Docket #0294 Date Filed: 07/23/2018

UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re ENDURO RESOURCE PARTNERS LLC, *et al*., Debtors.	Chapter 11 Case No.: 18-11174(KG) (Jointly Administered) **Hearing Date: July 30, 2018 at 10:00 a.m.** **Objections Due: July 23, 2018 at 5:00 p.m.** **Re Docket No. 71, 182, 193, 199, 202, 206, 251**

THE UNITED STATES TRUSTEE'S OBJECTION TO CONFIRMATION OF THE JOINT PLAN OF LIQUIDATION OF ENDURO RESOURCE PARTNERS LLC AND ITS DEBTOR AFFILIATES UNDER CHAPTER 11 OF THE BANKRUPTCY CODE (D.I. 71, 182, 193, 199, 202, 206, 251)

Andrew R. Vara, the Acting United States Trustee for Region 3 ("U.S. Trustee"), objects ("Objection") To Confirmation Of The Joint Plan Of Liquidation Of Enduro Resource Partners LLC And Its Debtor Affiliates Under Chapter 11 Of The Bankruptcy Code, and in support of that Objection states as follows:

PRELIMINARY STATEMENT

1. The Debtors seek confirmation of the Joint Plan of Liquidation of Enduro Resource Partners LLC and its Debtor Affiliates under Chapter 11 of the Bankruptcy Code (the "Plan"). The U.S. Trustee objects to confirmation because (a) the Plan contains impermissible exculpation and releases; (b) the Debtors must establish that the Plan is feasible; and (c) the Plan impermissibly seeks to provide the equivalent of a discharge to a liquidating corporate debtor.[1]

[1] The U.S. Trustee has raised additional confirmation issues with the Debtors. The parties have reached agreement in principle on those issues. The U.S. Trustee reserves these objections pending review of the revised Plan.

JURISDICTION

2. Under (i) 28 U.S.C. § 1334, (ii) applicable order(s) of the United States District Court for the District of Delaware issued pursuant to 28 U.S.C. § 157(a), and (iii) 28 U.S.C. § 157(b)(2), this Court has jurisdiction to hear and determine the Motion and this Objection.

3. The U.S. Trustee is charged with overseeing the administration of Chapter 11 cases filed in this judicial district, pursuant to 28 U.S.C. § 586. This duty is part of the U.S. Trustee's overarching responsibility to enforce the bankruptcy laws as written by Congress and interpreted by the courts to guard against abuse and over-reaching to assure fairness in the process and adherence to the provisions of the Bankruptcy Code. *See In re United Artists Theatre Co.*, 315 F.3d 217, 225 (3d Cir. 2003) ("U.S. Trustees are officers of the Department of Justice who protect the public interest by aiding bankruptcy judges in monitoring certain aspects of bankruptcy proceedings."); *United States Trustee v. Columbia Gas Sys., Inc.* (*In re Columbia Gas Sys., Inc.*), 33 F.3d 294, 298 (3d Cir. 1994) ("It is precisely because the statute gives the U.S. Trustee duties to protect the public interest . . . that the Trustee has standing to attempt to prevent circumvention of that responsibility."); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 499 (6th Cir. 1990) ("As Congress has stated, the U.S. trustees are responsible for 'protecting the public interest and ensuring that the bankruptcy cases are conducted according to [the] law").

4. Pursuant to 28 U.S.C. § 586(a)(3)(B), the U. S. Trustee has the duty to monitor plans and disclosure statements filed in Chapter 11 cases and to comment on such plans and disclosure statements.

5. Under section 307 of title 11 of the United States Code (the "Bankruptcy Code" or "Code"), the United States Trustee has standing to be heard on the Motion and the issues raised in this Objection.

BACKGROUND

6. On May 15, 2018, the Debtors filed voluntary petitions commencing these Chapter 11 Cases.

7. The Debtors remain in possession of their assets and continue to manage their business as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

8. No committee of creditors has been appointed in this case.

9. At the sale hearing held on July 20, 2018, the Court indicated that it would approve orders authorizing the Debtors to sell substantially all of their assets. The Debtors have filed proposed orders approving such sales under certification of counsel. D.I. 289.

