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Alert

Third Circuit Clarifies Appeal Process in Settlement and Reorganization Plan Disputes

July 3, 2019

The Third Circuit recently took a "pragmatic approach" when affirming lower court orders denying a stay of bankruptcy settlement distributions pending appeal. *In re S.S. Body Armor I, Inc.*, 2019 WL 2588533 (3d Cir. June 25, 2019). After holding that the district court's "stay denial order" was "final" for jurisdictional purposes, it also confirmed "the applicable standard of review" on motions for stays pending appeals.

Relevance

The Third Circuit's jurisdictional ruling was timely. First, the Circuit had "no direct precedent on the finality of the" order before it. Second, the U.S. Supreme Court recently granted certiorari in *Ritzen Group, Inc. v. Jackson Masonry, LLC*, 2019 WL 266853 (May 20, 2019), agreeing to address whether an order denying relief from the automatic stay is "final" under the bankruptcy appeals statute, 28 U.S.C. § 158(a)(i). The Sixth Circuit had held in *Jackson* that an order denying stay relief was "final," rejecting "vague" and "unpredictable" tests adopted by other circuits. 906 F.3d 494, 498 (6th Cir. 2018), citing *In re Atlas IT Export Corp.*, 761 F.3d 177, 185 (1st Cir. 2014)("Everything depends on the circumstances …").

A party appealing from a bankruptcy court's approval of a settlement or confirmation of a reorganization plan must ordinarily seek a stay pending appeal. Otherwise, as the Third Circuit noted in *Body Armor*, if the "settlement proceeds are distributed before resolution of" the appeal, "that appeal is 'all but assured' to become moot." *Id.* at *3, quoting *In re Revel AC, Inc.*, 802 F.3d 558, 567 (3d Cir. 2015).

Bankruptcy Code ("Code") § 363(m) provides that, absent a stay pending appeal, the reversal or modification on appeal of a bankruptcy sale order does not affect the validity of sale to a good faith purchaser. Code § 364(e) provides for the same result with a bankruptcy financing order. Drawing on these statutory mandates by analogy, courts have dismissed appeals from non-sale and non-financing orders as equitably moot when the appellant's failure to obtain a stay pending appeal rendered the appellate court unable to fashion a remedy that would restore the interested parties to their former position. *See*, *e.g.*, *In re JMC Memphis, LLC*, 655 F. App'x 802, 805 (11th Cir. 2016) (due to party's failure to request a stay from either bankruptcy court or district court, court found it inappropriate to "unwind select portions of the settlement agreement."); *In re Allied Nev. Gold Corp.*, 725 F. App'x 144, 148 (3d Cir. 2018) (appeal from plan confirmation order dismissed as "equitably moot" when appellants sought to unscramble complex reorganization plan; appellants "did not timely seek or obtain a stay."); *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 143-45 (2d Cir. 2005) (appeal of plan confirmation order dismissed as equitably moot when appellants never sought stay pending appeal or expedited review; vacatur of confirmation order could potentially unsettle substantially consummated plan). As shown below, the creditor in *Body Armor* appealed from the amount of the reserve to be set aside from which

its legal fees could be paid. Because the order in question was neither an asset sale nor a financing order, statutory mootness was not relevant, but equitable mootness was.

Facts

The appealing creditor in *Body Armor*, "C," was a law firm that had obtained a large cash settlement for the debtor's estate. It had filed a fee application seeking $1.86 million but then later asked the bankruptcy court to set aside a $25-million reserve from which its fees could be paid. "Without determining the exact amount of attorney's fees owed to [C], the Bankruptcy Court granted the motion in part, ordering Debtor to set aside $5 million from any settlement funds until resolution of [C's] fee application." *Id.* at *2. Because it thought the $5-million reserve "to be insufficient," C appealed and also asked the bankruptcy court to stay any distributions from the settlement proceeds pending its appeal. Both the bankruptcy and district courts denied a stay pending appeal.

The Third Circuit

Appellate Jurisdiction. The court held that it had "jurisdiction to hear this appeal" under 28 U.S.C. § 158(d) ("final" order required). As noted, because the lower court's stay denial order "all but assured" that C's fee reserve appeal would become moot "since it opened the door to immediate settlement distributions," that result would preclude C "from obtaining a full airing of its issues on appeal." Therefore, the order appealed from the district court "was final, [as] was the Bankruptcy Court's order." *Id.* at *4-5. *See Jackson Masonry*, 906 F.3d at 502 ("The more significant and unrepairable the consequences, the more likely a given order really is final …. [I]n ordinary litigation parties generally can only appeal once the entire case is complete and all issues have been resolved, but in bankruptcy, parties can appeal discrete disputes within the overall case …. We decline to …. ignore the longstanding and textually-compelled rule of looser finality in bankruptcy."), citing *Bullard v. Blue Hills Bank*, 135 S. Ct. 1686, 1696 (2015) (finality of bankruptcy order determined "first and foremost" by whether it "alters the status quo and fixes the rights and obligations of the parties.").

