

# AMERICAN BANKRUPTCY INSTITUTE JOURNAL

The Essential Resource for Today's Busy Insolvency Professional

## Feature

BY MARK M. MALONEY AND THADDEUS D. WILSON<sup>1</sup>

### Misguided Travelers

#### The First Circuit's Divergent Decision on Post-Sale Jurisdiction



**Mark M. Maloney**  
King & Spalding LLP  
Atlanta



**Thaddeus D. Wilson**  
King & Spalding LLP  
Atlanta

Mark Maloney is a partner and Thad Wilson is a senior associate in King & Spalding LLP's Financial Restructuring Practice in Atlanta. Mr. Maloney is also a member of ABI's Board of Directors.

The constraints of bankruptcy court jurisdiction have been hotly contested in recent years, with three cases reaching the U.S. Supreme Court.<sup>2</sup> Bankruptcy-related jurisdiction fights have recently erupted in the context of orders approving § 363 sales, particularly over the limits of post-sale jurisdiction. Given the increased frequency of § 363 sales in bankruptcy cases, the breadth of post-sale bankruptcy jurisdiction will continue to be litigated and will have important ramifications for all affected parties.

In particular, a recent decision by the U.S. Court of Appeals for the First Circuit, *Gupta v. Quincy Med. Ctr.*,<sup>3</sup> deviated from the Supreme Court's precedent in *Travelers Indem. Co. v. Bailey*<sup>4</sup> to conclude that a bankruptcy court lacks jurisdiction to enforce its sale order. The decision contained an express approval of the terms of the underlying sale agreement and a broad "retention-of-jurisdiction" provision. This article first summarizes the decision, argues that the First Circuit erred in its analysis and highlights *Gupta*'s potential impacts regarding jurisdictional disputes arising from other common bankruptcy court orders.

### The Decision

In *Gupta*, the First Circuit analyzed the scope of a bankruptcy court's post-sale jurisdiction. The question at issue was whether a buyer owed severance under the sale agreement to employees who were terminated post-closing.<sup>5</sup> In the sale agreement, the buyer "agreed to offer employment for a period of no less than three months to each employ-

ee of [the seller] as of the date of the sale closing at the salary and position enjoyed by such employee prior thereto[, and] in the event [that the buyer] terminated any former employee, [the buyer] agreed to honor any severance obligation based on [the seller's] severance policy."<sup>6</sup>

The bankruptcy court approved a 29-page sale order that contained provisions approving the terms and conditions of the underlying sale agreement. Indeed, the sale order expressly stated, "The sale of the Assets to [the buyer] pursuant to the [sale agreement] is authorized under Section 363(b) and (d)(1) of the Bankruptcy Code. The [sale agreement] is approved."<sup>7</sup> Among other pertinent provisions, the sale agreement stated:

The terms and provisions of the [sale agreement], together with the terms and conditions of this Order, shall be binding in all respects upon all entities, including, without limitation, the [debtor,] all creditors and equity interest holders of the [debtor], [the buyer], and their respective affiliates, successors and assigns, agents and any affected third parties, including, but not limited to, all persons asserting a claim against or interest in any of the Assets to be sold, conveyed or assigned to [the buyer] pursuant to the [sale agreement].<sup>8</sup>

The sale order also contained a common retention-of-jurisdiction clause,<sup>9</sup> which stated that the court retained jurisdiction to:

(a) interpret and enforce the provisions of the APA, the Assigned Agreements, the Sale Motion and this Order; (b) protect [the purchaser] and any of the Assets against any

<sup>1</sup> The opinions expressed herein are those of the authors only and do not represent the opinions of King & Spalding LLP or its clients.

<sup>2</sup> See, e.g., *Wellness Int'l Network Ltd. v. Sharif*, 135 S. Ct. 1932 (2015); *Exec. Benefits Ins. Agency v. Arkison* (*In re Bellingham Ins. Agency Inc.*), 134 S. Ct. 2165 (2014); *Stern v. Marshall*, 564 U.S. 462 (2011).

<sup>3</sup> Case No. 15-1183, 2017 U.S. App. LEXIS 9814, 858 F.3d 657 (1st Cir. 2017).

<sup>4</sup> 557 U.S. 137 (2009).

<sup>5</sup> *Id.* at \*1.

