ALERT MEMORANDUM

Second Circuit Reaffirms Its Preference for Equitable Mootness

February 24, 2021

On February 18, 2021, the United States Court of Appeals for the Second Circuit (the "Second Circuit") issued an opinion in *GLM DFW, Inc. v. Windstream Holdings, Inc.*,[1] dismissing a creditor's appeal of an order authorizing the debtor to pay prepetition debts to certain critical vendors on equitable mootness grounds. On appeal, the creditor argued that the equitable mootness doctrine was inapplicable in this case because it was not directly challenging the reorganization plan, which had been confirmed while the appeal was pending. The Second Circuit disagreed, noting that a finding for the creditor "could cause tens of millions of dollars in previously satisfied claims to spring back to life."[2] The opinion reaffirms the Second Circuit's preference for preserving confirmed plans of reorganization that have been substantially consummated. It also highlights the divide between the Second Circuit and other circuit courts who have signaled increasing skepticism towards the doctrine of equitable mootness, particularly the neighboring Third Circuit.

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[1] No. 20-1275-bk, 2021 U.S. App. LEXIS 4630 (2d Cir. Feb. 18, 2021).
[2] *Id.* at *6.

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Background

In February 2019, Windstream Holdings, Inc. ("Windstream"), a network communications provider, filed a voluntary petition for Chapter 11 relief in the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"). On the same day that it filed its petition, Windstream filed a motion requesting the authority to pay the prepetition claims of certain critical vendors while still in bankruptcy (the "Vendor Motion"). Windstream noted in its motion that it had identified approximately 263 vendors as critical, and that it owed those vendors approximately $80 million.[3] On February 28, 2019, the Bankruptcy Court entered an in interim order approving the Vendor Motion.

GLM DFW, Inc. ("GLM"), a waste management vendor who was not among the list of critical vendors identified by Windstream, objected to the interim order, arguing that it was for the Bankruptcy Court to determine who was a critical vendor, not Windstream. GLM further argued that Windstream should be compelled to disclose the identity of the critical vendors, and that the interim order failed to impose any standard on what facts qualified a vendor as critical. No other party objected to the Vendor Motion.

In April 2019, the Bankruptcy Court held a final hearing on the Vendor Motion. At the hearing, Windstream provided testimony on the process they used to identify critical vendors, which included a protocol to determine the disruption to Windstream's business if a critical vendor ceased providing services, along with daily meetings to reassess which critical vendors actually needed to be paid. Windstream further explained that maintaining the confidentiality of its list of critical vendors was essential in order to preserve Windstream's leverage in negotiations with those vendors and to avoid a run on the bank, given the limited pool of available cash.

The Bankruptcy Court denied GLM's objection and granted the Vendor Motion because Windstream's process for identifying critical vendors was sufficient to protect Windstream's business for all parties in interest, and constituted "a proper exercise of [Windstream's] judgment."[4] Shortly after the hearing, the Bankruptcy Court entered a final order authorizing Windstream to continue its prepetition business operations and pay accrued prepetition vendor claims in the ordinary course of business or as necessary to retain the vendor's service. In July 2019, the Bankruptcy Court approved Windstream's motion to reject its executory contract with GLM, thereby ending GLM's vendor relationship with Windstream.

Following the grant of the Vendor Motion, GLM appealed the Bankruptcy Court's order to the United States District Court for the Southern District of New York (the "District Court"). On appeal, GLM renewed its original objections to the Vendor Motion, arguing in particular that that the Bankruptcy Court had impermissibly delegated its judicial authority to Windstream by allowing Windstream to determine which vendors qualified as critical vendors.

