so it can keep its business alive and repay creditors.[108] Businesses can utilize one of two types of reorganization strategies: (1) reduce payments to creditors while extending the payment time frame and laying off employees; or (2) cancel existing purchase orders.[109] A court is likely to confirm a chapter 11 plan that is feasible

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103 *Id.*

104 Pernick & Dean, *supra* note 2, at 58.

105 Ollerman & Douglas, *supra* note 4.

106 *Id.*

107 BLOOMBERG LAW: BANKRUPTCY TREATISE, pt. 1, ch. 41, at 7 (D. Michael Lynn et al. eds., 2016), www.bloomberglaw.com/content/bankruptcytreatise; *see* 11 U.S.C. § 349(b)(2) (2012) ("Unless the court, for cause, orders otherwise, a dismissal of a case other than under section 742 of this title—(2) vacates any order, judgment, or transfer ordered, under sections 522(i)(1), 542, 550, or 553 of this title.").

108 United States Courts, *Chapter 11-Bankruptcy Basics*, http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basic (last visited Feb. 26, 2016).

109 *How Cases Move Through Federal Courts*, FED. JUD. CTR., http://www.fjc.gov/federal/courts.nsf/autoframe?openagent&nav=menu4c&page=/federal/courts.nsf/page/263?opendocument (last visited Aug. 28, 2016).

and in the best interests of the debtor's creditors.[110] Any proposed chapter 11 plan must comply with §§ 1123 and 1129 of the Code, among others.[111]

Requirements for the content of a chapter 11 plan are enumerated in § 1123.[112] The plan provisions in subsection (a) are mandatory, whereas the provisions in subsection (b) are discretionary.[113] Under subsection (a), the plan must specify the classes of claims (i.e., secured or unsecured), detail the treatment for each class, and provide plausible means to implement the plan.[114]

The Code's plan confirmation requirements are enumerated in § 1129.[115] Subsections (a)(1) through (6) and (a)(11) through (13) pertain to the plan itself and stipulate the necessary elements required to confirm a plan.[116] For example, (a)(3) requires the plan be proposed in good faith.[117] The remaining sections pertain to the treatment of classes of claim or interest holders.[118]

With respect to structured dismissals, the most significant requirement is § 1129(a)(8).[119] Under this provision, each class of claims or interests must vote to accept the proposed reorganization plan.[120] A collectively accepted plan is called a consensual plan.[121]

If all the requirements in § 1129(a), except (a)(8), are met, the court may still confirm the plan so long as it is fair and equitable.[122] This type of plan is a nonconsensual plan.[123] The Supreme Court held, "[t]he words 'fair and equitable' are terms of art—they mean that 'senior interests are entitled to full priority over junior ones.'"[124] "[N]o class may participate in distribution under

110 *See* 11 U.S.C. § 1129(a)(7)(A)(ii), (11); *see also* Pernick & Dean, *supra* note 2, at 58.
111 Pernick & Dean, *supra* note 2, at 58.
112 11 U.S.C. § 1123.
113 BLOOMBERG LAW: BANKRUPTCY TREATISE, *supra* note 107, pt. V, ch. 172.
114 11 U.S.C. § 1123(a)(1), (3), (5).
115 *Id.* § 1129.
116 John D. Ayer, Michael L. Bernstein & Jonathan Friedland, *Chapter 11-"101": Confirming a Plan*, AM. BANKR. INST. J., Dec.-Jan 2005, at 16.
117 11 U.S.C. § 1129.
118 Ayer, Bernstein & Friedland, *supra* note 116, at 16.
119 *See* 11 U.S.C. § 1129(a)(8).
120 *See id.* § 1129(a)(7).
121 *In re* United Marine, 197 B.R. 942, 948 (Bankr. S.D. Fla. 1996).
122 *See* 11 U.S.C. § 1129(b).
123 *In re* Genesis Health Ventures, Inc., 266 B.R. 591, 599 (Bankr. D. Del. 2001).
124 *In re* AWECO, Inc., 725 F.2d 293, 298 (5th Cir. 1984) (first citing SEC v. Am. Trailer Rentals Co., 379 U.S. 594, 612 (1965); then citing Protective Comm. for Indep. Stockholders of TMT Trailer Ferry v. Anderson, 390 U.S. 414, 441 (1968)).

the plan unless classes having priority are compensated in full."[125] This concept is commonly referred to as the absolute priority rule.[126] Essentially, the absolute priority rule reinforces the policies underlying the bankruptcy priority scheme codified in § 507.[127]

2. *Chapter 11 to Chapter 7 Conversion*

The goal of chapter 11 is reorganization, whereas, the goal of chapter 7 is liquidation and the fair treatment of creditors.[128] Under § 1112, a debtor may convert a chapter 11 case unless one of three scenarios exists: "(1) the debtor is not a debtor in possession; (2) the case originally was commenced as an involuntary case under [chapter 11]; or (3) the case was converted to a case under [chapter 11] other than on the debtor's request."[129] Upon conversion to a chapter 7 case, the court appoints a trustee to take control of liquidating the remaining assets and distributing the proceeds among creditors.[130] Because a court-appointed trustee immediately takes control of the estate in a chapter 7 case, the debtor has a limited role in the remainder of the process.[131] The debtor in chapter 7 primarily wants to retain property that is exempt from liquidation and receive a discharge for any remaining debts.[132]

3. *Dismissal with No "Bells and Whistles"*

When a bankruptcy court dismisses a case, the court and adversary proceedings related to the case cease.[133] Dismissals can occur voluntarily (at the debtor's request) or involuntarily (at the request of the creditors or sua sponte).[134] Section 1112(b) discusses the framework for chapter 11 dismissals.

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125 9D AM. JUR. 2d BANKR. § 2978.

126 *Id.*

127 *See* 11 U.S.C. § 1129(b)(1). Confirmable nonconsensual plans must still satisfy all requirements under § 1129(a), except (a)(8). *Id.* Section 1129(a)(9) mandates that a reorganization plan must satisfy § 507 to be confirmable. *Id.* § 1129(a)(9).

128 *See In re* Ionosphere Clubs, Inc., 98 B.R. 174, 176 (Bankr. S.D.N.Y. 1989) ("The policy of equality among creditors as articulated by IAM may be of significance in liquidation cases under Chapter 7, however, the paramount policy and goal of Chapter 11, to which all other bankruptcy policies are subordinated, is the rehabilitation of the debtor.").

129 11 U.S.C. § 1112(a).

130 John B. Newman, *Conversion of a Bankruptcy From Chapter 11 to Chapter 7*, NEWMAN & SIMPSON, LLP, http://www.newmansimpson.com/conversion-of-a-bankruptcy-from-chapter-11-to-chapter-7.html (last visited Feb. 26, 2016).

