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Hearing: September 23, 2020 at 11:00 a.m.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re	:	**Chapter 11**
JCK LEGACY COMPANY, *et al.*,	:	**Case No. 20-10418 (MEW)**
Debtor.	:	**(Jointly Administered)**

OBJECTION OF THE UNITED STATES TRUSTEE TO CONFIRMATION OF THE JOINT CHAPTER 11 PLAN OF DISTRIBUTION OF THE McCLATCHY COMPANY AND ITS AFFILIATED DEBTORS AND DEBTORS IN POSSESSION

William K. Harrington, the United States Trustee for Region 2 (the "**United States Trustee**"), by and through his undersigned counsel, hereby submits his objection (the "**Objection**") to confirmation of the *Joint Chapter 11 Plan of Distribution of the McClatchy Company and Its Affiliated Debtors and Debtors in Possession* [ECF No. 780] (the "**Plan**") filed by The McClatchy Company and its affiliated debtors and debtors in possession (collectively, the "**Debtors**") seeking certain relief under title 11 of the United States Code (the "**Bankruptcy Code**"), the Federal Rules of Bankruptcy Procedure (the "**Bankruptcy Rules**), and the Local Rules for the Southern District of New York (the "**Local Bankruptcy Rules**").[1] In support of the Objection, the United States Trustee respectfully states:

[1] Capitalized terms not otherwise defined herein shall have the same meaning as set forth in the Plan.

PRELIMINARY STATEMENT

The United States Trustee objects to confirmation of the Debtors' Plan on the following grounds:[2]

a. The Plan, which facilitates a liquidation of all or substantially all of the property of the Debtors' estates, provides for a discharge and a broad injunction against discharged claims in violation of 11 U.S.C. § 1141(d)(3). Liquidating corporate debtors are not entitled to a discharge under the plain language of the Bankruptcy Code.

b. The Plan provides that "all other Holders of Claims to the fullest extent permitted by law" will give broad releases to third parties. This portion of the definition of Releasing Parties is ambiguous and overly broad. The Debtors contend that the proposed third party releases are consensual. Accordingly, the definition of Releasing Parties should be clarified and narrowed to provide that only parties that have affirmatively manifested their consent are giving releases.

c. The Plan inappropriately provides prospective releases to entities that do not yet exist. Specifically, the Wind-Down Debtors, the Plan Administration Trust, and the GUC Recovery Trust all receive prospective releases under the Plan's release provisions.

d. The Plan's proposed exculpation and limitation of liability provision is overly broad and should be narrowed consistent with this Court's guidance on the appropriate scope of exculpation provisions as detailed below.

e. The Plan inappropriately provides for administrative expense treatment for the fees and expenses of non-estate professionals.

f. The Plan fails to provide for the filing of post-confirmation operating reports.

For these reasons, as detailed more fully below, the United States Trustee respectfully requests that the Court deny confirmation of the Plan unless modified to address these issues.

[2] The United States Trustee has relayed these objections to counsel for the Debtors and hopes to resolve most, if not all, of these concerns on a consensual basis. However, out of an abundance of caution, the United States Trustee files the instant Objection.

BACKGROUND

A. General Background

1. On February 13, 2020 (the "**Petition Date**"), each Debtor commenced a case by filing a petition for relief under chapter 11 of the Bankruptcy Code (collectively, the "**Chapter 11 Cases**"). The Chapter 11 Cases are jointly administered.

2. On the Petition Date, the Debtors filed the *Declaration of Sean M. Harding in Support of Chapter 11 Petitions and First Day Papers* [ECF No. 23] (the "**First Day Declaration**").

3. On the Petition Date, the Debtors filed an initial chapter 11 plan (the "**Initial Plan**") and disclosure statement (the "**Initial Disclosure Statement**"). ECF Nos. 25 and 27, respectively.

4. On February 26, 2020, the United States Trustee appointed an official committee of unsecured creditors in the Chapter 11 Cases (the "**Committee**"). *See Notice of Appointment of Official Committee of Unsecured Creditors*. ECF No. 114.