ARGUMENT

The Plan's Exculpation Provisions Are Too Broad

10. The Plan seeks to provide exculpation to all Exculpated Parties, defined as:

> each of the Debtors and their Affiliates, the First Lien Agent and its affiliates, and the Consenting First Lien Lenders and their Affiliates, and with respect to each of the foregoing, such Entity's current or former subsidiaries and Affiliates, and its and their managed accounts or funds, officers, directors, managers, managing members, principals, partners, members, employees, agents, financial advisors, attorneys, accountants, investment bankers, consultants, representatives and other Professionals, in their capacity as such.

Plan at Article I.A50.

11. The Plan seeks to exculpate the Exculpated Parties from Exculpated Claims, defined as:

> any Claim related to any act or omission in connection with, relating to or arising out of the Debtors' in- or out-of-court restructuring efforts, the Debtors' Chapter 11 Cases, formulation, preparation, dissemination, negotiation or filing of the Disclosure Statement or the Plan or any contract, instrument, release or other agreement or document created or entered into in connection with the Disclosure Statement or the Plan, the filing of the Chapter 11 Cases, the pursuit of Confirmation, the pursuit of Consummation, the administration and implementation of the Plan, including the distribution of property under the Plan or any other agreement; provided, however, that Exculpated Claims shall not include any act or omission that is determined in a Final Order to have constituted willful misconduct, gross negligence, or fraud.

Plan at Article I.A.49.

12. The exculpation provided by the plan is:

> To the fullest extent permitted by applicable law, except as otherwise specifically provided in the Plan, no Exculpated Party shall have or incur, and each Exculpated Party is hereby released and exculpated from any Exculpated Claim, obligation, Cause of Action or liability for any Exculpated Claim, except for those that are determined in a final order to have constituted actual fraud, gross negligence, willful misconduct, or criminal conduct.

Plan at Article X.D.

13. These provisions provide for impermissibly broad exculpation, both as to *who* is entitled to exculpation, and what *claims* are the subject of exculpation.

14. As stated by the Court in *In re Washington Mutual, Inc.*, 442 B.R. 314 (Bankr. D. Del. 2011)(Walrath, J.), an "exculpation clause must be limited to the **fiduciaries** who have served during the chapter 11 proceeding: estate professionals, the Committees and their members, and the Debtors' directors and officers." *Id.* at 350-51 (emphasis added). The Court in *In re Tribune Company*, 464 B.R. 126 (Bankr. D. Del. 2011)(Carey, J.), stated agreement with the holding in *Washington Mutual* relating to exculpated parties, and held that

the exculpation clause in *Tribune*, "must exclude non-fiduciaries." *Id.* at 189, quoting *Washington Mutual*, 422 B.R. at 350 -51. *Accord, Indianapolis Downs*, 486 B.R. 286 (Bankr. D. Del. 2013).

15. *In In re PTC Holdings LLC*, 55 Bankr. Ct. Dec 206, 2011 Bankr. LEXIS 4436, *38 (Bankr. D. Del. Nov. 10, 2011)(Shannon, J.), this Court sustained the U.S. Trustee's objection to the exculpation clause, stating that such clause "must be reeled in to include only those parties who have acted as estate fiduciaries and their professionals." *Id.* at * 38. In reaching this conclusion, the *PTC* Court reviewed the *Washington Mutual* decision, as well as the decision of the Third Circuit Court of Appeals in *In re PWS Holding Corp*., 228 F.3d 224, 246 (3d Cir. 2000), on which *Washington Mutual* relied. The issue in *PWS* was whether an official committee of unsecured creditors could receive exculpation. As described by the Court in *PTC Holdings*:

> In reaching its conclusion, the *PWS* court examined § 1103(c) and noted that the section "has been interpreted to imply both a fiduciary duty to committee constituents and a limited grant of immunity to committee members." "This immunity," the court found, "covers committee members for actions within the scope of their duties." The *PWS* court's reasoning thus implies that a party's exculpation is based upon its role or status as a fiduciary. That is why, as the *Washington Mutual* court pointed out, courts have permitted exculpation clauses insofar as they "merely state[] the standard to which ... estate fiduciaries [a]re held in a chapter 11 case." That fiduciary standard, however, applies only to estate fiduciaries, "no one else."

