Docket #0157 Date Filed: 07/02/2020

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
TEMPLAR ENERGY LLC, *et al.*,	:	Case No. 20-11441 (BLS)
	:	**Hearing Date: July 14, 2020, at 10:30 a.m.**
Debtors.	:	**Confirmation Objection: July 2, 2020, at 4:00 p.m.**

OBJECTION BY THE UNITED STATES TO THE JOINT PREPACKAGED PLAN OF LIQUIDATION OF TEMPLAR ENERGY LLC AND ITS DEBTOR AFFILIATES UNDER CHAPTER 11 OF THE BANKRUPTCY CODE

The United States, on behalf of its Department of Interior ("DOI"), by and through the undersigned attorneys, files this objection to the Joint Prepackaged Plan of Liquidation of Templar Energy LLC and its Debtor Affiliates under Chapter 11 of the Bankruptcy Code ("Plan"). [Docket No. 16]. In support of its objection, the United States avers as follows:

BACKGROUND

1. On June 1, 2020, the Debtors filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. [Docket No. 1].

2. The United States, on behalf of the DOI, is a party to at least thirty-five leases with the Debtors ("DOI Leases").

3. On June 1, 2020, the Debtors filed a Motion for Entry of Orders (A)(I) Approving Bidding Procedures for the Sale of All or Substantially All of the Debtors' Assets, (II) Approving Bid Protections, (III) Scheduling a Sale Hearing and Objection Deadlines with Respect to the Sale, (IV) Scheduling an Auction, (V) Approving the Form and Manner of Notice of the Sale Hearing

and Auction, (VI) Approving Contract Assumption and Assignment Procedures, and (VII) Granting Related Relief; and (B)(I) Approving the Sale of the Debtors Free and Clear of All Liens, Claims, Interests, and Encumbrances, (II) Approving the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases, and (III) Granting Related Relief ("Sale Motion"). [Docket No. 47].[1] The United States objects to the assumption or assignment of the DOI Leases, or any federal interests, without government consent and compliance by the Debtors and the purchaser with all non-bankruptcy law. The United States presently intends to object to the Sale Motion.

4. On June 1, 2020, the Debtors filed the Plan.

OBJECTION

5. **Effective Date should not be altered by the Plan**. The Plan provides that distributions made after the Effective Date to holders of Disputed Claims that are not Allowed Claims as of the Effective Date, but which later become Allowed Claims, shall be deemed to have been made on the Effective Date. (Plan, Article VII(C)(1)). The United States objects to the change in the meaning of Effective Date as unfair and prejudicial to creditors. The alteration of this defined Plan term allows the Debtors to avoid the payment of interest to creditors that they would otherwise be obligated to pay.

6. **Payment of Administrative Expense Claims and Priority Tax Claims does not comply with the Bankruptcy Code**. Sections 1129(a)(9)(A) and (C), respectively, and Section 511 of the Bankruptcy Code require the payment of interest on administrative expense claims and priority tax claims. The Plan states in relevant part:

[1] Debtors have informed the United States that all real property and wells of the debtors will be sold. The United States reserves all rights in the event that this representation is not correct.

> **Allowed**. …For purposes of computing Distributions under the Plan, a Claims that has been deemed "Allowed" shall not include interest, costs, fees, or charges on such Claim or Interest from and after the Petition Date, except as provided in section 506(b) of the Bankruptcy Code or as otherwise expressly set forth in the Plan. [Plan, Article I(A)(5)].

This Plan provision impairs the rights of creditors who do not receive the interest that they would otherwise be entitled to in accordance with the Bankruptcy Code. The United States objects to the Plan to the extent that it fails to provide for the payment of an adequate rate of interest on the secured claims, if any, and the administrative expense and priority tax claims of the United States. [Plan, Article II (A)(1) and (B)], *See* 11 U.S.C. Section 503(b)(1)(C) and Section 511; *United States v. Friendship College, Inc.*, 737 F.2d 430 (4th Cir. 1984); *In re Mark Anthony Construction, Inc.*, 886 F.2d 1101 (9th Cir. 1989).