B. The Sale and the Settlement Agreement

5. During the Chapter 11 Cases, the Debtors engaged in a Court-approved multiparty mediation with the Pension Benefit Guaranty Company (the "**PBGC**"), Chatham Asset Management, LLC (**Chatham**"), Brigade Capital Management ("**Brigade**"), and the Committee. Disclosure Statement (defined below) at 1.

6. While the mediation was ongoing, the Debtors engaged in a parallel marketing process of substantially all of their assets. *Id*. at 2. On May 11, 2020, the Court entered an order

which, *inter alia*, established bid procedures relating to a sale of substantially all of the Debtors' assets. ECF No. 432.

7. The Debtors ultimately selected the bid submitted by SIJ Holdings, LLC, an affiliate of Chatham (the "**Purchaser**") as the successful bid, which was comprised of a $262,851,000 credit bid component and $49,152,903 in cash consideration. Disclosure Statement at 2.

8. On August 7, 2020, the Court entered the *Order (I) Approving the Sale of the Acquired Assets Free and Clear of Claims, Liens, Interests and Encumbrances; (II) Approving the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases; And (III) Granting Related Relief* (the "**Sale Order**). ECF No. 744.

9. In connection with the Sale Order, the Debtors, the Committee, Chatham, Brigade, and the Purchaser entered into a mediated settlement agreement (the "**Settlement Agreement**"), which is annexed to the Sale Order as Annex A. The Sale Order approved the Settlement Agreement, provided that to the extent any provisions of the Settlement Agreement are to be implemented in the Plan, such provisions shall be incorporated into the Plan and approval thereof shall be subject to confirmation of such Plan. Sale Order at ¶ 39.

C. <u>The Plan</u>

10. The Debtors filed the Plan and a supplemental disclosure statement (the "**Disclosure Statement**") on August 21, 2020. ECF Nos. 780 and 781, respectively. On September 9, 2020, the Debtors filed a notice of proposed findings of fact, conclusions of law, and order approving the disclosure statement and confirming the Plan (the "**Proposed Order**"). ECF No. 829. Also, on September 9, 2020, the Debtors file the declaration of Sean M. Harding in

support of confirmation of the plan (the "**Harding Confirmation Declaration**"). ECF No. 828.

11. The Plan provides for a discharge of the Debtors pursuant to section 1141 of the Bankruptcy Code. Plan at § 10.2 (Discharge of the Debtors). The Plan also provides for a broad injunction against, *inter alia*, all Entities who have held, hold or may hold Claims or Interest that have been discharged under the Plan. Plan at § 10.7 (Injunction).

12. The Plan provides for a broad release to be given by certain "Releasing Parties" to the Debtors, the Wind-Down Debtors, the Plan Administration Trust, the GUC Recovery Trust, and certain other defined "Released Parties." Plan at § 10.5 (Release by Holders of Claims and Interests); § 1.139 (defining "Released Parties"); § 1.140 (defining "Releasing Parties").

13. The Plan provides for exculpation and limitation of liability for certain defined "Exculpated Parties" from certain defined "Exculpated Claim[s]." Plan at § 10.6 (Exculpation and Limitation of Liability); § 1.78 (defining "Exculpated Claim"); § 1.79 (defining "Exculpated Parties").

14. The Plan provides that certain non-estate professional fees and expenses shall constitute Allowed Administrative Claims and shall be paid in full on the Effective Date. Specifically, the professional fees and expenses of the Chatham Parties and the Brigade Parties shall constitute allowed Administrative Claims under the Plan and shall be paid in full subject to the Professional Fee Caps. Plan at § 2.2. The Plan also provides that the fees and expenses of counsel to each of the 2027 Debentures Trustee and the 2029 Debentures Trustee shall constitute Allowed Administrative Claims and shall be paid in full in cash on the Effective Date. Plan at § 2.4.