PTC Holdings at * 37-38 (citations omitted).

16. Even with respect to the estate fiduciaries that can be covered, the exculpation clause in the Plan is impermissibly broad, because it is not limited to actions taking place during the bankruptcy case, but also includes pre-petition activity. *See Washington*

Mutual, 442 B.R. at 350 (exculpations cover "actions in the bankruptcy case"), *citing PWS*, 228 F.3d at 246.

17. Unless the Exculpation provision in the Plan is amended so that it benefits only fiduciaries of the Debtors' estates and is limited to acts and omissions during the course of the bankruptcy cases, provision, the Plan should not be confirmed.

The Debtors Releases are Impermissibly Broad Under Applicable Law

18. The Plan provides for the Debtors and their estates to provide broad releases (the "Debtor Releases"). The Debtor Releases, set forth in Article X.B. of the Plan, provides:

> To the extent permitted by applicable law and approved by the Bankruptcy Court, pursuant to section 1123(b) of the Bankruptcy Code, and except as otherwise specifically provided in the Plan, for good and valuable consideration, on and after the Effective Date, the Released Parties shall be deemed released and discharged by the Debtors and the Estates from any and all Claims, obligations, rights, suits, damages, Causes of Action, remedies, and liabilities whatsoever, including any derivative Claims, asserted on behalf of the Debtors, whether known or unknown, foreseen or unforeseen, existing or hereinafter arising, in law, equity, or otherwise, that the Debtors, the Estates, or their Affiliates would have been legally entitled to assert in their own right (whether individually or collectively) or on behalf of the Holder of any Claim or Interest or other Entity, based on or relating to any act, omission, transaction, event, or other occurrence taking place on or prior to the Effective Date; provided, however, that the foregoing "Debtor Releases" shall not operate to waive or release any Causes of Action of any Debtor: (1) against a Released Party arising from any contractual obligations owed to the Debtors that are pursuant to an Executory Contract that is not otherwise rejected by the Debtors pursuant to section 365 of the Bankruptcy Code before, after, or as of the Effective Date; (2) expressly set forth in and preserved by the Plan or related documents; or (3) arising from claims for fraud, gross negligence, willful misconduct, or criminal conduct. Notwithstanding anything to the contrary in the foregoing, the "Debtor Releases" set forth above do not release any post-Effective Date obligations of any party under the Plan or any document, instrument, or agreement executed in connection

with the Plan with respect to the Debtors or the Estates.

19. "Released Parties" are defined as:

> collectively, and in each case in its capacity as such, (a) the Debtors, (b) the First Lien Agent, (c) each Holder of a First Lien Claim, (d) the Second Lien Agent, (e) each Holder of a Second Lien Claim, and (f) with respect to each of the foregoing Entities in clauses (a) through (e), such Entity's current or former subsidiaries and Affiliates, and its and their managed accounts or funds, officers, directors, managers, managing members, principals, partners, members, employees, agents, financial advisors, attorneys, accountants, investment bankers, consultants, representatives and other Professionals; provided, however, that (x) if a Holder of Second Lien Claim does not vote to approve the Plan or objects to confirmation of the Plan, such Holder shall be excluded from clause (e) of this defined term and (y) if the Second Lien Agent objects to confirmation of the Plan, the Second Lien Agent and the Holders of Second Lien Claims shall not be Released Parties and clauses (d) and (e) shall read "[reserved]."

Plan at Article I.A..114.

20. The release as presently drafted is broad, and covers not just actions and omissions relating to the Debtors, but rather any claim "based on or relating to any act, omission, transaction, event, or other occurrence taking place on or prior to the Effective Date." While the Debtors have indicated that they intend to limit this release to actions relating to the Debtors, even such limitation remains overly broad.