131 *Id.*

132 *Id.*

133 UNITED STATES BANKR. COURT CENT. DIST. OF CAL., *supra* note 73.

134 *Id.*

The party requesting a chapter 11 dismissal must prove, by a preponderance of the evidence, that sufficient cause to dismiss the case exists.[135] Section 1112(b)(4) list sixteen permissible causes for dismissal;[136] courts may, however, consider other factors and dismiss a case at their discretion.[137]

Once cause is established and the court dismisses the case, the debtor is returned to its prebankruptcy status.[138] This type of dismissal has no bells and whistles. In other words, there are no additional proceedings or tasks for the debtor to follow or tasks for the debtor to complete related to its bankruptcy case.[139] Dismissal releases the debtor's estate from the court's control and allows creditors to resume attempts to collect any owed debt from the debtor.[140]

D. Bankruptcy Priority Scheme

Section 1129(a)(9) requires that a reorganization plan must satisfy § 507 to be confirmable.[141] Section 507, the bankruptcy priority scheme, dictates the order that claims are paid.[142] The bankruptcy priority scheme is analogous to a ladder where each rung represents a priority level.[143] Section 507 lists the mandatory asset distribution order based on class priorities.[144] Bankruptcy prioritizes repayment in full to claim holders based upon their position on the ladder; claim holders positioned higher up on the ladder will be paid in full before lower positioned claim holders.[145]

There are two major categories of claims: "secured" and "unsecured."[146] Secured claims give the claim holder the right to collect its debt from a specific

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[135] BLOOMBERG LAW: BANKRUPTCY TREATISE, *supra* note 107, pt. V, ch. 165.

[136] 11 U.S.C § 1112(b)(4) (2012).

[137] *In re* Charles St. Afr. Methodist Episcopal Church of Bos., 499 B.R. 66, 112 (Bankr. D. Mass. 2013).

[138] *Bankruptcy Dismissal*, THIS MATTER, http://thismatter.com/money/credit/bankruptcy/dismissal.htm (last visited Aug. 25, 2016).

[139] *See id.*

[140] *Id.*; *see also* Monica S. Blacker, Michael P. Cooley & Vickie Driver, *Structured Dismissals: The Least Worst Option*, DALLAS BAR ASSOCIATION: BANKRUPTCY & COMMERCIAL LAW SECTION (Nov. 5 2014), http://images.jw.com/com/publications/2024.pdf.

[141] *See* 11 U.S.C. § 1129(a)(9).

[142] *See id.* § 507.

[143] *See* 4 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 507.02 ("The preferred categories of claims are designated as having priority over other categories of claims and are entitled to payment in full before those not granted priority.").

[144] 11 U.S.C § 507.

[145] *See* 4 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 507.02.

[146] *See id.* ¶ 507.02[4][a].

piece of property.[147] If a debtor pledges a piece of its property as collateral when he or she incurs the debt, the claim is voluntary.[148] In contrast, claim holders can create involuntary claims by obtaining a lien on a debtor's property through a court order.[149]

Unsecured claims are debts not protected by a security interest in the debtor's property.[150] Examples of unsecured claims include medical bills, credit card bills, and cash advance loans. If a debtor does not pay its unsecured debts, the creditor does not have the authority to collect its debt from a specific piece of the debtor's property.

Secured claims are not included in the priority scheme ladder because the nature of a secured claim allows the claim holder to recover its debt directly from a specific piece of property.[151] Unsecured claims, however, are positioned in hierarchal order in accordance with the priority scheme.[152] The remaining unsecured claims are arranged in descending order of priority according to § 507.[153]

II. DISCUSSION

Part II begins with an analysis of the permissibility of structured dismissals under the Code, followed by a discussion of when structured dismissals are appropriate. This Comment concludes with an examination of the competing circuit court views on whether structured dismissals are allowed.

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147 *See id.* ("A lien is a charge against or interest in property to secure payment of a debt or performance of an obligation."). Common types of secured claims are mortgages and car loans. For example, if a debtor does not make the necessary payments on a car loan, the claim holder has the power to repossess the car and sell it to repay the debt.

148 *See id.*

149 *See id.* ¶ 507.02[3][a][i].

150 Unsecured claims are representative of the claims assessed under § 507. *See* 11 U.S.C. § 507(a) (2012); 4 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 507.02[4][a] ("The priorities granted by section 507 are priorities as against holders of unsecured claims only."). In drafting the priority scheme, Congress decided that domestic support obligations should hold the highest priority amongst unsecured claimants. *See* 11 U.S.C. § 507(a)(1)(A)–(C).

151 James H. Barnhill, *The Conundrum of an Inadequately Protected Secured Creditor*, 97 COM. L.J. 367, 369 (1992).

152 4 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 507.01.

153 *See id.*

A. The Code Allows Structured Dismissals

The Code does not explicitly provide bankruptcy courts with the power to grant structured dismissals.[154] As a result, structured dismissals are a by-product of courts' and parties' creativity. Parties seeking a structured dismissal invoke §§ 1112(b), 305(a)(1), 349(b), and 105(a) for statutory validation.[155] A plain reading of these sections provides ample support for structured dismissals under the Code. Furthermore, the legislative intent of § 349 confirms Congress's desire to provide courts with the discretion to implement creative judgments within the bounds of the Code.

The court's statutory authority to grant a dismissal, structured or not, is derived from § 1112(b).[156] To obtain a dismissal under § 1112(b), the debtor must demonstrate cause.[157] If a debtor successfully demonstrates cause, the court must dismiss the case, absent unusual circumstances identified by the court.[158] To justify cause for a structured dismissal, debtors can assert that there

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154 *In re* Jevic Holding Corp., 787 F.3d 173, 181 (3d Cir. 2015).

155 Blaire Cahn, In re Jevic Holding Corp. *Part I: Third Circuit Authorizes Structured Dismissals in Limited Circumstances*, WEIL BANKR. BLOG (June 30, 2015), https://business-finance-restructuring.weil.com/rules-and-procedures/in-re-jevic-holding-corp-part-i-third-circuit-authorizes-structured-dismissals-in-limited-circumstances/.

156 11 U.S.C. § 1112(b) (2012). Specifically, the language of this section reads:

> Except as provided in paragraph (2) and subsection (c), on request of a party in interest, and after notice and a hearing, the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.

Id.

157 *See* 7 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 1112.04[6].

158 *In re* Hinesley Family Ltd. P'ship, No. 1, 460 B.R. 547, 551 (Bankr. D. Mont. 2011). Specifically, the court noted:

> Although section 1112(b) does not define the phrase "unusual circumstances," it clearly contemplates conditions that are not common in most chapter 11 cases. Although each chapter 11 case is to some extent unique, and unusual circumstances may exist in any particular case regardless of its size or complexity, the import of section 1112(b) is that, if cause exists, the case should be converted or dismissed unless unusual facts or circumstances demonstrate that the purposes of chapter 11 would be better served by maintaining the case as a chapter 11 proceeding.