<sup>6</sup> *In re Quincy Med. Ctr. Inc.*, 466 B.R. 26, 28 (Bankr. D. Mass. 2012).

<sup>7</sup> *Id.* at ¶ 4.

<sup>8</sup> *In re Quincy Med. Ctr. Inc.*, Case No. 11-16394, Dkt. 339 at ¶ 30 (Bankr. D. Mass. Sept. 26, 2011).

<sup>9</sup> *Id.* at \*3.

Lien or Claim; (c) resolve any disputes arising under or relating to the APA, the Assigned Agreements, the Sale Motion and this Order; and (d) determine the validity, extent and priority of asserted pre-Closing Liens or Claims on, and the disposition of the gross proceeds of sale of, the Assets.<sup>10</sup>

Shortly after closing its acquisition of the hospital, the buyer failed to offer two senior executives employment and refused to pay them severance.<sup>11</sup> The employees brought a lawsuit in bankruptcy court, seeking enforcement of the sale agreement and order.<sup>12</sup> Citing *Travelers*, the bankruptcy court determined that it had the jurisdiction “to interpret and enforce its own prior orders,” including the sale order that was binding on the buyer and employees.<sup>13</sup> Because the sale agreement clearly provided that the seller assumed the employee-severance obligations, the bankruptcy court ruled in the former employees’ favor.<sup>14</sup>

On appeal, the district court reversed, holding that the bankruptcy court lacked subject-matter jurisdiction.<sup>15</sup> The First Circuit agreed.<sup>16</sup>

Notwithstanding the provisions of the sale order and sale agreement, including retention-of-jurisdiction language in the sale order, the First Circuit — with retired Supreme Court Justice David Souter on the panel — held that the bankruptcy court lacked “arising-in” jurisdiction to consider the dispute.<sup>17</sup> Thus, the parties were required to litigate their dispute outside of bankruptcy court.<sup>18</sup>

On appeal, the executives argued that the bankruptcy court had subject-matter jurisdiction as a result of the sale order and the retention-of-jurisdiction language contained therein.<sup>19</sup> Applying the bankruptcy jurisdiction statute,<sup>20</sup> the First Circuit analyzed whether the bankruptcy court had one of the three bases of bankruptcy jurisdiction: “related to,” “arising under” or “arising in.” The court initially determined that no related-to jurisdiction existed because the executives lacked claims against the debtor and there was not a conceivable effect on the debtor’s bankruptcy estate.<sup>21</sup> The court also held that no arising-under jurisdiction existed because the executives’ claims did not arise under the Bankruptcy Code.<sup>22</sup>

As for arising-in jurisdiction, the court analyzed whether the executives’ claims “could arise only in the context of a bankruptcy case.”<sup>23</sup> Because the claims “look[ed] like ones that could have arisen entirely outside of the bankruptcy context,” the bankruptcy court did not have arising-in jurisdiction.<sup>24</sup> In other words, if the bankruptcy court need only conduct “a state law breach-of-contract analysis,” no arising-in jurisdiction exists.<sup>25</sup>

## The First Circuit Disregards *Travelers*

The First Circuit’s decision is troubling for several reasons. First, while the First Circuit cited the Supreme Court’s decision in *Travelers* — which then-Justice Souter authored — it effectively ignored the underlying reasoning. In *Travelers*, the Second Circuit held that the bankruptcy court’s enforcement of its prior orders could not “enjoin claims over which it had no jurisdiction,”<sup>26</sup> and “[t]he ancillary jurisdiction [that] courts possess to enforce their own orders is itself limited by the jurisdictional limits of the order sought to be enforced.”<sup>27</sup> The Supreme Court unequivocally held that the Second Circuit erred.

The Supreme Court said that it was “easy” to determine that the bankruptcy court “had jurisdiction to interpret and enforce its own prior orders” and had “explicitly retained jurisdiction” in order to enforce those prior orders.<sup>28</sup> It was erroneous for the Second Circuit to re-evaluate the bankruptcy court’s jurisdiction to enter the original orders once the orders became “final.”<sup>29</sup> As the Court explained, the orders “became *res judicata* to the parties and those in privity with them,” even as to subject-matter jurisdiction.<sup>30</sup> Thus, “[s]o long as [the parties seeking to invoke the court’s jurisdiction] or those in privity with them were parties to the [original] proceeding, and were given a fair chance to challenge the Bankruptcy Court’s subject-matter jurisdiction, they cannot challenge it now by resisting enforcement of the [prior orders].”<sup>31</sup>