21. Pursuant to this Court's decision in *In re Tribune Company*, 464 B.R. 126 (Bankr. D. Del. 2011)(Carey, J.), and *In re Washington Mutual, Inc*., 442 B.R. 314 (Bankr. D. Del. 2011)(Walrath, J.), among others, the five factors set forth in *In re Zenith Elecs. Corp*., 241 B.R. 92, 110 (Bankr. D. Del 1999) and *In re Master Mortgage Inv. Fund, Inc.,* 168 B.R. 930, 937-38 (Bankr. W. D. Mo. 1994) should be considered to determine whether, notwithstanding § 524(e) of the Code, a plan may provide for releases by debtors of non-debtor entities. *See Tribune,* 464 B.R. at 186; *Washington Mutual*, 442 B.R. at 346; *In re Spansion, Inc.,* 426 B.R.

114, 142-43, n. 47 (Bankr. D. Del 2010)(Carey, J.); *In re Coram Healthcare Corp.,* 315 B.R. 321, 335 (Bankr. D. Del. 2004)(Walrath, J). Those factors are as follows:

> 1. identity of interests between debtor and non-debtor releasee, so that a suit against the non-debtor will deplete the estate's resources (e.g., due to a debtor's indemnification of a non-debtor);
>
> 2. substantial contribution to the plan by non-debtor;
>
> 3. necessity of release to the reorganization;
>
> 4. overwhelming acceptance of plan and release by creditors; and
>
> 5. payment of all or substantially all of the claims of the creditors and interest holders under the plan.

Tribune, 464 B.R. at 186 (*citing Washington Mutual,* 442 B.R. at 346 (*citing Zenith*, 241 B.R. at 110)). "The factors are neither exclusive nor conjunctive requirements, but simply provide guidance in the Court's determination of fairness." *Tribune,* 464 B.R. at 186 (*citing Washington Mutual*, 442 B.R. at 346).

22. In the present cases, there is an insufficient factual record to determine whether any of the *Zenith* factors are met for any of the Released Parties.

23. With respect to the first *Zenith* factor, which is identity of interests between the Debtors and non-debtor releasees, the only Released Parties as to whom such factor could arguably apply are the officers and directors of the Debtors. However, even if such factor is present, it alone is not sufficient to justify providing the Debtors' officers and directors with Debtor Releases. *See Washington Mutual*, 442 B.R. at 349-350 (finding insufficient basis for the debtors' release of their directors, officers and professionals, even though one of the *Zenith* factors, identity of interest, was present) (*citing Gillman v. Continental Airlines (In re Continental Airlines),* 203 F.3d 203, 216 (3d Cir. 2000)). As to the other categories of Released

Parties, there has been no assertion, let alone proof, of any identity of interests between those parties and the Debtors.

24. As to the second *Zenith* factor, the Debtors must make a sufficient record of any "substantial contribution" made to the Plan by any of the Released Parties. An example of a substantial contribution would be if a Released Party made a lump sum payment to the Plan, thereby allowing the Debtors to make a distribution to unsecured creditors. *See, e.g., Coram*, 315 B.R. at 335. In *Coram*, after examination of the Zenith factors, this Court allowed the debtors to release noteholders who had contributed $56 million in funding to the plan, which funds allowed the debtors to repay in full all creditors other than the noteholders, as well as make a significant distribution to the debtors' shareholders. *Id.*

25. While the Debtors' officers, employees and professionals and fiduciaries may have assisted in negotiating or drafting the Plan, this Court has determined that such efforts do not qualify as the kind of contribution to the Plan that would justify a release. *Washington Mutual*, 442 B.R. at 349-50, 354, and *In re Genesis Health Ventures, Inc.,* 266 B.R. 606–07 (Bankr. D. Del. 2001). In *Washington Mutual*, this Court held that there was no basis for allowing debtor releases or third party releases of the debtors' directors, officers, or professionals when "[t]he only 'contribution' made by them was in the negotiation of the Global Settlement and the Plan, [which] activities are nothing more than what is required of directors and officers of debtors in possession (for which they have received compensation and will be exculpated) . . . ." 442 B.R. at 354. The court found that, although the first *Zenith* factor may be met (identity of interests), the other four were not. The Court commented that, with respect to their post-petition activities that the directors, officers and professionals of the debtors and the Committee were

receiving exculpations, which were sufficient, and releases were "unnecessary, duplicative and exceed the limits of what they are entitled to receive." Id. at 350.

