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THE BANKRUPTCY STRATEGIST

# Landmines In Bankruptcy Appellate Practice

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Pundits are raving about the current increase in business bankruptcy cases. But they rarely, if ever, mention the spike in bankruptcy appeals. A brief survey of recent decisions shows that appellate courts are, among other things, finding ways to (a) avoid making decisions or to (b) avoid litigation delay and uncertainty by expediting appellate review. Practitioners can avoid surprises by grasping what these courts are actually doing.

The recent decisions summarized below show how a simple reading of the Bankruptcy Rules and the Judicial Code will provide only limited guidance. Recent case law, summarized below, often undermines some of the accepted maxims recited in bankruptcy appellate practice. Stays pending appeal; appellate standing; timeliness; leave to appeal; direct appeals from the bankruptcy court to the Court of Appeals; appellate jurisdiction; appeals from fee awards; and appeals from arbitration are all addressed in a series of articles over the next few months.

## Maxim 1: A Stay Pending Appeal Is Hard to Get

### *Stay Pending Appeal from Confirmation Order*

The Second Circuit summarily denied a Chapter 11 debtor's motion to vacate the district court's stay of a plan confirmation order pending appeal. *In re Voyager Digital Holdings, Inc.*, 2023 WL 4310688 (2d Cir. Apr. 11, 2023). According to the court, it lacked jurisdiction because "the stay is neither a final order" under 28 U.S.C. §158(d) "nor sufficiently like an injunction" under 28 U.S.C. § 1291(a)(1). The stay here, said the court, "also does not meet the requirements of the 'collateral order' doctrine." In addition, because the debtor and creditors' committee failed "to show that the district court usurped power or clearly abused its discretion," the court denied their petition for a writ of mandamus. The Second Circuit once again found a way to avoid a decision.

The district court had earlier granted the emergency motion of the United States and the United States Trustee (collectively, the "Government") for a stay pending appeal of a bankruptcy court's plan confirmation order. *In re Voyager Digital Holdings, Inc.*, 2023 WL 2731737 (S.D.N.Y. Apr. 1, 2023). According to that court, a "stay is warranted because the Government has demonstrated a substantial case on the merits and irreparable harm in the absence of a stay." *Id*. at *7. The Government had challenged the scope of exculpation provision in the plan that would "prospectively immunize debtors and non-debtors from law enforcement and other actions undertaken by the Government." Rejecting the position of the debtor and creditors' committee, the court explained that the rationale for exculpation provisions in reorganization plans did not apply "to exculpation from Government enforcement of the law following confirmation." *Id*. at *8.

Neither the debtor nor the committee rebutted the Government's argument that "an Article I bankruptcy court lacks any power over criminal matters." Nor did the debtor and the Committee rebut "the proposition that immunity must be raised as an affirmative defense, rather than granted preemptively before any action has even taken place." *Id*. at *9. "Using generic equity principles to enjoin a future criminal prosecution violates 'the general rule that equity will not interfere with the criminal processes, by entertaining actions for injunction or declaratory relief in advance of

criminal prosecution." *Id*., quoting *Zemel v. Rusk*, 381 U.S. (1) (1965).

The Government had objected to a provision in the plan, as modified, that exculpated certain parties "from … any claim for fines, penalties, damages or other liabilities based on their execution and completion of the … transactions and the distribution … to creditors in the … Plan." *Id*. at *5. The bankruptcy court stressed that "no regulatory authority has taken the position during [court hearings] that such conduct would violate applicable laws or regulations." According to that court, the Government had "sat on the sidelines and said nothing … to indicate that there is anything illegal about what [the parties] are going to do …." Not only did the bankruptcy court disagree with the Government, but said that "the very suggestion offends me to no end. I can't believe that you would even take the position in front of me that you should have that right. It's preposterous …. If you think something's that illegal, speak up, but don't dare tell me that you kind of want to reserve that right to do that to somebody." *Id*., at *4 n. 4. In short, the bankruptcy court approved "an Exculpation Provision insulating Debtors and others from prospective governmental liability in … their consummation of the transactions contemplated in the Plan and related documents." *Id*. at *4. But, held the district court, the Government made out a "substantial case on the merits" that weighed in favor of a stay. *Id*. at *9, quoting *Ctr. For Int'l Env't L. v. Off. of U.S. Trade Representative*, 240 F. Supp. 2d 21, 21-24 (D.D.C. 2003).

The court also addressed the issues of injury to the parties and the public interest. "[W]hile all parties would face meaningful injury in the event that a stay were wrongly granted or denied, the balance of hardship lies with the Government …. [A] harm to the public interest … satisfies" at least two requirements for a stay. "[A] stay pending appeal would preserve the Government's — and the public's — right to meaningful appellate review of the Exculpation Provision and the significant issues raised here …." *Id*. at *10. The court also wanted to avoid having the Government's appeal mooted — "a reality that 'even the [debtor] and the Committee acknowledge.'" *Id*., quoting *In re Klein Sleep Prod., Inc.*, 1994 WL 652459, at *1 (S.D.N.Y. Nov. 18, 1994).

***No Stay Pending Appeal***

The district court denied a motion for a stay pending appeal because the appellant failed to carry "its burden for obtaining a stay under [Bankruptcy] Rule 8025 …." *In re Roman Catholic Church of Archdiocese of New Orleans*, 2023 WL 5479132 (E.D. La. Aug. 24, 2023). Even if the appeal raised a "serious" legal question showing a substantial likelihood of success on the merits, which the district court doubted, the appellant had "not demonstrated the requisite degree of irreparable harm since litigation expenses typically do not satisfy this factor, and it [had] not established that a stay poses no substantial harm to others …, or serves the public interest." *See also, In re Arcapita Bank B.S.C. (c)*, 2023 WL 3558243 (S.D.N.Y. May 18, 2023) (district court denied stay pending appeal from bankruptcy court's contempt order because appellant "failed to make a strong showing that it is likely to succeed on merits[,] … failed to demonstrate it would suffer irreparable harm absent a stay, … [failed to show] that the [appellee]" creditors' committee "will not suffer substantial harm if the stay is granted," and because "the public interest weighs in favor of the expedient and sound administration of" bankruptcy cases.).