Id.; *accord* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 442, 119 Stat. 23. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 amended § 1112(b) to clarify that courts *must* grant a dismissal where cause is adequately demonstrated. *See* 11 U.S.C. § 1112(b) (2012) (emphasis added). Obtaining a dismissal is a bifurcated process. *See* 7 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 1112.04[7]. Step one requires debtors to demonstrate cause, and step two allows courts to is a "substantial or continuing loss to or diminution of the estate and the absence of a reasonable likelihood of rehabilitation" or an "inability to effectuate substantial consummation of a plan."[159] For example, the debtors and creditors in *In re Jevic* agreed that a structured dismissal was a more appropriate strategy than continuing bankruptcy proceedings.[160] A dismissal was more desirable to the parties because continuing bankruptcy proceedings would only drain the value of the debtor's limited remaining assets.[161] A dismissal is typically an appropriate strategy for debtors that have either liquidated a majority of their assets, do not have the necessary assets to proceed with a confirmation plan, or both.[162]

As discussed in Part I *supra*, structured dismissals can occur after a § 363 asset sale.[163] Under § 1112(b), courts typically grant a dismissal, structured or otherwise, after a § 363 sale because the debtor has liquidated most of its assets and cannot consummate a reorganization plan.[164]

Section 305(a)(1), while traditionally applied in involuntary bankruptcy cases, serves as another source of justification for structured dismissals.[165] Involuntary bankruptcy cases often arise when creditors involved in out-of-court restructuring negotiations force a debtor into bankruptcy to obtain more desirable treatment.[166] Section 305(a)(1) grants the court the authority to dismiss a case at any time if "the interests of creditors and the debtor would be better served by such dismissal or suspension."[167] Courts generally perceive § 305(a)(1) dismissals as an extraordinary remedy because they are final judgments not eligible for appellate review.[168]

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consider if granting the dismissal is in the best interest of creditors and the estate. Rollex Corp. v. Associated Materials, Inc. (*In re* Superior Siding & Window, Inc.), 14 F.3d 240, 242 (4th Cir. 1994).

159 11 U.S.C. § 1112(b); *accord* Camden Ordnance Mfg. Co. of Ark. v. U.S. Trustee (*In re* Camden Ordnance Mfg. Co. of Ark.), 245 B.R. 794, 799–800 (E.D. Pa. 2000) (holding that a dismissal is appropriate where the debtor's assets have been liquidated and there are no assets to reorganize); Ollerman & Douglas, *supra* note 4; Kane, *supra* note 58.

160 787 F.3d 173, 177 (3d Cir. 2015).

161 *Id.* at 176–77.

162 Pernick & Dean, *supra* note 2, at 57.

163 *See* Part I.B *supra*.

164 *See* 11 U.S.C. § 1112(b)(4)(M).

165 *See* 2 COLLIER ON BANKRUPTCY, *supra* note 89, ¶ 305.02.

166 11 U.S.C. §§ 303, 305(a)(1) (2012); Ollerman & Douglas, *supra* note 4.

167 11 U.S.C. § 305(a)(1).

168 *Id.* § 305(c):

> An order under subsection (a) of this section dismissing a case or suspending all proceedings in a case, or a decision not so to dismiss or suspend, is not reviewable by appeal or otherwise by the

In conjunction with §§ 1112(b) and 305(a)(1), proponents of structured dismissals rely on § 105(a) to extend the court's dismissal authority. Section 105(a) permits bankruptcy courts to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of" the Code.[169] "Thus, § 105(a) appears to grant bankruptcy courts authority to approve structured dismissals, because §§ 305 and 1112 of the Code provide means for dismissing cases."[170] Sections 105(a) does not, however, give the court the authority to issue orders inconsistent with the Code.[171] The Supreme Court in *Law v. Siegel* held that "a bankruptcy court may not contravene specific statutory provisions [of the Code]."[172] Section 105(a), therefore, allows courts to issue structured dismissal orders pursuant to §§ 1112(b) or 305(a)(1).

In re 155 Route 10 Associates illustrates the court's willingness to approve structured dismissals so long as they do not conflict with the Code. In *In re 155 Route 10*, the debtors sought a structured dismissal, citing § 105(a).[173] The trustee objected, and argued that because structured dismissals are not expressly permitted by the Code, they are prohibited.[174] The court disagreed, and granted the debtor's structured dismissal pursuant to § 105(a).[175]

While §§ 1112(b), 305(a)(1), and 105(a) govern courts' authority to issue dismissal orders, § 349 discusses the effect of a dismissal. Section 349(b) gives courts discretion to deviate from a standard dismissal "for cause";[176] however, the ways in which courts have interpreted "for cause" varies, as illustrated by the two decisions in *In re Sadler* and *In re Naartjie Custom Kids, Inc*.[177]

The Seventh Circuit in *In re Sadler* defined "cause" as "an acceptable reason," based on the facts and circumstances surrounding the case.[178] The Bankruptcy Court for the District of Utah in *In re Naartjie Custom Kids, Inc.*,

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court of appeals under section 158(d), 1291, or 1292 of title 28 or by the Supreme Court of the United States under section 1254 of title 28.

169 *Id.* § 105(a); *accord* Law v. Siegel, 134 S. Ct. 1188, 1194 (2014).

170 Kane, *supra* note 58.

171 Law v. Siegel, 134 S. Ct. at 1194; *In re* Fesco Plastics Corp., 996 F.2d 152, 156 (7th Cir. 1993) (holding § 105 allows courts to "enforce the provisions of the Code, not to add on to the Code as they see fit").

172 134 S. Ct. at 1194.

173 2012 WL 3570157.

174 *Id.*

175 *Id.*

176 11 U.S.C. § 349 (2012); *In re* Jevic Holding Corp., 787 F.3d 173, 181 (3d Cir. 2015); *In re* Naartjie Custom Kids, Inc., 534 B.R. 416, 422 (Bankr. D. Utah 2015).

177 *See, e.g.*, *In re* Sadler, 935 F.2d 918, 921 (7th Cir. 1991); *In re Naartjie*, 534 B.R. at 422.