26. Similarly, in *In re Genesis Health Ventures, Inc.*, 266 B.R. 606–07 (Bankr. D. Del. 2001), the Court rejected Debtor releases of its officers, directors, employees and professionals, holding that:

> [T]he release of the debtors' pre-petition claims against the officers, directors, employees and professionals of the debtors is beyond the post-petition focus of the *PWS Holding Corporation* [228 F.3d 224 (3d Cir. 2000)] release clause. . . . As in *Zenith*, the officers and directors of the debtors no doubt made meaningful contribution to the reorganization by designing and implementing the operational restructuring of the companies, and negotiating the financial restructuring with parties in interest. However, the officers, directors and employees have been otherwise compensated for their contributions, and the management functions they performed do not constitute contributions of "assets" to the reorganization.

Genesis Health, 266 B.R. at 606–07 (emphasis added).

27. The Third Circuit Court of Appeals came to the same conclusion in the context of examining third party releases of the Debtors' directors and officers. *See Continental*, 203 F.3d at 215 ("[W]e have found no evidence that the non-debtor D & Os provided a critical financial contribution to the Continental Debtors' plan that was necessary to make the plan feasible in exchange for receiving a release of liability").

28. Like in *Genesis*, the Debtor Releases here are not limited to post-petition activity, as permitted by *PWS*, but also cover all prepetition activity.

29. As to the third *Zenith* factor, the U.S. Trustee leaves the Debtors to their proof as to whether the release of any of the Released Parties is necessary to the reorganization.

30. The fourth *Zenith* factor is overwhelming acceptance of the plan and release provisions by creditors. This information is not yet available.

31. The fifth *Zenith* factor, which is the payment of all or substantially all of the claims of the Debtors' creditors and interest holders cannot be met here, as impaired creditors are receiving a small distribution on account of their claims.

32. The Debtors have the burden to establish whether the *Zenith* factors have been met as to each of the non-debtors who are the beneficiaries of the Debtor Releases. Because an evidentiary predicate is necessary to approve the Debtor Releases, the U.S. Trustee reserves argument on this issue until the record at the confirmation hearing is closed.

The Third-Party Releases Are Not Permissible

33. The Plan's broad releases are not being granted solely by parties who affirmatively vote to accept the Plan or who affirmatively indicate actual consent to the releases, but also extend to numerous parties who have not consented to the releases:

> "Releasing Parties" means, collectively, and in each case in its capacity as such: (a) the Debtors,[2] (b) the First Lien Agent, (c) each Holder of a First Lien Claim, (d) the Second Lien Agent, (e) each Holder of a Second Lien Claim, (f) each Holder of a Claim or Interest that accepts or is deemed to accept the Plan, (g) each other Holder of a Claim or Interest that is entitled to vote on the Plan and does not both (i) vote to reject the Plan or abstain from voting to accept or reject the Plan and (ii) elect the Release Opt Out on its Ballot, and (h) with respect to each of the foregoing Entities in clauses (a) through (g), such Entity's current or former subsidiaries and Affiliates (except for the Debtors' Affiliates), and its and their managed accounts or funds, officers, directors, managers, managing members, principals, partners, members, employees, agents, financial advisors, attorneys, accountants, investment bankers, consultants, representatives and other Professionals.

Plan at Article I.A.115.

[2] The inclusion of the Debtors in the third party releases contained in Article X.C. is problematic for the reasons set forth above regarding the Debtor releases.

