Bankruptcy ADVISORY ■

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Seven Factors and Good Faith: The Eleventh Circuit Clarifies Bankruptcy Courts' Authority

The Eleventh Circuit's recent opinion in *SE Property Holdings, LLC v. Seaside Engineering & Surveying, Inc. (In re Seaside Engineering & Surveying, Inc.)*, No. 14-11590 (11th Cir. March 12, 2015), clarifies the circuit's stance on the authority of bankruptcy courts to issue nonconsensual, non-debtor releases or bar orders and the circumstances under which such bar orders might be appropriate. In addition, the court gave a broad reading of what it means for a plan to have been proposed in good faith.

Non-debtor Releases or Bar Orders

The court acknowledged that "[o]ther circuits are split as to whether a bankruptcy court has the authority to issue a non-debtor release and enjoin a non-consenting party who has participated fully in the bankruptcy proceedings but who has objected to the non-debtor release barring it from making claims against the non-debtor that would undermine the operations of the reorganized entity."

The Eleventh Circuit then concluded that its own precedent, along with its survey of the other circuits' rationales and its own reading of Sections 524(e) and 105(a) of the Bankruptcy Code, placed it with the majority of circuits that permits non-debtor releases. The court cautioned:

> …that such bar orders ought not to be issued lightly, and should be reserved for those unusual cases in which such an order is necessary for the success of the reorganization, and only in situations in which such an order is fair and equitable under all the facts and circumstances. The inquiry is fact intensive in the extreme.

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The Sixth Circuit's seven factor test from *In re Dow Corning Corp.* (280 F.3d 648, 658 (6th Cir. 2002)) was endorsed as a guide for bankruptcy courts to consider. The seven factor test, as approved by the Eleventh Circuit, is as follows:

1. There is an identity of interests between the debtor and the third party, usually an indemnity relationship, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete the assets of the estate;
2. The non-debtor has contributed substantial assets to the reorganization;
3. The injunction is essential to reorganization, namely, the reorganization hinges on the debtor being free from indirect suits against parties who would have indemnity or contribution claims against the debtor;
4. The impacted class, or classes, has overwhelmingly voted to accept the plan;
5. The plan provides a mechanism to pay for all, or substantially all, of the class or classes affected by the injunction;
6. The plan provides an opportunity for those claimants who choose not to settle to recover in full and;
7. The bankruptcy court made a record of specific factual findings that support its conclusions.

Good Faith Proposal of a Plan

The court also addressed one of the requirements that must be met in order to confirm a plan—that it has been "proposed in good faith." Previously, the court had ruled that this requires "that there is a reasonable likelihood that the plan will achieve a result consistent with the objectives and purposes of the Code." *In re McCormick*, 49 F.3d 1524, 1526 (11th Cir. 1995).

In *SE Property Holdings*, the court elaborated on those objectives and purposes, permitting courts to consider more than just strict economic returns to creditors, stating:

> Those purposes include preserving jobs in the community, allowing the business to continue to operate instead of liquidation, and achieving a consensual resolution between debtors and creditors. ... "Bad faith exists if there is no realistic possibility of reorganization and the debtor seeks merely to delay or frustrate efforts of secured creditors."
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> The Reorganization Plan benefits more than just the Seaside insiders. [N]on-shareholder employees will maintain their jobs; other creditors will receive compensation over time; and [a customer] will continue to receive engineering services. The Plan falls well within the purposes of the Bankruptcy Code and is therefore proposed in good faith. Simply because one creditor is dissatisfied is insufficient to show bad faith.

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