178 935 F.2d at 921.

however, began its analysis of § 349 by looking to the plain language of the statute.[179] The court held that § 349(b) is unambiguous because it clearly reads, "unless the court, *for cause*, orders otherwise, a dismissal of the case . . ."[180] Under this interpretation of the statute, a bankruptcy court is not bound to ordering a dismissal that solely discharges the parties and closes the case.[181] The legislative intent of § 349 is also parallel with the literal writing of the statute.[182] The House Report enumerates the effects of dismissal and states, "the court is permitted to order a different result for cause."[183]

B. Under What Circumstances Is a Structured Dismissal Appropriate?

The Third Circuit in *In re Jevic* refrained from deciding the question of whether structured dismissals are allowed if a confirmable chapter 11 plan or chapter 7 conversion is possible.[184] The court did not need to answer the question because there was no prospect of the debtors proposing a confirmable chapter 11 plan with the limited remaining assets in the estate.[185] Opponents of structured dismissals argue that debtors will use this type of dismissal to circumvent plan confirmation or conversion processes.[186] To prevent this practice, the court serves as a safeguard against a debtor's ability to abuse structured dismissals.[187] Though dictum, the Third Circuit noted that "absent a

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179 534 B.R. at 422; Kane, *supra* note 58.

180 *Id.* at 422.

181 *See id.*; *see also In re* Jevic Holding Corp., 787 F.3d 173, 181 (3d Cir. 2015).

182 *In re Naartjie*, 534 B.R. at 422.

183 *Id.* at 423 (citing H.R. REP. NO. 95-595, at 338 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6294).

184 787 F.3d at 182.

185 *Id.* at 181–82.

186 *See* Lambert, Eitel & Tinker, *supra* note 18, at 20.

187 *See In re* Biolitec, Inc., 528 B.R. 261, 269 (Bankr. D.N.J. 2014) ("Courts serve as a safeguard against abuse by rejecting plans and dismissals that circumvent the protections allotted in the Bankruptcy Code."). *In re Biolitec* serves as a more recent example of courts serving as a safeguard. 528 B.R. 261. The court in *In re Biolitec* rejected a motion for an entry of an order dismissing the debtor's chapter 11 case pursuant to 11 U.S.C. §§ 105(a), 305(a), 349, and 1112(b) and a settlement agreement pursuant to Federal Rule of Bankruptcy Procedure 9019. *Id.* at 272. The debtor's settlement and structured dismissal proposed that the Debtor's chapter 11 case would be dismissed pursuant to § 1112(b); however, the Court would retain jurisdiction over the two adversary proceedings that were pending in the case, the claims reconciliation and objection process, and all matters related to the Liquidating Trust. *Id.* The settlement further stated:

> (1) With the exception of any potential interest of the estate in the Massachusetts Action, the Trustee will contribute all remaining estate assets to the Liquidating Trust. The estate will relinquish and assign any interest it has in the Massachusetts Action (or in any new action commenced by AngioDynamics against the Non-Debtor Affiliates to collect on its Judgment Claim) to AngioDynamics, although AngioDynamics will contribute a portion of any recovery obtained in these actions (up to $2,000,000) to the Liquidating Trust.

showing that a structured dismissal has been contrived to evade the procedural protections and safeguards of the plan confirmation or conversion processes, a bankruptcy court has discretion to order such a disposition."[188] Courts normally reject any resemblance of a plan, settlement, or dismissal order that aims to circumvent the standard chapter 11 proceedings because of the judicially–created concept of *sub rosa* plans.[189]

In a *sub rosa* plan, "a chapter 11 debtor constructs a broad settlement that amounts to a de facto plan of reorganization, which enables a debtor to restructure its debt while bypassing many of the Bankruptcy Code's fundamental creditor protections."[190] Section 1129 provides four significant and fundamental protections: (1) the right of impaired creditors to vote on a proposed plan;[191] (2) the requirement of good faith;[192] (3) best interest of

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(2) AngioDynamics will fund the formation of the Liquidating Trust and make additional contributions for the payment of allowed administrative expense claims. AngioDynamics will also contribute any interest it might have in the real property that is the subject of the CeramOptec Proceeding to the Liquidating Trust.

(3) Development Specialists, Inc. ("DSI") will be appointed as the liquidating trustee ("Liquidating Trustee"). AngioDynamics will serve as trust advisor to DSI and "provide direction or consent to all significant actions of the Liquidating Trust."

(4) The Liquidating Trustee will be substituted for the Trustee in the two pending adversary proceedings and any other action commenced by the Trustee. The Liquidating Trustee will also be substituted for the Trustee to oversee the claims reconciliation and objection process. AngioDynamics will be joined as a party to these actions and pursue them for the benefit of the Liquidating Trust.

(5) All claims of the Non-Debtor Affiliates will be subordinated to all allowed claims.

(6) The Trustee will be released from any liability in connection with the chapter 11 case.

Id. at 265–66 (numerals added). The court declined to grant the order because the debtor did not demonstrate that the proposed settlement and dismissal were in the best interests of the estate and its creditors. *Id.* at 270. "[I]n the absence of the consent of all parties, the Court is precluded from approving a settlement that alters parties' rights but ignores many of the Code's most important creditor protections." *Id.* at 272.

188 *In re Jevic*, 787 F.3d at 182.

189 *In re Biolitec*, 528 B.R. at 261 (denying the chapter 11 trustee's motion for a structured dismissal because it sought to "alter parties' rights without their consent and lacks many of the Code's most important safeguards").

190 Del. Tr. Co. v. Energy Future Intermediate Holdings, LLC (*In re* Energy Future Holding Corp.), 527 B.R. 157, 168 (Bankr. D. Del. 2015).

191 11 U.S.C. § 1129(a)(8), (10) (2012).

192 *Id.* § 1129(a)(3).

creditors;[193] and (4) the feasibility test.[194] These protections ensure that creditors are on notice by the proposed plan.[195]

In re Braniff Airways Inc. was the first case to conceptualize a *sub rosa* plan.[196] The debtor, Braniff Airways, Inc., filed for bankruptcy under chapter 11 in May 1982.[197] In turn, the FAA promulgated a special regulation to mitigate the effect of Braniff Airways's termination and bankruptcy.[198] The FAA allocated Braniff Airways's four hundred landing slots amongst various other airline carriers.[199] The Unsecured Creditors' Committee then questioned whether the FAA's allocation of the slots interfered with Braniff Airways's property.[200] The bankruptcy court and FAA responded by stipulating that the slots would be returned "should Braniff or an air carrier succeeding to the rights, duties and obligations of Braniff begin operations."[201]

In December 1982, Braniff Airways proposed a settlement agreement to the bankruptcy court.[202] Under the settlement agreement, the debtor would transfer cash, landing slots, and equipment to Pacific Southwest Airlines in exchange for profit participation in future Pacific Southwest Airlines operations.[203] The settlement also specified that future profits would be issued to only Braniff Airways's employees, shareholders, or a limited amount of unsecured creditors.[204] In a separate stipulation agreement designated for Braniff Airways's creditors, the debtor developed provisions that required secured creditors "to vote a portion of their deficiency claim in favor of any future reorganization plan approved by a majority of the unsecured creditors' committee."[205]After a month of oral arguments from interested parties, the

193 *Id.* § 1129(a)(7).