15. The Plan fails to require post-confirmation operating reports. *See generally* Plan.

OBJECTION

Section 1129(a)(1), (2) and (3) provide, respectively, that in order for a chapter 11 plan to be confirmed, (i) the plan must comply with "the applicable provisions of this title," (ii) the proponent must comply with "the applicable provisions of this title," and (iii) the plan must be proposed by means not forbidden by law. 11 U.S.C. § 1129(a)(1), (2), (3). The plan proponent bears the burden of proof with respect to each of these elements. *In re Charter Commc'ns*, 419 B.R. 221, 243 (Bankr. S.D.N.Y. 2009) (citing *Heartland Fed. Savs. & Loan, Ass'n v. Briscoe Enters. (In re Briscoe Enters.)*, 994 F.2d 1160, 1165 (5th Cir. 1993) (stating that "[t]he combination of legislative silence, Supreme Court holdings, and the structure of the Code leads this Court to conclude that preponderance of the evidence is the debtor's appropriate standard of proof both under § 1129(a) and in a cramdown")); *In re Worldcom, Inc.*, No. 02-13533 (AJG), 2003 WL 23861928, at *46 (Bankr. S.D.N.Y. Oct. 31, 2003) (citing *Briscoe*); 7 *Collier on Bankruptcy* ¶ 1129.02 (16th ed. 2020).

Consistent with these standards, the United States Trustee raises the following specific objections to confirmation of the Plan.

A. The Plan Provides for a Discharge and an Overly Broad Injunction in Violation of 11 U.S.C. § 1141(d)(3)

The Plan provides for a discharge of the Debtors pursuant to section 1141 of the Bankruptcy Code. Plan at § 10.2. However, section 1141(d)(3) expressly provides that confirmation of a chapter 11 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 the Bankruptcy Code if the case were a case under chapter 7. 11 U.S.C. §

1141(d)(3). A debtor is denied a discharge under section 727(a)(1) if it is not an individual, which is the case here. 11 U.S.C. § 727(a)(1). Under sections 1141(d)(3) and 727(a)(1), a liquidating corporate debtor is not entitled to a discharge. *In re Prudential Lines Inc.*, 928 F.2d 565, 573 (2d Cir. 1991) ("[A] liquidating corporation's debts are not discharged in bankruptcy."); *In re Dominguez*, 51 F.3d 1502, 1508 (9th Cir. 1995) ("Liquidating corporations[. . .] are automatically precluded from discharge.") (internal citations omitted); *Credit Suisse First Bos. Mortg. Capital LLC v. Cohn*, No. 03 CIV. 6146 (DC), 2004 WL 1871525, at *8 n. 3 (S.D.N.Y. Aug. 19, 2004) ("[I]t is unlikely that [corporate liquidating debtor] will receive a discharge of liability."); *Ackles v. A.H. Robins Co. (In re A.H. Robins Co.)*, 59 B.R. 99, 102, n. 3 (Bankr. E.D.Va. 1986), *aff'd*, 828 F.2d 1029 (4th Cir.1987) ("If it is a liquidating Chapter 11, the corporate debtor does not receive a discharge of any of its debts."); *Dutcher v. Reorganized Pettibone Corp.*, 193 B.R. 667, 668 (S.D.N.Y. 1996) ("Confirmation of a plan discharges a corporation of all its debts unless it is a liquidating plan.")

Here, the Debtors are liquidating, they will not engage in business after consummation of the plan, and they are not individuals. The Debtors have sold substantially all of their assets. Harding Confirmation Declaration at ¶ 39 ("The Debtors have already sold substantially all of their assets through the Sale Transaction); Proposed Order at ¶ 27 (". . .the Debtors have already sold substantially all of their assets . . ."); Settlement Agreement at ¶ 1 ("The parties will affirmatively support entry of an order [. . .] approving [. . .] the sale [. . .] of substantially all of the Debtors' assets to the buyer-entity . . ."). Pursuant to the Settlement Agreement, the Debtors are now attempting to confirm a plan of distribution and wind down their estates. *See* Harding Confirmation Declaration at ¶ 9. The Plan contemplates that certain debtors shall continue in

existence after the Effective Date only for certain limited purposes as Wind-Down Debtors. Disclosure Statement at 7. Upon completion of the Wind Down, the Plan Administrator will take steps to dissolve any remaining Debtor entity. *Id.* Consequently, pursuant to section 1141(d)(3), these liquidating corporate Debtors are not entitled to a discharge and any portion of the Plan providing for a discharge should not be approved.