7. **Administrative Claim Bar Date does not comply with the Bankruptcy Code and the Local Rules**. The United States objects to the Plan to the extent the Plan purports to set an administrative claims bar date for taxes described in 11 U.S.C. Section 503(b)(1)(B) and (C) in violation of Section 503(b)(1)(D) of the Bankruptcy Code. [Plan, Article I(A)(2)]. This provision violates not only Section 503(b)(1)(D) of the Bankruptcy Code but Delaware Local Bankruptcy Rule 3002-1(a). Delaware Local Rule 3002-1(a) provides in pertinent part:

> Chapter 11 Administrative Claims. Notwithstanding any provision of a plan of reorganization, any motion, notice, or court order in a specific case, the government shall not be required to file any proof of claim or application for allowance for any claims covered by Section 503 (b) (1) (B), (C), or (D).

8. **Settlement not appropriate**. The United States objects to the provision in the Plan which provides:

> Compromise and Settlement of Claims, Interests and Controversies. Pursuant to section 363 of the Bankruptcy Code and Bankruptcy Rule 9019 and in consideration for the distributions and other benefits provided

> pursuant to the Plan, the provisions of the Plan shall constitute 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. The entry of the Confirmation Order shall constitute the Bankruptcy Court's approval of the compromise or settlement of all such Claims, Interests and controversies, as well as a finding by the Bankruptcy Court that such compromise or settlement is in the best interests of the Debtors, their Estates, and Holders of Claims and Equity Interests and is fair, equitable, and reasonable... [Plan, Article X(A)].

Section 1123(b)(3)(A) of the Bankruptcy Code provides for the settlement or adjustment of any claim belonging to the Debtor or to the estate. The Debtors here are not settling their own claims but instead are attempting to settle the unknown claims of unknown creditors without providing adequate notice. This would result in substantial injustice to the interests of the United States. By virtue of the Plan process, the United States does not waive sovereign immunity and has not consented to the compromise or settlement of its claims and this provision is unfairly prejudicial to the rights of the United States.

9. **Non-Debtor Releases**. The United States opts out of and objects to the third party non-debtor limitation of liability, discharge, injunction, exculpation and release provisions set forth in Article X and elsewhere in the Plan. The Plan currently provides for broad third party injunctions, exculpations and releases. While the Third Circuit stopped short of adopting a *per se* rule that a non-debtor release in a reorganization plan is not permissible (as other circuits have done), it held that, at most, such a provision could only be valid in "extraordinary" cases. *Gillman v. Continental Airlines (In re Continental Airlines),* 203 F.3d 203, 212 (3d Cir. 2000). At minimum, *Continental* held that such a nonconsensual release of non-debtor entities must contain all of the following "hallmarks": "fairness, necessity to the reorganization, and specific factual findings to support these conclusions." *Id*. at 214*; see also In re Wash. Mut., Inc.*, 442 B.R. 314, 351-52 (Bankr. D.

Del. 2011) (collecting cases). This Court has interpreted *Continental's* holding on non-debtor releases to mean that "limiting the liability of non-debtor parties is a *rare thing that should not be considered absent a showing of exceptional circumstances* in which several key factors are present." *In re Genesis Health Ventures, Inc.*, 266 B.R. 591, 608 (Bankr. D. Del. 2001) (emphasis added). This Court has previously held that a non-debtor release over a creditor's objection "would not pass muster." *Wash. Mut.*, 442 B.R. at 352 ("This Court has previously held that it does not have the power to grant a third party release of a non-debtor."). Where this Court has even contemplated approval of a non-consensual release, it has required the following factors be present to justify the "rare" release: "(1) the non-consensual release was necessary to the success of the reorganization, (2) the releases have provided a critical financial contribution to the Debtor's plan, (3) the releases' financial contribution is necessary to make the plan feasible, and (4) the release is fair to the non-consenting creditors, i.e., whether the non-consenting creditors received reasonable compensation in exchange for the releases." *In re Tribune Co.*, 464 B.R. 126, 177-78 (Bankr. D. Del. 2011); *see also Genesis Health Ventures*, 266 B.R. at 607-09. Here, setting aside the question of whether the Debtors have made such a showing against all creditors generally (and it has not), the Debtors make no adequate showing of a single factor, let alone all of the *Tribune/Genesis* factors, that justifies the extraordinary release of non-debtors in these liquidating cases with respect to their potential liability to the United States.