194 *See id.* § 1129(a)(11); Craig A Sloane, *The Sub Rosa Plan of Reorganization: Side-Stepping Creditors Protections in Chapter 11*, 16 BANKR. DEV. J. 37, 41–42 (1999). The *Emory Bankruptcy Developments Journal* published without the name of the sponsoring school until 2004.

195 Sloane, *supra* note 194, at 40.

196 700 F.2d 935 (5th Cir. 1983); *see also* Kimon Korres, Note, *Bankrupting Bankruptcy: Circumventing Chapter 11 Protections Through Manipulation of the Business Justification Standard in § 363 Asset Sales, and a Refined Standard to Safeguard Against Abuse*, 63 FLA. L. REV. 959, 964 n.50 (2013).

197 *In re Braniff Airways*, 700 F.2d at 938.

198 *Id.*

199 *Id.* Landing slots are specific timeframes given to airlines for departing and arriving aircrafts. *Id.* at 940.

200 *Id.* at 938.

201 *Id.*

202 *Id.*

203 *Id.* at 939.

204 *Id.*

205 *Id.* at 940.

bankruptcy court entered its order approving the Braniff Airways and Pacific Southwest Airlines settlement agreement.[206]

On review, the court held that the settlement agreement was null because it dictated future provisions of a reorganization plan.[207] For example, if devised according to the settlement agreement, any future reorganization plan would have to allocate the profits to a limited group of creditors.[208] According to the court, Braniff was not allowed to "short circuit" the chapter 11 confirmation process for a reorganization plan by predetermining profit allocations.[209] Additionally, the stipulation agreement disenfranchised creditors during the reorganization plan process.[210]

In re Braniff Airways serves as a pillar for the notion that courts should not confirm any plan, settlement, or dismissal order that effectively encroaches on the protections and proceedings in the Code. In bankruptcy proceedings, a structured dismissal is only appropriate when the debtor can adequately show that confirming a plan or converting a chapter 11 case would be overly burdensome.[211] Otherwise, the structured dismissal will highly resemble a *sub rosa* plan, thus constituting a tactic to circumvent the explicit exit strategies.[212]

Ultimately, chapter 11 confirmation plans are preferred in comparison to structured dismissals because they give debtors the opportunity to reorganize their business while simultaneously repaying creditors.[213] Chapter 11 to chapter 7 conversions, when in the best interest of creditors and the estate,[214] are also advantageous because the remaining estate assets are liquidated and distributed according to the Code's priority scheme.[215] As the Bankruptcy Court for the District of New Jersey noted, "[i]f a chapter 11 case could be dismissed solely to avoid additional expenses associated with liquidating the estate, parties

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206 *Id.* at 938.
207 *Id.* at 940.
208 *Id.* at 939.
209 *Id.* at 940.
210 *Id.*
211 Brent Weisenberg, *Expediting Chapter 11 Liquidating Debtor's Distribution to Creditors*, AM. BANKR. INST. J., Apr. 2012, at 36, 106.
212 11 U.S.C. § 1129(a) (2012) (listing the requirements to confirm a plan); *id.* § 1112 (a)–(b) (listing the requirements to either convert a chapter 11 case to chapter 7 case or dismiss a case).
213 FED. JUD. CTR., *supra* note 109, http://www.fjc.gov/federal/courts.nsf/autoframe?openagent&nav=menu1&page=/federal/courts.nsf/page/201.
214 Ollerman & Douglas, *supra* note 4.
215 Lambert, Eitel & Tinker, *supra* note 18, at 20.

would rarely, if ever, convert to chapter 7 and the conversion option in section 1112(b) would essentially be rendered superfluous."[216]

In consideration of the Third Circuit's dictum in *In re Jevic* and the § 1129 requirements for plan confirmation, a structured dismissal, specifically one in the form of a settlement agreement, is not appropriate where a confirmable chapter 11 plan or chapter 7 conversion is possible.

C. The Code's Priority Scheme Applies to Structured Dismissal Settlements

Caselaw divides settlements into two categories.[217] The first type of settlement is one that is proposed as a part of a chapter 11 reorganization plan.[218] Courts have limited discretion in approving these types of settlements because of the fair and equitable standard.[219] Thus, any settlement proposed as a part of a reorganization plan must arrange the distribution of claim payments in accordance with the bankruptcy priority scheme.[220]

The second type of settlement is an agreement parties reach outside of a reorganization plan.[221] These types of settlements have received different methods of treatment from the circuit courts.[222] The circuits are split on whether a court must apply the fair and equitable standard when considering a proposed nonconsensual settlement that parties formed outside of a reorganization plan.[223]

The following sections will review the Fifth, Second, and Third Circuit approaches to the fair and equitable standard. This Comment will then argue that the Fifth Circuit's rule is favorable, and that the fair and equitable standard should also apply to settlements outside of the reorganization plan; therefore, deviation from the Code's priority scheme would be impermissible.

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216 *In re* Biolitec, Inc., 528 B.R. 261, 269 (Bankr. D.N.J. 2014).

217 *Compare* Protective Comm. for Indep. Stockholders of TMT Trailer Ferry v. Anderson, 390 U.S. 414, 424 (1968), *with In re* AWECO, Inc., 725 F.2d 293, 297 (5th Cir. 1984).

218 *See In re AWECO*, 725 F.2d at 298.

219 *Id.*; *In re* Jackson Brewing Co., 624 F.2d 599, 602 (5th Cir. 1980).

220 *In re AWECO*, 725 F.2d at 298; *see* 11 U.S.C. 1129(a)(9) (2012).

221 *See In re AWECO*, 725 F.2d at 298.

222 *Compare id.*, *and In re* Iridium Operating LLC, 478 F.3d 452, 466–67 (2d Cir. 2007), *with In re* Jevic Holding Corp., 787 F.3d 173, 186 (3d Cir. 2015).

223 *Compare In re AWECO*, 725 F.2d at 298, *and In re Iridium*, 478 F.3d at 466–67, *with In re Jevic*, 787 F.3d at 186.