In *Gupta*, the First Circuit apparently disregarded the fact that the sale order was a “final” order that was never appealed by the buyer — the party fighting the bankruptcy court’s post-sale jurisdiction. Indeed, the buyer agreed to the retention-of-jurisdiction provision in the sale order — and the order, per paragraph 30, stated that the terms and conditions of the sale agreement were binding on “all entities,” including the buyer (which had expressly agreed to hire the employees and/or pay their severances). Accordingly, under *Travelers*, the First Circuit erred when it re-evaluated whether the bankruptcy court had jurisdiction to enforce its sale order. Under *Travelers*, that issue was *res judicata*.<sup>32</sup>

The First Circuit also appeared to ignore numerous paragraphs in the sale order. By disregarding paragraph 30 and other provisions of the sale order approving the sale agreement, the First Circuit essentially wrote those paragraphs out of the order.

In addition to these flaws, the First Circuit’s *Gupta* decision runs afoul of long-standing, established precedent from other jurisdictions. For example, bankruptcy courts have subject-matter jurisdiction to enforce their sale orders in disputes concerning alleged “successor-liability” claims.<sup>33</sup>

10 *Quincy Med. Ctr.*, 2017 U.S. App. LEXIS 9814 at \*4.

11 *Id.* at \*4-5.

12 *Id.* at \*5.

13 See *Quincy Med. Ctr.*, 466 B.R. at 32.

14 See *In re Quincy Med. Ctr. Inc.*, 479 B.R. 229, 237 (Bankr. D. Mass. 2012).

15 See *Quincy Med. Ctr. v. Gupta*, Case No. 12-40128-RWZ, 2015 WL 58633, at \*1, \*6 (D. Mass. Jan. 5, 2015).

16 See *Quincy Med. Ctr.*, 2017 U.S. App. LEXIS 9814 at \*15-16.

17 *Id.* at \*16.

18 *Id.* at \*15.

19 *Id.* at \*12-13.

20 28 U.S.C. § 1334(b).

21 *Id.* at \*12. The *Gupta* employees stipulated in their briefs that the bankruptcy court did not have related-to jurisdiction. See *Quincy Med. Ctr.*, 2017 U.S. App. LEXIS 9814 at \*12. However, the overarching issue was whether the debtor/seller or the buyer was liable for the payment — thus, potentially affecting the bankruptcy estate, both in potential liability and the incurrence of related fees and expenses. *Quincy Med. Ctr.*, 466 B.R. at 32. Therefore, it would seem that related-to jurisdiction might have existed.

22 *Id.* at \*12.

23 *Id.* at \*13.

24 *Id.* at \*15-16.

25 *Id.* at \*15.

26 *In re Johns-Manville Corp.*, 517 F.3d 52, 61 (2d Cir. 2008).

27 *Id.* at 65, n.22 (internal quotation marks omitted).

28 *Travelers*, 557 U.S. at 151.

29 *Id.* at 152.

30 *Id.* (internal quotation marks omitted).

31 *Id.* at 153.

32 *Id.* at 152.

33 See, e.g., *In re Allegheny Health, Educ. & Research Found.*, 383 F.3d 169, 175-76 (3d Cir. 2004) (bankruptcy court had jurisdiction to consider “core proceeding” that required court “to interpret and give effect to its previous sale orders”); *Luan Inv. S.E. v. Franklin 145 Corp.* (*In re Petrie Retail Inc.*), 304 F.3d 223 (2d Cir. 2002) (bankruptcy court had jurisdiction to enforce sale order against party seeking to recover “excluded liability” under sale agreement); *In re Old Carco LLC*, No. 14-CV-2225 JMF, 2014 WL 6790781, at \*5 (S.D.N.Y. Dec. 1, 2014) (bankruptcy court had jurisdiction to enforce sale order in dispute over successor liability); *In re Motors Liquidation Co.*, 514 B.R. 377 (Bankr. S.D.N.Y. 2014) (bankruptcy court has post-sale jurisdiction to interpret and enforce its sale order). The First Circuit also ignored a similar precedent in its own circuit. See, e.g., *White v. Kubotek Corp.*, 487 B.R. 1 (D. Mass. 2012) (bankruptcy court had authority to enforce its sale order with respect to successor-liability claims).