In April 2020, the District Court affirmed the Bankruptcy Court's order, noting that Windstream's Vendor Motion thoroughly outlined the deliberative process it had used to identify critical vendors and that the list of critical vendors had been submitted to the U.S. Trustee, the Official Committee of Unsecured Creditors, and the Bankruptcy Court itself (for *in camera* review). Furthermore, the District Court noted the impracticability of having the Bankruptcy Court interrogate Windstream about each of the 263 critical vendors in open court. Under the circumstances, the District Court held that it was appropriate for the Bankruptcy Court to rely on Windstream's "sound business judgment" in determining which vendors qualified as critical vendors.[5]

GLM appealed the District Court's decision to the Second Circuit, again renewing its arguments below. While GLM's Second Circuit appeal was pending, the Bankruptcy Court confirmed Windstream's plan of reorganization on June 26, 2020. Windstream

[3] *GLM DFW, Inc. v. Windstream Holdings, Inc.*, 614 B.R. 441, 445 (S.D.N.Y. 2020).

[4] *Id.* at 448.

[5] *Id.* at 452.

subsequently raised the issue of equitable mootness in its appellate brief.

The Second Circuit's Opinion

The Second Circuit began its opinion by noting that Windstream's plan of reorganization had already been confirmed and "substantially consummated."[6] Without reaching GLM's specific objections to the Vendor Motion, the Second Circuit analyzed the appeal under the doctrine of equitable mootness.

The court reaffirmed its precedent defining equitable mootness as a tool for courts "to avoid disturbing a reorganization plan once implemented."[7] Under this precedent, the Second Circuit has created a presumption that once a plan has already been substantially consummated, an appeal that would disturb that plan is equitably moot. In order to overcome the presumption of equitable mootness, a party must demonstrate five factors, dubbed the *Chateaugay* factors, including:

(1) "the court can still order some effective relief;"

(2) "such relief will not affect the re-emergence of the debtor as a revitalized corporate entity;"

(3) "such relief will not unravel intricate transactions so as to knock the props out from under the authorization for every transaction that has taken place and create an unmanageable, uncontrollable situation for the [b]ankruptcy [c]ourt;"

(4) "the parties who would be adversely affected by the modification have notice of the appeal and an opportunity to participate in the proceedings;" and

(5) "the appellant pursued with diligence all available remedies to obtain a stay of execution of the objectionable order if the failure to do so creates a situation rendering it inequitable to reverse the orders appealed from."[8]

GLM argued "that the equitable mootness doctrine is simply inapplicable in this case because the appeal does not directly concern the bankruptcy court's order confirming Windstream's plan of reorganization."[9] The Second Circuit rejected this reasoning, noting that nothing in its interpretation of the equitable mootness doctrine requires that the mooted appeal be a direct challenge to the reorganization plan itself. Rather, the doctrine of equitable mootness relates to "the important interest of finality that attaches once a reorganization plan is approved and consummated," and therefore applies wherever an appeal impacts that plan.[10] To underscore this point, the court noted that the *Chateaugay* case itself involved a challenge to several orders that were independent of a plan of reorganization.[11]

The Second Circuit found that GLM failed to satisfy all five of the *Chateaugay* factors. In particular, the court took issue with GLM's failure to seek a stay of the Bankruptcy Court's order approving the Vendor Motion, along with its failure to seek an expedited appeal or ask the Bankruptcy Court to hold off on plan confirmation. In light of GLM's lack of diligence, the Second Circuit determined that fairness concerns counseled towards dismissal of the appeal.

In conclusion, the Second Circuit stated, "[g]ranting GLM the relief it seeks could cause tens of millions of dollars in previously satisfied claims to spring back to life, thereby potentially requiring the bankruptcy court to reopen the plan of reorganization."[12] In light of this uncertainty, and compounded with GLM's failure to seek a stay or an expedited appeal, the court held that it would be inequitable to grant GLM its requested relief.