1. *Fifth Circuit*

The Fifth Circuit in *In re AWECO, Inc.* was the first circuit to decide the applicability of the Code's priority scheme to settlements outside of a reorganization plan.[224] When AWECO, Inc., filed for bankruptcy in early 1981, it had four major creditors.[225] Of these creditors, United American Car Co. held an unsecured claim for approximately $27 million that was the result of a breach of contract lawsuit.[226] Litigation between AWECO and United American lasted for almost two years while AWECO's chapter 11 bankruptcy proceeding was pending.[227] Ultimately, AWECO and United American agreed to settle the lawsuit.[228] The terms of the settlement provided that AWECO would transfer $5.3 million in cash and property to United American.[229] The settlement did not include any repayment of AWECO's outstanding debts to its other three creditors.[230] Notably, one of the three excluded creditors held a secured claim in the property that AWECO agreed to transfer to United American under the settlement agreement.[231]

After AWECO notified the bankruptcy court of its intention to settle, its creditors objected.[232] The creditors argued that the settlement between AWECO and United American was unfair.[233] The court approved the settlement over the creditors' objection, and the creditors appealed.[234]

On appeal, the Fifth Circuit considered whether the bankruptcy court must "apply the fair and equitable standard in considering a priority creditor's objections to a settlement."[235] The court declined to adopt United American's argument that the fair and equitable standard does not extend to any outside

224 725 F.2d at 298; Peter Doggett Jr., *What Exactly Does the Term "Fair and Equitable" Mean?*, 1 ST. JOHN'S BANKR. RESEARCH LIBR. 1 (2009), http://www.stjohns.edu/academics/graduate/law/journals/abi/sjbrl/volume/v1/doggett.stj.

225 *In re AWECO*, 725 F.2d at 295. In addition to United American's claim, the Department of Energy had a $45 million claim; the IRS had two priority claims totaling over $7 million; and Sutton Investments, Inc., had a claim for approximately $8 million. *Id.*

226 *Id.*

227 *Id.*

228 *Id.*

229 *Id.* at 296.

230 *See id.*

231 *See id.*

232 *Id.* at 295.

233 *Id.* at 296.

234 *Id.* at 297.

235 *Id.* at 298. This issue is narrower than simply deciding whether the fair and equitable standard applies to any outside settlement. *See id.*; *see also* Doggett Jr., *supra* note 224.

settlements.[236] Instead, the court analyzed the policy implications of the fair and equitable standard:

> As soon as a debtor files a petition for relief, fair and equitable settlement of creditors' claims becomes a goal of the proceedings. The goal does not suddenly appear during the process of approving a plan of compromise. Moreover, if the standard had *no* application before confirmation of a reorganization plan, then bankruptcy courts would have the discretion to favor junior classes of creditors so long as the approval of the settlement came before the plan[237]

The Fifth Circuit reasoned that the fair and equitable standard must apply because it prevents bankruptcy courts from favoring one group of creditors solely because a settlement is created outside the reorganization plan.[238] The court explained that the decision to apply the fair and equitable standard was not to "radically restrict" bankruptcy courts from approving settlements, but rather to ensure that "settlements do not impose an unfair detriment on creditors."[239]

2. *Second Circuit*

Over twenty years after the Fifth Circuit's decision in *In re AWECO*, the Second Circuit adopted its own application of the priority rules to outside settlement agreements in *In re Iridium Operating LLC*.[240] Iridium Operating LLC operated as a subsidiary of Motorola, Inc., until 1998 when it became an independent company.[241] Iridium's independence was short-lived; it filed for chapter 11 in 1999.[242] Months before filing bankruptcy, Iridium borrowed $1.55 billion from JPMorgan Chase Bank.[243]

JPMorgan asserted claims over the remaining Iridium assets, and the Official Committee of Unsecured Creditors objected to the claims.[244] The Committee also sought recourse against Motorola, alleging breach of contract,

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236 *In re AWECO*, 725 F.2d at 298.

237 *Id.*

238 *Id.* (determining that if the standard had *no* application before confirmation of a reorganization plan, then bankruptcy courts would have the discretion to favor junior classes of creditors so long as the approval of the settlement came before the plan was proposed).

239 *Id.* at 299.

240 478 F.3d 452 (2d Cir. 2007); Doggett Jr., *supra* note 224.

241 *In re Iridium*, 478 F.3d at 456.

242 *Id.* at 457.

243 *Id.*

244 *Id.* at 456.

breach of fiduciary duty, and avoidance of fraudulent conveyances.[245] Because the Committee did not have sufficient funds to both contest the claims and pursue legal action against JPMorgan *and* Motorola, however, the Committee and JPMorgan reached a settlement agreement.[246] In the agreement, the Committee and JPMorgan proposed to divide Iridium's remaining assets amongst themselves.[247] Against Motorola's objection that the settlement would distribute estate property to lower priority creditors before more senior ones, the bankruptcy court approved the settlement.[248] The decision was affirmed by the district court, and Motorola appealed.[249]

Motorola contended that the bankruptcy court improperly approved the settlement because it did not meet the fair and equitable standard—junior creditors were paid before senior creditors.[250] Motorola claimed "a settlement can never be fair and equitable if junior creditors' claims are satisfied before those of more senior claims."[251]

The court agreed that the fair and equitable standard is a requirement for settlements proposed within a reorganization plan, relying on the Supreme Court's decision in *TMT Trailer Ferry v. Anderson*.[252] There, the Supreme Court held that "the requirements . . . that plans of reorganization be both 'fair and equitable[]' apply to compromises just as to other aspects of reorganizations."[253] The Supreme Court further distinguished that the established requirement applied explicitly to settlements that are a part of a reorganization plan.[254]

Applying the Supreme Court's reasoning, the Second Circuit concluded that the settlement between JPMorgan and the Committee was not bound by the fair and equitable standard because it was not proposed as a part of Iridium's chapter 11 reorganization plan.[255] The Second Circuit noted: "[W]hether a particular settlement's distribution scheme complies with the Code's priority scheme must be the most important factor for the bankruptcy

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245 *Id.* at 458.
246 *Id.* at 458–59.
247 *Id.* at 459.
248 *Id.*
249 *Id.*
250 *Id.* at 462.
251 *Id.*
252 *Id.* at 461 (citing 390 U.S. 414, 424 (1968)).
253 *TMT Trailer Ferry*, 390 U.S. at 424.
254 *Id.*; *see also In re Iridium*, 478 F.3d at 461.
255 *In re Iridium*, 478 F.3d at 463.

court to consider when determining whether a settlement [within a reorganization plan] is 'fair and equitable . . . .'"[256] The court also noted that if a court approves a settlement that deviates from the priority scheme, it must articulate its reasoning in the opinion.[257]

The Second Circuit in *In re Iridium* applied the Supreme Court's reasoning in *TMT Trailer Ferry* too narrowly.[258] Although *TMT Trailer Ferry* involved discussed a settlement agreement that was connected to a reorganization plan, the Court's ruling covers settlements devised during a bankruptcy proceeding.[259] The Supreme Court held that "requirements . . . that plans of reorganization be both 'fair and equitable[]' apply to compromises just as to other aspects of reorganizations."[260] Other aspects of the reorganizations should encompass structured dismissals.