Additionally, the Plan inappropriately provides for a broad injunction against, *inter alia*, all Entities who have held, hold or may hold Claims or Interests that have been discharged under the Plan. Plan at § 10.7. This injunction runs afoul of section 1141(d)(3) and should not be approved. Because this is a liquidating plan, any injunction should be limited to an injunction against interference with the Plan or with the property to be distributed under the Plan.

B. The Definition of "Releasing Parties" is Ambiguous and Overly Board

Section 10.5 of the Plan provides that "Releasing Parties" will give a broad release, waiver, and discharge of claims against the Debtors, the Wind-Down Debtors, their Estates, the Plan Administration Trust, the GUC Recovery Trust, and the "Released Parties," which includes DIP Lenders, the DIP Agent, the Brigade Parties, the Chatham Parties, the Purchaser; the 2027 Debentures Trustee, the 2029 Debentures Trustee, and the Committee and its members (each in their capacities as such). Plan at § 10.5. The Initial Plan filed by the Debtors on the Petition Date defined the term "Releasing Parties" to make clear the effect of voting and opting in or out of the release provisions. *See* Initial Plan, ECF No. 25 at § 1.154. This is no longer the case. The current Plan now defines Releasing Parties to include, among other parties, "all other Holders of Claims to the fullest extent permitted by law." Plan at § 1.140(j). This definition is ambiguous

and leaves open to interpretation the question of who is giving a broad release.[3] The Court should not approve the proposed release provision unless the definition of Releasing Parties is clearly and narrowly defined to include only parties that have affirmatively consented to granting releases.

This Court has previously gone to great lengths to explain "just how extraordinary a thing it is for [the Court] to impose involuntarily releases, and why, as commanded by the Second Circuit in [*In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 141-43 (2d Cir. 2005)], [the Court] should do so only in those extraordinary cases where a particular release is essential and integral to the reorganization itself." *In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 726 (Bankr. S.D.N.Y. 2019). This Court has also explained that consent should be affirmatively manifested by the releasing parties, rather than deemed by the Court. *See In re Chassix Holdings, Inc.*, 533 B.R. 64, 78 (Bankr. S.D.N.Y. 2015) (Debtors' proposed procedures found consent "by deeming 'consent' to exist in situations where no affirmative consent had actually been manifested. Finding 'consent' in these circumstances is to some extent a legal fiction.") Through the Proposed Order, the Debtors ask the Court to make a finding that the proposed third party releases are consensual. Proposed Order at ¶ 48 ("The third party releases set forth in section 10.5 of the Plan [. . .] are [. . .] consensual[.]"). Accordingly, the definition of Releasing Parties should be amended to make clear that only parties who have affirmatively manifested their consent are granting releases.

[3] At least two parties have already filed objections in attempts to "opt-out" of this broad third party release to which they do not consent. *See Oracle's Limited Objection and Opt-Out of Third-Party Release of the [Plan] ("Opt-Out")* [ECF No. 850]; *Objection of Beth Desmond to Confirmation of the [Plan] and Approval of the Debtors' Disclosure Statement* [ECF No. 852].

C. The Plan Inappropriately Provides Prospective Releases for Entities that Do Not Yet Exist

The Plan's release provisions provide prospective releases for entities that do not yet exist. Specifically, while they are not included in the definition of "Released Parties," the Wind-Down Debtors, the Plan Administration Trust, and the GUC Recovery Trust all receive broad releases under both the Debtors' release provision and the third party release provision. Plan at §§ 10.4 and 10.5. None of these entities will be established until the Plan's Effective Date. *See* Plan at § 1.124 (defining "Plan Administration Trust"); § 1.93 (defining "GUC Recovery Trust"); 1.185 (defining "Wind-Down Debtors"). The Plan should not grant prospective releases to entities that do not yet exist for conduct that has not yet occurred and of claims that could not yet have arisen. These entities were appropriately excluded from the definition of "Released Parties," and they should be similarly stricken from the Plan's release provisions.