10. **Setoff and Recoupment**. The United States objects to the Plan to the extent it fails to preserve the setoff and recoupment rights of the United States. Confirmation of a plan does not extinguish setoff claims when they are timely asserted. *In re Continental Airlines*, 134 F.3d at 542 (3d Cir. 1998). Like other creditors, the United States has the common law right to setoff mutual debts. "The government has the same right which belongs to every creditor, to apply the

unappropriated moneys of his debtor, in his hands, in extinguishment of the debts due to him." *United States v. Munsey Trust Co. of Washington, D.C.*, 332 U.S. 234 (1947) (citing *Gratiot v. United States*, 40 U.S. (15 Pet) 336, 370, 10 L.Ed. 759 (1841)); *see also Amoco Prod. Co. v. Fry*, 118 F.3d 812, 817 (D.C. Cir. 1997). This right – "which is inherent in the federal government – is broad and 'exists independent of any statutory grant of authority to the executive branch.'" *Marre v. United States*, 117 F.3d 297, 302 (5th Cir. 1997) (quoting *United States v. Tafoya*, 803 F.2d 140 (5th Cir. 1986)). Hence, the United States can setoff mutual prepetition debts and claims as well as postpetition debts and claims. *Zions First Nat'l Bank, N.A. v. Christiansen Bros.* (*In re Davidson Lumber Sales, Inc.*), 66 F.3d 1560, 1569 (10th Cir. 1995); *Palm Beach County Bd. of Pub. Instruction (In re Alfar Dairy, Inc.)*, 458 F.2d 1258, 1262 (5th Cir.), *cert. denied*, 409 U.S. 1048 (1972); *Mohawk Indus., Inc. v. United States (In re Mohawk Indus., Inc.)*, 82 B.R. 174, 178-79 (Bankr. D. Mass. 1987). The Plan makes no provision for these rights. Such treatment is impermissible, because Section 553 of the Bankruptcy Code preserves the right of setoff in bankruptcy as it exists outside bankruptcy, *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 18 (1995), neither expanding nor constricting it, *United States v. Maxwell*, 157 F.3d 1099, 1102 (7th Cir. 1998). "[T]he government of the United States suffers no special handicap under § 553 of the Bankruptcy Code," *id*. at 1103, that alters this principle. Moreover, because "[s]etoff occupie[s] a favored position in our history of jurisprudence," *Bohack Corp. v. Borden, Inc.*, 599 F.2d 1160, 1164 (2d Cir. 1979), courts do not interfere with its exercise absent "the most compelling circumstances." *Niagara Mohawk Power Corp. v. Utica Floor Maintenance, Inc. (In re Utica Floor Maintenance, Inc.)*, 41 B.R. 941, 944 (N.D.N.Y. 1984); *see also New Jersey Nat'l Bank v. Gutterman (In re Applied Logic Corp.)*, 576 F.2d 952 (2d Cir. 1978) ("The rule allowing setoff ... is not one that courts are free to ignore when they think application would be unjust.").

Compelling circumstances generally entail criminal conduct or fraud by the creditor. *In re Whimsy, Inc.*, 221 B.R. 69 (S.D.N.Y. 1998). No such compelling circumstances are present here, and accordingly, the Plan must provide for and preserve the federal government's setoff rights. Failure to do so violates Section 1129(a)(1). ("The court shall confirm a plan only if . . . the plan complies with the applicable provisions of this title.")

11. Similarly, the Plan improperly fails to preserve recoupment rights of the United States. Recoupment is unaffected by discharge. *Megafoods Stores, Inc. v. Flagstaff Realty Assocs.* (*In re Flagstaff Realty Assocs.*), 60 F.3d 1031, 1035-36 (3rd Cir. 1995) (holding that recoupment survives discharge following confirmation and implementation of chapter 11 plan even if creditor did not object to plan or seek a stay pending appeal); *see also Beaumont v. Dep't of Veteran Affairs* (*In re Beaumont*), 586 F.3d 776 (10th Cir. 2009); *Saif Corp. v. Harmon* (*In re Harmon*), 188 B.R. 421, 425 (B.A.P. 9th Cir. 1995) ("Because recoupment only reduces a debt as opposed to constituting an independent basis for a debt, it is not a claim in bankruptcy, and is therefore unaffected by the debtor's discharge."); *Lunt v. Peoples Bank* (*In re Lunt*), 500 B.R. 9, 16 (D. Kan. 2013); *Mercy Hosp. of Watertown v. New York*, 171 B.R. 490, 495 (N.D.N.Y. 1994); *Brown v. General Motors Corp.*, 152 B.R. 935, 938 (W.D. Wis. 1993) (holding right of recoupment not a claim or debt to be discharged in bankruptcy). For the same reasons as stated above with respect to setoff rights, this Plan provision dispensing creditors' recoupment rights is impermissible and impairs creditors.