3. *Third Circuit*

In *In re Jevic*, the Third Circuit elected to adopt the more flexible rule from *In re Iridium*.[261] The court highlighted that deviations from the § 507 priority scheme are only permissible if the court can articulate "specific and credible grounds to justify the deviation."[262]

This flexible rule presents several issues, however. Primarily, the doors of discretion are left open for courts to create varying interpretations of "specific and credible grounds." Both the Second and Third Circuits were wary of establishing a less rigid adaptation of the Fifth Circuit's rule in *In re AWECO*, and for good reason.[263] In his dissenting opinion in *In re Jevic*, Judge Scirica departed from the majority opinion on the grounds that the facts from this case did not present a credible justification to deviate from the priority scheme.[264]

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256 *Id.* at 465.

257 *Id.*

258 *See* Brief of *Amici Curiae* States of Illinois, et al. at 9, Czyzewski v. Jevic Holding Corp., 136 S. Ct. 2541 (2016) (No. 15-649), 2015 WL 9315587, at *9.

259 390 U.S. 414, 424 (1968); Brief of *Amici Curiae* States of Illinois, et al., *supra* note 258, at 9.

260 *TMT Trailer Ferry*, 390 U.S. at 424.

261 *In re* Jevic Holding Corp., 787 F.3d 173, 184 (3d Cir. 2015) ("We agree with the Second Circuit's approach in *Iridium* . . . .").

262 *Id.*

263 *Id.* ("We admit that it is a close call . . . ."); *In re Iridium*, 478 F.3d at 464 ("Rejection of a *per se* rule has an unfortunate side effect, however: a heightened risk that the parties to a settlement may engage in improper collusion.").

264 *In re Jevic*, 787 F.3d at 186 (Scirica, J., dissenting).

Judge Scirica went on to suggest a way that the court could have effectively unwound the case in accordance with the priority scheme:

> I recognize that if the settlement were unwound, this case would likely be converted to a Chapter 7 liquidation in which the secured creditors would be the only creditors to recover. Accordingly, I would not unwind the settlement entirely. Instead, I would permit the secured creditors to retain the releases for which they bargained and would not disturb any of the proceeds received by the administrative creditors either. But I would also require the bankruptcy court to determine the WARN Plaintiffs' damages under the New Jersey WARN Act, as well as the proportion of those damages that qualifies for the wage priority. I would then have the court order any proceeds that were distributed to creditors with a priority lower than that of the WARN Plaintiffs disgorged, and apply those proceeds to the WARN Plaintiffs' wage priority claim. To the extent that funds are left over, I would have the court redistribute them to the remaining creditors in accordance with the Code's priority scheme.[265]

Judge Scirica's ability to construct a viable exit strategy, despite the majority's contention that there was no conceivable alternative to deviating from the priority scheme, reveals the dangers of an arbitrary "specific and credible grounds" standard.[266] With the standard from *In re Iridium* permitting the court's discretion, creditors and debtors cannot evaluate whether their case amounts to the level of credibility needed to deviate from the priority scheme.

Beyond the grave confusion and arbitrariness created by the Second and Third Circuit's flexible standard, the Code simply does not permit selective deviations from the priority scheme in bankruptcy proceedings. Thus, the priority scheme applies to reorganization plans as well as settlements.[267] "Section 507 priorities reflect important and long-standing congressional judgments about what is fair and equitable in relation to the distribution of bankruptcy estate property."[268] When the Code was written, Congress did not intend, in any way, for the priorities to apply exclusively to select aspects of a bankruptcy proceeding.[269] The purpose of priorities is to ensure that the

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265 *Id.* at 189.

266 *Id.* at 186.

267 Brief of *Amici Curiae* National Employment Law Project & National Consumers League at 10, Czyzewski v. Jevic Holding Corp., 136 S. Ct. 2541 (2016) (No.15-649), 2015 WL 9252251, at *10.

268 *Id.*

269 Brief of the United States as *Amicus Curiae* Supporting Reversal at 1–2, *In re* Jevic Holding Corp., 787 F.3d 173 (No. 14-1465), 2014 WL 4184509, at *1–2:

creditors Congress deemed most vulnerable and important receive their portion of the estate before unsecured creditors.[270] Accordingly, § 103 of the Code extends the priority scheme to chapters 5, 7, 11, 12, and 13.[271]

Since Congress designed the priority scheme to apply to all bankruptcy chapters, it follows that Congress intended the priority scheme to apply to all estate distributions within a bankruptcy proceeding. The court in *In re AWECO* noted: "[A]s soon as a debtor files a petition for relief, fair and equitable settlement of creditors' claims becomes a goal of the proceedings."[272] In other words, the fair and equitable standard does not suddenly appear during plan proposals; instead, distributing the assets in accordance with the priority scheme is a goal that permeates the *entire* bankruptcy proceeding.[273]

Neither the Code nor legislative history supports applying § 507 exclusively to reorganization plans.[274] The Third Circuit's willingness to permit class-skipping also creates a dangerous practice of manipulation and evasion of the Code. The ex-employees in *In re Jevic* held a perfected WARN Act claim, which under § 507(a)(4) entitled them to payment before other unsecured creditors.[275] Almost seven years later, the ex-employees have yet to receive the unpaid wages and benefits they are entitled to under federal labor laws.[276] The practice of select creditors constructing a settlement agreement amongst

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> The bankruptcy court's decision sanctions a mechanism that permits parties to distribute estate assets (here proceeds from the compromise of estate causes of action) in violation of the priorities established by the Bankruptcy Code for the payment of creditor claims. That decision undermines a fundamental principle of bankruptcy that the debtor's assets will be distributed fairly and threatens to destroy confidence in the bankruptcy system. Moreover, there appears to be no reason why the . . . rationale could not be extended to permit parties to violate other Code requirements in the context of a settlement, so long as the bankruptcy court found that the settlement benefitted some of the creditors.

270 Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 10 ("The Third Circuit's decision undermines fundamental bankruptcy principles and invites manipulation of the bankruptcy process to eviscerate the priority rights Congress expressly conferred on those most in need of protection in the bankruptcy process.").

271 11 U.S.C. § 103 (2012); Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 10.

272 725 F.2d 293, 298 (5th Cir. 1984); Brief of *Amici Curiae* States of Illinois, et al., *supra* note 258, at 9.

273 *See* Brief of Amici Curiae States of Illinois, et al., *supra* note 258, at 11.

274 *See id.*

275 *In re* Jevic Holding Corp., 787 F.3d 173, 177 (3d Cir. 2015); *see* 11 U.S.C. § 507(a)(4)(A); *see also* Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 10.