Judicial Requirements for Stay. Fed. R. Bankr. P. 8007 allows a party to move for a stay pending appeal. The judicially established criteria for ruling on these motions are like those for preliminary injunctions: "(1) whether the stay applicant has made a strong showing that [it] is likely to succeed on the merits; (2) whether the applicant will be irreparably injured absent a stay; (3) whether issuance of the stay will substantially injure the other parties interested in the proceedings; and (4) where the public interest lies."

Hilton v. Braunskill, 481 U.S. 770, 776 (1987). According to the Supreme Court, the first two criteria are "the most critical." *Nken v. Holder*, 556 U.S. 418, 434 (2009). *Accord*, *Revel*, 802 F.3d at 568 (strong showing of likelihood of success and irreparable harm). A "likelihood of success 'is arguably the more important piece of the stay analysis.'" *Id*. In *Revel*, the Third Circuit adopted a "sliding-scale" approach to determine how strong a case the appellant must show: "[t]he more likely the [movant] is to win, the less heavily need the balance of harms weigh in [its] favor; the less likely [it] is to win, the more [heavily] need [the balance of harms] weigh in [its] favor." *Revel*, 802 F.3d at 569.

Standard of Review. The Court of Appeals ordinarily reviews the denial of a stay "for abuse of discretion, giving proper regard to the district court's feel of the case." *Id*. at 567. Because the likelihood of success criterion turns on "a purely legal determination," though, the court reviewed the district court's ruling de novo. *Body Armor*, 2019 WL 2588533, at * 6, citing *Revel*, 802 F.3d at 567.

The Merits. The Third Circuit found that C had "a fatally low likelihood of succeeding in its Fee Reserve Appeal," compelling an affirmance of the district court's denial of the stay, "even without considering any of the remaining stay factors." *Id.* Applying the so-called "lodestar" method for calculating C's requested fees to determine whether the $5-million reserve was adequate to cover C's fee request, the bankruptcy court, said the Third Circuit, had found "a very low likelihood of [C's] receiving a fee award in excess of $5 million." *Id*. at *8. Moreover, the district court found that the bankruptcy court had not abused its discretion.

The Court of Appeals thus found that "the $5 million reserve was sufficient" because an award in that amount "for 1502.2 hours of legal work" would "yield an hourly rate of $3,328.45 and a lodestar multiplier of over 9." *Id.* As the court noted, C "showed tremendous skill and expended substantial time in preserving a highly valuable claim. But its attempts to argue that it is somehow due attorneys' fees more than $5 million are belied by its initial fee application in the bankruptcy court," where it "sought attorney's fees totaling $1.86 million using a lodestar multiplier of 3.38," asserting its request was reasonable.

The Third Circuit was "confident that a $5 million reserve [was] sufficient to award [C] the attorneys' fees it is due." *Id.* Without further analysis, it affirmed the denial of a stay because C had "not carried its burden of demonstrating that it has a 'significantly better than negligible' chance of succeeding on the merits of its pending Fee Reserve Appeal." *Id*. at *8, quoting *Revel*, 802 F.3d at 57.

Comments

1. The *Body Armor* jurisdictional holding on the finality of bankruptcy court orders is noteworthy. Consistent with the Sixth Circuit's *Jackson Masonry* decision, it suggests how the Supreme Court will resolve a circuit split next term in that case: finality will turn on whether the order "finally dispose[s] of discrete disputes within the larger case." *Bullard*, 135 S. Ct. at 1692 (quoting *Howard Delivery Serv., Inc. v. Zurich Am. Ins. Co.*, 547 U.S. 651, 657n.3 (2006).

2. *Body Armor* is also consistent with the many decisions denying a stay pending appeal because of the applicable stringent requirements. But the court's heavy reliance on its earlier *Revel* decision shows that an appellant can obtain a stay by making a strong record. As the court there held when granting a stay and reversing the lower courts' denial, "that [appellant] would prevail on the merits was all but assured …. [Appellant further] demonstrated that, absent a stay, it would lose its … business …, and this was sufficient to show irreparable harm."). *Revel*, 802 F.3d at 575.

3. The appellant in *Body Armor* alternatively relied on 28 U.S.C. § 1292(a)(i) (courts of appeals may hear appeals from interlocutory orders "refusing … injunctions") to support appellate jurisdiction, but the Third Circuit relied instead on the bankruptcy appeals statute, 28 U.S.C. § 158(a). It declined to "reach" § 1292(a)(i). The dissenting judge in *Revel*, though, would have "reach[ed]" the jurisdiction issue under § 1292(a)(i) to uphold jurisdiction under that statute. *Revel*, 802 F.3d at 575n.2.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or the author.

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