34. Some Courts in this District have determined that third party releases of non-debtors[3] should be allowed only if they are consensual. *See In re Washington Mutual, Inc.,* 442 B.R. 314, 352 (Bankr. D. Del. 2011), *citing, inter alia, In re Coram Healthcare Corp.,* 315 B.R. 321, 335 (Bankr. D. Del. 2004)(holding that the "Trustee (and the Court) do not have the power to grant a release of the Noteholders on behalf of third parties," and that such release must be based on consent of the releasing party); *In re Zenith Electronics Corp.,* 241 B.R. 92, 111 (Bankr. D. Del. 1999)(release provision had to be modified to permit third parties' release of non-debtors only for those creditors who voted in favor of the plan); *In re Exide Technologies*, 303 B.R. 48, 74 (Bankr. D. Del. 2003)(approving releases which were binding only on those creditors and equity holders who accepted the terms of the plan).

35. Some Courts in this District have determined that third-party releases of non-debtors should be allowed only to the extent the releasing parties have given affirmative consent. *See In re Washington Mutual, Inc.,* 442 B.R. 314, (Bankr. D. Del. 2011). In *Washington Mutual* the Court held that "any third party release is effective only with respect to those who affirmatively consent to it by voting in favor of the Plan and not opting out of the third party releases." *Id.* at 355 (emphasis added). Moreover, the Court clarified that merely having an opt out mechanism is not enough, holding that an "opt out mechanism is not sufficient to support the third party releases . . . particularly with respect to parties who do not return a ballot (or are not entitled to vote in the first place). Failing to return a ballot is not a sufficient manifestation of consent to a third party release." *Id.* (emphasis added), citing *In re Zenith Electronics Corp.,* 241 B.R. 92, 111 (Bankr. D. Del. 1999).

[3] The Debtors are not entitled to a discharge in these cases, and therefore should not be included in any non-consensual third party release.

36. Other decisions from Court in this District are in accord with *Washington Mutual*. *See In re Coram Healthcare Corp.,* 315 B.R. 321, 335 (Bankr. D. Del. 2004)(holding that the "Trustee (and the Court) do not have the power to grant a release of the Noteholders on behalf of third parties," and that such release must be based on consent of the releasing party); *In re Exide Technologies*, 303 B.R. 48, 74 (Bankr. D. Del. 2003)(approving releases which were binding only on those creditors and equity holders who accepted the terms of the plan); *Zenith*, 241 B.R. at 111 (release provision had to be modified to permit third parties' release of non-debtors only for those creditors who voted in favor of the plan).

37. Under the holding of *Washington Mutual*, and the other cases cited above, the third-party release provision in the Plan renders it unconfirmable because the releases are being forced upon parties who have not provided affirmative consent. Non-consensual releases are being forced upon non-debtor parties in voting classes who do not return a ballot, non-debtor parties in voting classes who submit a vote to reject the plan, but do not also opt out, all unimpaired creditors with no right to opt out, as well as equity holders who are receiving nothing under the plan and are not entitled to opt out of the releases. Releases from such persons and entities are simply not consensual, cannot be simply "deemed" consensual and therefore should not be allowed.

38. In this case, the fiction of "deemed consent" is particularly problematic. The solicitation version of the Plan provided a broad release, of any and all causes of action held by the Releasing Parties against the Released Parties, "based on or relating to any act, omission, transaction, event, or other occurrence taking place on or prior to the Effective Date." It is ludicrous to suggest that creditors would be willing to release claims they hold against releasing parties that are wholly unrelated to the Debtors or these chapter 11 cases for the distributions

being paid on such creditors' claims against the Debtors. This bolsters the conclusion that the failure to respond, object, or opt-out of the release was not an affirmative manifestation of consent to grant the releases.

39. In addition, simply returning a ballot rejecting the Plan should be sufficient manifestation of an intent to reject the releases. "If (as prior cases have held) a creditor who votes in favor of a plan have implicitly endorsed and 'consented' to third party releases that are contained in that plan, then by that same logic a creditor who votes to reject a plan should also be presumed to have rejected the proposed third party releases that are set forth in the plan." *In re Chassix Holdings, Inc*., 533 B.R. 64, 79 (Bankr. S.D.N.Y. 2015). In *Chassix*, the Court determined that creditors who voted to reject the plan would be bound by the third party releases only if they affirmatively elected to opt into such releases.