276 Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 7.

themselves that intentionally excludes other priority creditors amounts to an unlawful evasion of the Code.[277] If courts permit this type of behavior, creditors can essentially bypass the priority scheme whenever the Code does not afford them a favorable outcome.[278]

The Third Circuit described its decision to grant a settlement that deviated from the Code's priorities as "the least bad alternative."[279] In summation, the Third Circuit reasoned that the bankruptcy court should have adopted the corporate respondents' settlement proposal over the employees' objections because the corporate respondents would be better off and the ex-employees would be no worse off.[280] A bankruptcy court, however, does not have the discretion to grant this type of order.[281] "Claims of necessity or hardship cannot justify approving a distribution of estate assets outside a plan in a manner that violates the priority scheme."[282]

In adopting the flexible standard from *In re Iridium*, the Second and Third Circuits determined that bankruptcy courts can choose when and how to apply the Code's priority rules. Their understanding is incorrect. In a recently published student Note, *Up the Chute, Down the Ladder: Shifting Priorities Through Structured Dismissals in Bankruptcy*, the author proposed a multi-faceted analysis for courts to use when assessing whether to approve a noncompliant structured dismissal.[283] Some of the considerations included: "[W]hether and when stakeholders whose rights would be affected by the structured dismissal were informed of the negotiations leading up to the

277 *Id.* at 7 ("This represents an additional opportunity for wage theft—employers failing to pay employees what they have earned."); Reply Brief for Petitioners at 6, Czyzewski v. Jevic Holding Corp., 136 S. Ct. 2541 (2016) (No. 15-649), 2016 WL 424790, at *6 ("Allowing debtors and select creditors to collude on a private deal to dispose of estate property outside this framework, in violation of the priority scheme, undermines those provisions and is incompatible with the Code's structure.").

278 Reply Brief for Petitioners, *supra* note 277, at 2; Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 6 ("Moreover, the Third Circuit's liberal approach to approving settlements in structured dismissals, creating an opportunity for the settling corporate parties to bypass priority creditors, is likely to encourage more, and more problematic, motions for approval of structured dismissals.").

279 *In re* Jevic Holding Corp., 787 F.3d 173, 185 (3d Cir. 2015).

280 Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 14.

281 *See* United States v. Reorganized CF & I Fabricators of Utah, Inc., 518 U.S. 213, 229 (1996); United States v. Noland, 517 U.S. 535, 543 (1996); Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 276, at 9.

282 Reply Brief for Petitioners, *supra* note 277, at 8.

283 Bethany Kate Smith, Note, *Up the Chute, Down the Ladder: Shifting Priorities Through Structured Dismissals in Bankruptcy*, 84 FORDHAM L. REV. 2989, 3012 (2016).

proposed agreement; [and] whether such stakeholders received sufficient opportunity to participate in the negotiations."[284]

The author's suggested considerations are strikingly similar to the flexible standard from *In re Iridium*. Both the court in *In re Iridium* and the author prioritized the absolute priority rule in deciding whether to approve a structured dismissal or settlement that deviates from § 507. What these interpretations fail to recognize is that the application of § 507 is not flexible or at the discretion of the court. Congress has already provided specific mechanisms for distributing proceeds of an estate outside of the priority scheme.[285] Other than the exceptions provided for in §§ 364(c), 510, 724(b), 726(a)–(b), and 901, the only permissible deviation from § 507 is with the consent of all creditors.[286] Under § 1129, creditors are explicitly given the authority to waive their priority rights.[287] The *In re Iridium* standard and proposed considerations in *Up the Chute, Down the Ladder* are therefore unnecessary. As the court in *In re Roth American, Inc*. noted, where "Congress intended to alter the priority scheme established in section 507, it has done so explicitly."[288] The Third Circuit's decision to approve the structured dismissal in *In re Jevic* was therefore in error. None of the § 507 exceptions were present in the case, and the settlement was not consensual amongst all the creditors, namely the ex-employees.

The Fifth Circuit's decision falls on the correct side of the argument. Section 1129(b) is applicable when the parties do not agree on a proposed reorganization plan, but all the other requirements, enumerated in § 1129(a),

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[284] *Id.* ("A bankruptcy court, in deciding whether a structured dismissal that violates section 507 is 'fair and equitable' under Rule 9019, should pay particular attention to: whether and when stakeholders whose rights would be affected by the structured dismissal were informed of the negotiations leading up to the proposed agreement; whether such stakeholders received sufficient opportunity to participate in the negotiations; whether such stakeholders received adequate opportunity to be heard on their objections; the nature of the claims or interests that would be subordinated by the proposed agreement; the nature of the claims or interests that would be protected or advanced through such subordination; whether there exists a viable alternative to the proposed agreement; and the relative difference in payout that would result to each class of creditors through the alternative course of conduct.").

[285] Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 9 ("Where Congress found cause for an exception, Congress specified it expressly.").

[286] 11 U.S.C. §§ 364(c); 510; 724(b); 726(a)–(b); 901 (2012); Brief of *Amici Curiae* National Employment Law Project & National Consumers League, *supra* note 267, at 15; *see* 11 U.S.C. § 1129(a)(9) ("[e]xcept to the extent that the holder of a particular claim has agreed to a different treatment of such claim . . . .").

[287] 11 U.S.C. § 1129(a)(9).

[288] 975 F.2d 949, 956 (3d Cir. 1992).

are met.[289] The court can confirm a nonconsensual plan so long as the plan is "fair and equitable."[290] The fair and equitable requirement is critical because it protects nonconsenting parties. For example, without the protections of § 1129(b) nonconsenting parties would be strongly coerced into plans that pay lower priority creditors before paying more senior creditors in full. The fair and equitable requirement must apply to all aspects of a bankruptcy case, including structured dismissals, because without it, the § 507 priority scheme would not be implicated.[291]

As previously discussed, § 507 enumerates the mandatory order in which assets in a bankruptcy estate are distributed.[292] A court's discretionary authority to deviate from the priority scheme is directly in conflict with Congress's promulgation of § 507. Nowhere in § 507 does the Code provide that the priority scheme applies exclusively to one particular type of asset distribution in a bankruptcy case. To afford claimants the same § 507 protections that they have in reorganization plans, the absolute priority rule's fair and equitable requirement must therefore apply to settlements in the context of structured dismissals.

CONCLUSION

Through statutory support, this Comment has shown that structured dismissals are permissible so long as they do not deviate from the Code's priority rules. Under the Code, judges may grant structured dismissals where both confirming a chapter 11 plan and converting to chapter 7 are implausible. Structured dismissals are permissible so long as they abide by the provisions within the Code. Specifically, a settlement devised in the context of a structured dismissal must conform to § 507 of the Code, unless the exceptions provided in §§ 364(c), 510, 724(b), 726(a)–(b), 901, and 1129(b) are met. On review, the United States Supreme Court should affirm the permissibility of structured dismissals, but reject the notion that structured dismissals may deviate from the priority scheme.

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289 11 U.S.C § 1129(b).

290 *Id.*

291 *Id.* § 1129(b)(1).

292 *Id.* § 507.

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