**Maxim 2. The Losing Party Can Always Appeal**

***Person-Aggrieved Standard Foreclosed Appeal***

Because the appellants had not asked the Court of Appeals "to abrogate the person-aggrieved test" for appellate standing, they "forfeited any challenge to the doctrine", held the Sixth Circuit, and dismissed their appeal. *In re Schubert*, 2023 WL 2663257 (6th Cir. Mar. 28, 2023). The lender appellants had appealed from a bankruptcy court order directing the debtors' bankruptcy estate to abandon a breach-of-contract claim against the lenders. The lenders had sought an order in the bankruptcy court declaring that the debtors' claim against them had "belonged to the estate," not to the debtors, and sought to enjoin the debtors from pursuing state court litigation. The bankruptcy court ruled that the debtors' claim belonged to the estate and ordered the bankruptcy trustee to abandon the debtors' claim but denied injunctive relief. Although the court agreed that the lenders had standing to appeal, they still failed the so-called person-aggrieved test, which permits a party to appeal "only if the appeal's result will put money in the party's pocket or compel it to write a check." *Id*. at *2. The court doubted that the "person aggrieved" doctrine survived enactment of the Bankruptcy Code, but still declined to hear the appeal because the parties neither presented nor briefed the issue. Moreover, the lenders lacked a "direct financial stake in the appeal's outcome" because "the threat of litigation" does not give a party the requisite interest to appeal. *Id*. at *3. *See also*, *In re Highland Capital Management, L.P.*, 2023 WL 4621466 (5th Cir. July 19, 2023) (the 'person aggrieved' test continues to govern

standing in bankruptcy [appeals]."; appellant's status as purported administrative claimant did not give it standing because bankruptcy court had disallowed its administrative expense claim; appellant's status as defendant in an adversary proceeding "fares no better" because there was no judgment against it and "speculative prospect of harm is far from a direct, adverse, pecuniary hit;" and Supreme Court never overruled "person aggrieved" test for appellant standing.).

***No Article III Standing to Appeal***

The Ninth Circuit reversed a district court's order affirming a fee award to a trustee because the appellant, an unsecured creditor, lacked "an injury in fact" and thus lacked "Article III standing." *In re East Coast Foods, Inc.*, 2023 WL 5965812 (9th Cir. Sept. 14, 2023) (amended). In short, the appellant creditor "failed to show that [an] enhanced fee award [to the trustee in the case] will diminish its payment under the bankruptcy plan …." *Id*. at *2.

The Chapter 11 plan here provided for hourly compensation to the trustee plus expenses. It also "guaranteed the creditors full payment with interest" secured by collateral consisting of all of the debtor's assets and a $10 million contribution from the debtor's principal. *Id*. at *2.

The trustee had requested not only his hourly-based fees, but also a "65% enhancement for exceptional services." *Id*. at *3. The total amount represented "the maximum allowable under the fee cap statute, 11 U.S.C. §326(a)."

The bankruptcy court rejected the creditor's objection, holding "that the fee cap was presumptively reasonable and, in the alternative, that the case was exceptional and merited deviation from the lodestar." *Id*. After subsequent appeals, the bankruptcy court reiterated its holding and was affirmed by the district court.

The Ninth Circuit first addressed the appellant creditor's Article III standing because "the Constitution limits our jurisdiction to 'cases' and 'controversies.'" *Id*. at *3. Although earlier bankruptcy cases "historically addressed prudential standing with little attention to Article III standing," the Ninth Circuit "first examine[d] Article III standing." *Id*. at *4. The appellant here had to show that it had "(1) suffered an 'injury in fact' that is concrete, particularized, and actual or imminent, (2) the injury is 'fairly traceable' to the defendant's conduct, and (3) the injury can be 'redressed by a favorable decision'." *Id*. at *4, quoting *Lujan v. Defs. of Wildlife*, 504 U.S. 555, 561 (1992).

The "Plan here does not relate to a limited fund because there is no finite amount of assets from which all creditors could be paid." *Id*. at *6. Instead, the plan proposed to pay all creditors in full from the debtor's ongoing operations and other sources. The creditor appellant "understood these terms" and that the "promise of full payment with interest [was] unconditionally guaranteed and secured by a 'Collateral Package', which includes all of the [the debtor's] assets." Additional funds were also available from other persons and entities.

The court further rejected the creditor's argument that the timing of payment harmed it. According to the court, the creditor's "alleged harms are thus conjectural at best." Not only did the creditor consent to the plan, but the creditor also "failed to establish that the timing of its payment has been harmed beyond what the Plan initially provided." The plan never even guaranteed payment by a specific date, and the creditor "is entitled to interest on the payments that are due." *Id*. at *7.

The plan further anticipated payment of the creditor's claims "even if the trustee received the challenged bonus …. [T]he availability of additional funds to satisfy [the creditor's] claims foreclose standing." Because standing "must exist from the start of an action", the creditor "failed to establish actual injury … and therefore lacks Article III standing to challenge the Fee Award." *Id*.

*The next installment in this series will cover timeliness of appeals, leave to appeal and direct appeals.*

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