40. These releases do not pass muster even if the Court were to approve them as non-consensual releases. In *Gillman v. Continental Airlines (In re Continental Airlines)*, 203 F.3d 203 (3d Cir. 2000), the Third Circuit surveyed cases from various circuits as to when, if ever, a non-consensual third party release is permissible. The Court acknowledged that a number of Circuits do not allow such non-consensual releases under any circumstances. *See id*. at 212. Other Circuits, the Court found, "have adopted a more flexible approach, albeit in the context of extraordinary cases," such as mass tort cases. *See id*. at 212, *citing Securities and Exchange Commission v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Group, Inc.),* 960 F.2d 285, 293 (2d Cir. 1992); *Kane v. Johns-Manville Corp. (In re Johns-Manville Corp.),* 843 F.2d 636, 640, 649 (2d Cir. 1988). *See also, In re Metromedia Fiber Network, Inc.,* 416 F.3d 136, 141 (2d Cir. 2005)(third party release may be granted "only in rare cases").

41. The Third Circuit in *Continental Airlines* ultimately determined that the proposed releases in that case, which enjoined shareholder lawsuits against debtors' directors and officers, did "not pass muster under even the most flexible test for the validity of non-debtor releases." *Continental*, 203 F.3d at 214. Therefore, the Court determined that it "need not speculate on whether there are circumstances under which we might validate a non-consensual release that is both necessary and given in exchange for fair consideration." *Id.* at 214, n. 11. However, the Court did describe the "hallmarks of permissible non-consensual releases" to be "fairness, necessity to the reorganization, and special factual findings to support these conclusions." *Id.* at 214.

42. In *In re Genesis Health Ventures, Inc.,* 266 B.R. 591 (Bankr. D. Del. 2001), the Court held that the exculpation clause was actually a release that required factual showings under *Continental* – that the releases were necessary for the reorganization and were given in exchange for fair consideration. *Id.* at 607. The Court elaborated that "necessity" under *Continental* requires a showing: (a) that the success of the debtors' reorganization bear a relationship to the release of the non-consensual non-debtor parties and (b) that the non-debtor parties being released from liability have provided "a critical financial contribution to the debtors' plan" in exchange for the receipt of the release. *Id*. at 607. A financial contribution is considered "critical" if without the contribution, the debtors' plan would be infeasible. *Id*. Fairness of a release is determined by examining whether non-consenting non-debtors are receiving reasonable consideration in exchange for the release. *Id.* at 608. In most instances of a release provision in a plan, this will entail examining the proposed dividend that non-consenting creditors will receive under a plan with the releases compared to what they would receive under

a plan without the releases. *See id.; see also In re Spansion, Inc.*, 426 B.R. 114, 144 (Bankr. D. Del 2010)(applying same factors).

43. The *Genesis* Court found that the senior lenders had made a financial contribution to the plan, which allowed the debtors to make the 7.34% distribution to the unsecured creditors, who otherwise would be "out of the money." *Id.* at 608. Ultimately, though, the Court found that such contribution was not enough, because "even if the threshold *Continental* criteria of fairness and necessity for approval of non-consensual third-party releases were marginally satisfied by these facts . . . . [the] financial restructuring plan under consideration here would not present the extraordinary circumstances required to meet even the most flexible test for third party releases." *Id.* (emphasis added).

44. In the present cases, there is nothing in the record to indicate the presence of "extraordinary circumstances," or that that the high threshold necessary for approval of non-consensual third party releases has been met with respect to each of the non-debtor parties that would be the recipients of these non-consensual releases. *See Continental,* 203 F.3d at 215 ("[W]e have found no evidence that the non-debtor D & Os provided a critical financial contribution to the Continental Debtors' plan that was necessary to make the plan feasible in exchange for receiving a release of liability"); *Genesis*, 266 B.R. at 606–07 ("[T]he officers, directors and employees have been otherwise company pensated for their contributions, and the management functions they performed do not constitute contributions of 'assets' to the reorganization.").