D. The Plan's Exculpation and Limitation of Liability Provision is Overly Broad

Section 10.6 of the Plan provides that a broad list of "Exculpated Parties" shall neither, have, nor incur any liability to any Person or Entity for certain defined "Exculpated Claim[s]," subject to certain carveouts. Plan at § 1.78. Subject to certain carveouts, the Plan defines "Exculpated Claim" to mean:

> [A]ny Cause of Action or any Claim related to any act or omission derived from, based upon, related to, or arising from the Debtors' in- or **out-of-court restructuring efforts and related negotiations**, the Chapter 11 Cases, the formulation, preparation, dissemination, or negotiation of the Disclosure Statement, the Plan (including any term sheets related thereto), the Asset Purchase Agreement, or any contract, instrument, release or other agreement or document (including, for the avoidance of doubt, providing any legal opinion requested by any Entity regarding any transaction, contract, instrument, document, or other agreement contemplated by the Plan or the reliance by any Exculpated Party on the Plan or the Confirmation Order in lieu of such legal opinion) created or entered into in connection with any of the foregoing, including without limitation (i) the Asset

> Purchase Agreement, (ii) the Sale Transaction, (iii) the execution, delivery, and performance of the DIP Credit Agreement, and (iv) the distribution of property under the Plan or any other agreement under the Plan [. . .]

Plan at § 1.78 (emphasis added).

This provision is overly broad. Parties should not receive exculpation or a limitation of their liability in connection with out-of-court restructuring efforts. The exculpation and limitation of liability provision should be expressly limited to the extent permitted by section 1125(e) of the Bankruptcy Code. *See* 11 U.S.C. § 1125(e) (providing for limitation of liability in connection with certain good faith solicitation and plan participation efforts). Alternatively, the exculpation and limitation of liability provision should be limited, as this Court has previously explained, to bar only "claims against the exculpated parties based on the negotiation, execution, and implementation of agreements and transactions that were approved by the Court." *In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 721 (Bankr. S.D.N.Y. 2019).

Additionally, the exculpation and limitation of liability should contain an express carve-out for malpractice claims consistent with Rule 1.8(h) of the New Rules of Professional Conduct, which provides that a lawyer shall not make an agreement prospectively limiting the lawyer's liability to a client for malpractice.

E. The Plan Improperly Treats the Professional Fees and Expenses of Non-Estate Professionals as Allowed Administrative Expense Claims

The Plan improperly treats the professional fees and expenses of certain non-estate professionals as allowed administrative expense claims without demonstrating an entitlement to such treatment under section 503(b) of the Bankruptcy Code. Additionally, by deeming these professional fees and expenses as allowed administrative claims, the Plan forecloses any possible review of the reasonableness of these fees and expenses.

Administrative expenses – generally, expenses incurred after the bankruptcy petition has been filed – receive special payment priority under the Bankruptcy Code. The kinds of expenses that qualify as administrative expenses are listed in section 503(b), and the special treatment given to those expense is established by section 507(a)(2). *In re Lehman Bros. Holdings Inc.*, 508 B.R. 283, 289 (S.D.N.Y. 2014). "The list [in section 503(b)] is meant to be illustrative of the whole universe of administrative expenses." *Id.* Additionally, "the priority status that defines administrative expenses is granted **only** to expenses falling under § 503(b)." *Id.* (citing 11 U.S.C. § 507(a)(2) (granting priority to "administrative expenses allowed under section 503(b)")) (emphasis added). To the extent a plan provision based on a restructuring support agreement or settlement agreement seeks to circumvent section 503(b), the broader business judgment rule for the approval of such provision should not apply. *In re Lehman Bros. Holdings Inc.*, 508 B.R. at 289 (citing *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 132 S. Ct. 2065, 2071 (2012) ("*RadLAX*") ([N]either the need for flexibility, the consensual nature of [such a payment], nor a bankruptcy court's approval of a payment as 'reasonable' can justify a plan provision that is merely a backdoor to administrative expenses [. . .] [T]he federal scheme cannot remain comprehensive if interested parties [. . .] in each case are free to tweak the law to fit their preferences")).