12. The United States further objects to the Debtors' attempts to strip the United States of its rights to assert setoff on an expedited time schedule that is entirely for the benefit of, and mandated by, the Debtors. The Plan provides that "[i]n no event shall any Holder of Claims or Interests be entitled to set off any Claim or Interest against any claim, right or Cause of Action of the applicable Debtor or the Plan Administrator unless such Holder has Filed a motion with the

Bankruptcy Court requesting the authority to perform such setoff on or before the Confirmation Date." [Plan, Article X(F)]. The Plan has a similar egregious provision relating to recoupment. [Plan, Article X(H)]. The Debtors are seeking a sale of their assets and confirmation of the Plan barely a month after filing for bankruptcy. The United States is entitled to file claims in the bankruptcy cases for a period of six months after the date the Debtors filed their Bankruptcy petitions. Fed. R. Bankr. P. 3002(c)(1). The facts of this case are unlike those considered by the Third Circuit in its *Continental* decision. The Third Circuit surely did not intend that where the government is forced into an expedited bankruptcy process, it would lose its setoff rights months before the government is even required to file its claims. *In re Continental Airlines*, 134 F.3d 536, (3d. Cir. 1998).

13. **Rejection Damage Claims**. The United States objects to the treatment of rejection damages claims as outlined in the Plan. While rejection damages claims are limited to money damages which will receive no distribution under the Plan, notwithstanding any nonbankruptcy law to the contrary, the Debtors expressly reserve and do not waive any right to receive, or any continuing obligation of a counterparty to provide, warranties or continued maintenance obligations on goods previously purchased by the contracting Debtors, as applicable, from counterparties to rejected or repudiated executory contracts or unexpired leases. [Plan, Article VI(B]. The United States objects to these provisions in the Plan as inequitable and prejudicial to creditors.

14. **Undeliverable Property**. The United States objects to the time frames set forth in the Plan governing undeliverable property and the cashing of checks as being unreasonably short and prejudicial to creditors. [Plan, Article VII(D)].

15. **No Consent Rights**. The Plan provides in pertinent part that "[n]otwithstanding anything in the Plan to the contrary, any and all consent rights of the RBL Agent or the Requisite Lenders set forth in the RSA (irrespective of whether the RSA has been assumed by the Debtors) with respect to the form and substance of this Plan, the Plan Supplement, and any other documents contemplated under the Plan shall apply to the Plan as if stated in full herein until such time as the RSA is terminated in accordance with its terms**."** The United States objects to the imposition of any consent rights that govern the substance of the Plan and related Plan documents unless and until such rights are disclosed and fully stated in the Plan. [Plan, XIV(C)].

CONCLUSION

16. **The Plan does not comply with Section 1129(a)(1) of the Bankruptcy Code**. For the reasons stated above, the Plan does not comply with the applicable provisions of Title 11 and therefore cannot be confirmed pursuant to Section 1129(a)(1) of the Bankruptcy Code.

WHEREFORE, the United States respectfully requests that the Court deny confirmation of the Plan and grant such other and further relief as the Court deems necessary and just.

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BY: */s/ Ellen Slights*
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Dated: July 2, 2020

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AFFIDAVIT OF SERVICE

I, Shane Macas, an employee in the Office of the United States Attorney for the District of Delaware, hereby attest that on July 2, 2020, I caused to be served a copy of the **OBJECTION BY THE UNITED STATES TO THE JOINT PREPACKAGED PLAN OF LIQUIDATION OF TEMPLAR ENERGY LLC AND ITS DEBTOR AFFILIATES UNDER CHAPTER 11 OF THE BANKRUPTCY CODE** by electronic service on the registered parties via the Court's CM/ECF system and upon the following parties

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