45. The Debtors have the burden of establishing whether any of the Released Parties provided a "critical financial contribution," and whether the other *Continental/ Genesis* factors have been met. The Debtors here should not be allowed the unfettered discretion to force

creditors to discharge nondebtors from liability, because a permanent injunction limiting the liability of nondebtor parties is a rare thing that should not be considered absent a showing of "extraordinary circumstances." *See Continental*, 203 F.3d at 212; *Tribune*, 464 B.R. at 178 (interpreting *Continental* to allow non-consensual releases only in "extraordinary cases."); *Genesis*, 266 B.R. at 608.

46. Finally, the scope of Third-Party Releases is much broader than is permissible. As the Court in *Washington Mutual* determined, the scope of releases given by creditors and shareholders, even when consensual, should be limited to "claims of creditors relating to claims they have asserted against the Debtors." 442 B.R. at 356. When limited in that manner, the releases would not affect any direct claims the creditors may have against non-debtor parties. As the third-party releases in the Plan are not so limited, the Plan is not confirmable.

47. The Debtors have the burden of justifying the validity of the Third-Party Releases, whether consensual or non-consensual, for each and every party to be released. Because an evidentiary predicate is necessary to approve the Third-Party Releases, the U.S. Trustee reserves argument on this issue until the record at the confirmation hearing is closed.

The Debtors Must Establish That The Plan Is Feasible

48. In order to be confirmable, the Plan must provide that certain claimholders receive payment in full of their claims. 11 U.S.C. § 1129(a)(9). Furthermore, confirmation of the plan is must not be likely to be followed by further financial reorganization of the debtor, unless such liquidation or reorganization is proposed in the plan. 11 U.S.C. § 1129(a)(11).

49. The Debtors must establish that they have sufficient funds to pay Administrative Expense Claims and Priority Tax Claims in full, as required by the Bankruptcy Code.

The Debtors are Not Entitled to a Discharge

50. These Debtors are corporate Debtors who are liquidating all of their assets and will not continue in operations post-confirmation. As such, they are not entitled to a discharge.

51. Section 1141(d)(3) of the Bankruptcy Code states:

> The confirmation of a plan does not discharge a debtor if-
>
> (A) the plan provides for the liquidation of all or substantially all of the property of the estate;
>
> (B) the debtor does not engage in business after consummation of the plan; and
>
> (C) the debtor would be denied a discharge under Section 727(a) of this title if the case were a case under chapter 7 of this title.

52. Section 727(a)(1) provides: "The court shall grant the debtor a discharge, unless the debtor is not an individual...".

53. Here, the Debtors are not individuals, they have liquidated substantially all of the property of their estates, and they will not engage in any business. Thus, the Debtors would not be entitled to a discharge even if they were otherwise able to confirm a chapter 11 plan of liquidation.

54. While the Plan does not expressly provide a discharge to the Debtors, it contains provisions that effectively provide an impermissible discharge.

55. First, the Plan provides that it is a "good faith compromise of all Claims, Interests and controversies relating to the contractual, legal and subordination rights that a

Holder of a Claim or Interest may have with respect to any Allowed Claim or Allowed Interest, or any distribution to be made on account of such Allowed Claim or Allowed Interest." Plan, at Article X.A. This language provides the equivalent of a discharge, by requiring that the distributions required to be made under the Plan constitute a settlement and compromise with creditors. To the contrary, they are the distributions required to be made under the Plan, but the underlying claims, which are not being paid in full, are not compromised or settled.

56. The Bankruptcy Code permits the Debtors to "settle" claims *it holds* in a Plan, but not claims *held by creditors against the Debtors.* 11 U.S.C. § 1123(b)(3)(A) (the plan may provide for "the settlement or adjustment of any claim or interest belonging to the debtor or to the estate."

57. Second, the injunction provision of the Plan must be modified so as to exclude the Debtors from its protections. Enjoining claims against the Debtors is the equivalent of an improper Discharge.

WHEREFORE, the United States requests that this Court deny confirmation of the Plan, and grant such other relief as this Court deems appropriate, fair and just.

Dated: July 23, 2018 Wilmington, Delaware	Respectfully submitted, **ANDREW R. VARA** **ACTING UNITED STATES TRUSTEE** By: */s/ Linda J. Casey*
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