Implications of the Second Circuit's Decision

The Second Circuit's decision in *GLM DFW, Inc. v. Windstream Holdings, Inc.* reaffirms the circuit's

[6] *GLM*, 2021 U.S. App. LEXIS 4630, at *2.
[7] *Id.* (quoting *Deutsche Bank AG v. Metromedia Fiber Network, Inc.*, 416 F.3d 136, 144 (2d Cir. 2005)).
[8] *Id.* at *3 (quoting *Frito-Lay, Inc. v. LTV Steel Co.* (*In re Chateaugay Corp.*), 10 F.3d 952–53 (2d Cir. 1993)).
[9] *Id.* at *3–4.
[10] *Id.* at *4.
[11] *Id.*
[12] *Id.* at *6.

strong presumption against disturbing confirmed plans of reorganization that have been substantially consummated. GLM's appeal was not a challenge to the plan itself, and it was commenced before the Bankruptcy Court had confirmed a reorganization plan. Nevertheless, the intervening confirmation and consummation of Windstream's reorganization plan fourteen months after the critical vendor order was entered was sufficient for the Second Circuit to dismiss GLM's appeal as equitably moot.

The Second Circuit's full-throated embrace of equitable mootness comes even as other circuits have expressed increasing concerns about the doctrine. Notably, the neighboring Third Circuit, which includes the influential Bankruptcy Court for the District of Delaware, takes a far more reserved approach to dismissing appeals as equitably moot. In the 2015 case *In re Tribune Media Co.*,[13] the Third Circuit outlined its approach to equitable mootness, which it described as a "narrow doctrine" that should be applied "with a scalpel rather than an axe."[14] In the converse of the Second Circuit's presumption, the Third Circuit requires the party seeking to invoke the doctrine to overcome "the strong presumption that appeals from confirmation orders of reorganization plans . . . need to be decided."[15] Indeed, in *Tribune Media*, the Third Circuit refused to invoke equitable mootness to preserve a substantially consummated plan where the appeal at issue would only affect a small portion of that plan, and chastised the lower court for "elevat[ing] finality over all other interests" by finding the appeal equitably moot.[16]

Just last month, the Third Circuit in *In re Nuverra Environmental Solutions, Inc.* considered whether a challenge to a confirmed plan was equitably moot. Although the court ultimately dismissed the appeal on equitable mootness grounds, it did so over a strongly-worded opinion by Judge Krause, who concurred in the judgment but wrote separately "to call attention to the consequences of our ill-advised expansion of the [equitable mootness] doctrine, as exemplified in this case."[17] In the opinion of Judge Krause, both the Third Circuit and other courts have too often "allowed the doctrine itself to short-circuit the merits analysis."[18] Although Judge Krause would have reached the same result as the majority of her panel, she would have done so on the merits of the appellant's claims, not on equitable mootness grounds, a doctrine which in her view "precludes the development of bankruptcy law" as to the substantive questions raised on appeal.[19]

In contrast to the Second Circuit's willingness to set aside GLM's appeal due to the intervening confirmation of a reorganization plan, Judge Krause's dissent highlights the Third Circuit's comparative reluctance to use equitable mootness as a tool to preserve already-confirmed plans. The widening gulf between these two major circuits on the doctrine of equitable mootness highlights the difference in access to appellate review on orders directly or indirectly impacting a confirmed plan. Parties in the Second Circuit, especially those pursuing an objection to any order implicating the finality of a plan of reorganization, must be mindful of the very real possibility that appellate review may not be available after a plan is confirmed and substantially consummated. Moreover, debtors analyzing available venues should be mindful of the additional powers afforded to them under Second Circuit caselaw to insulate orders from challenge on appeal. The Second Circuit's opinion is also instructive on the point that any objector must be mindful to act with diligence to pursue all remedies in order to satisfy the final *Chateaugay* factor and preserve its ability to overcome equitable mootness.

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[13] 799 F.3d 272 (3d Cir. 2015).
[14] *Id*. at 277–78.
[15] *Id*. at 278.
[16] *Id*. at 283.
[17] *In re Nuverra Envtl. Solutions, Inc.*, No. 18-3084, 2021 U.S. App. LEXIS 244, at *11–12 (3d Cir. Jan. 6, 2021) (Krause, J., concurring in the judgment).
[18] *Id*. at *12.
[19] *Id*. at *14.