Other sale-related examples illustrate *Gupta*'s strained reasoning. For example, a bankruptcy court might lack jurisdiction to adjudicate post-closing disputes related to other types of assumed liabilities — gift cards or rewards-program benefits in the retail context, environmental clean-up in the energy sector and pension-related obligations of manufacturing companies. Myriad other examples exist. Thus, under *Gupta*, parties whose liabilities were assumed by the buyer likely could not seek recompense in bankruptcy court because it would lack the jurisdiction to enforce the provisions of the sale agreement expressly approved by a “final” sale order, even though the buyer expressly accepted the bankruptcy court’s post-sale jurisdiction as a condition to buying the debtor’s assets and did not challenge or appeal the order.<sup>34</sup>

## **Gupta Applied More Broadly**

Sale orders may not be the only orders affected by the First Circuit’s *Gupta* decision. Thus, at least in the First Circuit, other bankruptcy court orders containing retention-of-jurisdiction clauses could be subject to the same reasoning.

For example, the *Gupta* decision could affect post-confirmation disputes — closely analogous to post-sale disputes. Most plan-confirmation orders approve and incorporate highly negotiated reorganization or liquidation plans. Such orders also typically include retention-of-jurisdiction language that states that the bankruptcy court retains jurisdiction to interpret and enforce the terms and conditions of the confirmation order and confirmed plan.

Similarly, the *Gupta* decision could undermine bankruptcy courts’ authority to interpret and enforce Rule 9019 settlement orders. For example, it is not uncommon for parties to reach “global” settlements in bankruptcy cases that often require payments in exchange for releases and dismissals of pending litigation. Rule 9019 orders approving settlements also usually incorporate the terms and conditions of a settlement agreement and contain retention-of-jurisdiction paragraphs similar to those contained in sale orders.

What happens if a post-confirmation dispute arises regarding the enforcement of a specific plan provision approved by a “final” confirmation order? Similarly, can a bankruptcy court enforce the terms of a settlement agreement approved by a settlement order where the parties consented to the court’s jurisdiction to enter the settlement order in the first instance? Just like an order approving a sale agreement under § 363, it would be difficult to argue that the bankruptcy court did not have subject-matter jurisdiction because the effects of such agreements on a debtor’s bankruptcy estate give rise to related-to<sup>35</sup> or arising-in<sup>36</sup> jurisdiction in the first instance.

## **Conclusion**

The *Gupta* decision is suspect given binding Supreme Court precedent in *Travelers*. It is a cautionary reminder for both sellers/debtors and buyers of assets in bankruptcy cases, as well as those whose rights are to be affected by § 363 sales, that parties should be acutely aware of the potential constraints on a bankruptcy court’s authority to adjudicate post-closing disputes. Particularly for those in the First Circuit, parties should also be wary of the broader potential implications that *Gupta* might portend for disputes arising from other types of agreements approved by “final” bankruptcy court orders. **abi**

*Reprinted with permission from the ABI Journal, Vol. XXXVI, No. 10, October 2017.*

*The American Bankruptcy Institute is a multi-disciplinary, non-partisan organization devoted to bankruptcy issues. ABI has more than 12,000 members, representing all facets of the insolvency field. For more information, visit [abi.org](http://abi.org).*

<sup>34</sup> *Gupta* also raises the prospect that sale orders will have to become more voluminous so as to explicitly restate every specific aspect of the sale agreement over which the bankruptcy court retained post-closing jurisdiction.

<sup>35</sup> See *Celotex v. Edwards*, 514 U.S. 300, 308 (1995) (“[T]he test for determining whether a civil proceeding is related to a bankruptcy is whether the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy.” (citation omitted)).

<sup>36</sup> See *Sterling Vision Inc. v. Sterling Optical Corp.* (*In re Sterling Optical Corp.*), 302 B.R. 792, 801 (Bankr. S.D.N.Y. 2003) (“Matters involving the enforcement or construction of a bankruptcy court order are in [the ‘arising in’] category.”); see also 1 *Collier on Bankruptcy* ¶ 3.01[3][e][iv] (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2016) (noting that arising-in jurisdiction refers to “administrative matters” that could not “have been the subject of a lawsuit absent the filing of a bankruptcy case”).