In the instant case, the Plan provides that certain non-estate professional fees and expenses shall constitute Allowed Administrative Claims and receive payment on the Effective Date. Specifically, the professional fees and expenses of the Chatham Parties and the Brigade Parties shall constitute Allowed Administrative Claims under the Plan and shall be paid in full subject to the Professional Fee Caps. Plan at § 2.2. The Plan also provides that the fees and

expenses of counsel to each of the 2027 Debentures Trustee and the 2029 Debentures Trustee shall constitute Allowed Administrative Claims and shall be paid in full in cash on the Effective Date. Plan at § 2.4.

The Plan treats the claims of these unretained professionals as allowed administrative expenses without any of these professionals having established a statutory entitlement to this treatment, such as having made a substantial contribution under the evidentiary requirements of sections 503(b)(3)(D) and 503(b)(4). The plain meaning of the Bankruptcy Code's text is clear and determinative. "**To the extent an expense is not covered by § 503(b), it is not an administrative expense**." *In re Lehman Bros. Holdings Inc.*, 508 B.R. at 289 (citing *Norton Bankruptcy Law and Practice 3d Dictionary of Bankruptcy Terms* § A60 (defining "administrative expenses" solely by reference to § 503(b))) (emphasis added). Section 503(b) controls entitlement to administrative expense priority, not the Debtors' business judgment under section 363 or Bankruptcy Rule 9019.[4] The "general language of a [Bankruptcy Code] statutory provision, although broad enough to include it, will not be held to apply to a matter specifically dealt with in another part of the same enactment." *RadLAX*, 132 S. Ct. at 2071 (internal quotation, citation, and modification omitted). This rule "is particularly true where [. . .] Congress has enacted a comprehensive scheme and has deliberately targeted specific problems with specific solutions." *Id.* (internal quotation and citation omitted). Here, unless the non-estate professionals demonstrate a statutory entitlement to administrative expense treatment under one of the enumerated subsections of section 503(b), they cannot be treated as allowed administrative

[4] The United States Trustee recognizes that Courts in this district have, at times, approved the payment of professional fees and expenses pursuant to section 363(b) of the Bankruptcy Code and/or Bankruptcy Rule 9019. *See, e.g.*, *In re Stearns Holdings, LLC*, 607 B.R. 781, 792 (Bankr. S.D.N.Y. 2019). The United States Trustee respectfully disagrees that such authorization is permitted for the reasons set forth herein.

claims under the Plan. To the extent the parties may believe there is an independent basis for this priority treatment – such as in the case of the indenture trustees – that basis needs to be clearly articulated and established.

Finally, the Plan's attempt to deem these fees and expenses as Allowed Administrative Claims is also problematic because it precludes any review of the reasonableness of these fees and expenses by the Court. The Court has an independent burden to review fee applications and serves a vitally important gate-keeping role in (i) enforcing the Bankruptcy Code's requirements that only reasonable fees be approved and paid and (ii) maintaining public confidence in the bankruptcy system itself. *In re Temple Ret. Cmty., Inc.*, 97 B.R. 333, 337 (Bankr. W.D. Tex. 1989); *see also In re Child World, Inc.*, 185 B.R. 14, 17 (Bankr. S.D.N.Y. 1995) ("the judiciary should retain control of fees, given the sensitivities they generate and the need to promote public confidence in the system."). Had the parties filed applications pursuant to sections 503(b)(3)(D) and 503(b)(4), the fees would be subject to a reasonableness review. Here, no such review is possible.

For these reasons, the Plan cannot be confirmed to the extent it treats the professional fee and expense claims of non-estate professionals as allowed administrative expense claims.

F. The Plan Does Not Expressly Provide for the Filing of Post-Confirmation Operating Reports

The Plan fails to provide for the filing of post-confirmation operating reports until the case is closed, dismissed, or converted. The United States Trustee has provided proposed standard language to the Debtors regarding the filing of post-confirmation operating reports and the payment of statutory fees and any applicable statutory interest thereon. The United States Trustee expects to resolve this issue consensually, but he raises it in the instant Objection out of an abundance of caution.

CONCLUSION

For the foregoing reasons, the United States Trustee respectfully requests that the Court deny confirmation of the Plan absent modification to address the concerns raised herein, and grant such other relief as is just and proper.

Dated: New York, New York
September 18, 2020

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