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THIRD-PARTY BANKRUPTCY RELEASES AND THE SEPARATION OF POWERS: A *STERN* LOOK

ABSTRACT

In the last few years, bankruptcy scholars and professionals have criticized mass tort debtors' use of chapter 11 bankruptcy as a litigation forum. One such criticism concerns mass tort debtors' use of third-party releases: provisions in chapter 11 reorganization plans that enjoin creditors' claims against non-debtor third parties. If a bankruptcy court approves such releases, creditors lose claims against the released third parties, which often include the debtor's directors, insurers, or employees.

Third-party releases have troubled many. Critics and courts have said that third-party releases violate (1) the Bankruptcy Code, (2) bankruptcy policy, (3) the constitutional right to due process, and (4) the separation of powers. All four of these issues hold water, but the separation of powers especially warrants addressing because of its prophylactic nature—implemented correctly, the separation of powers mitigates the other three concerns. The separation of powers problem is that bankruptcy courts exceed their Article I authority by approving releases that alter only non-debtors' legal rights, a job typically reserved for Article III courts.

The Supreme Court guided bankruptcy courts on the separation of powers in the seminal case Stern v. Marshall. *Yet bankruptcy courts still lack a uniform separation of powers approach for third-party releases. This Comment proposes a framework to help bankruptcy courts gauge the constitutionality of third-party releases. Bankruptcy courts should analyze each proposed release individually using the "public rights exception" from* Stern, *presuming the releases unconstitutional until the debtor proves otherwise. Doing so will protect constitutional sanctity, serve bankruptcy policy, and mitigate due process risks.*

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INTRODUCTION: THIRD-PARTY RELEASES & MASS TORT DEBTORS

A. Third-Party Releases

Third-party releases are provisions in chapter 11 reorganization plans that enjoin creditors' claims against non-debtor third parties.[1] Chapter 11 generally provides for the financial restructuring of businesses, like corporations and partnerships.[2] A chapter 11 debtor can propose a reorganization plan, a legal document that keeps the debtor's business alive, enjoins creditors' claims against the debtor, and replaces those claims with a binding repayment scheme.[3]

Creditors with claims against a bankrupt business often have other related claims against affiliated third parties.[4] These third parties may be the business's directors, managers, employees, or insurers.[5] When a chapter 11 plan contains third-party releases, it enjoins creditors' claims against *both* the bankrupt business and its affiliated third parties.

Third-party releases often arise in complex mass tort cases.[6] Releases provide two benefits to mass tort debtors. First, because releases bar creditors from suing the third parties, those third parties will not seek indemnity from the debtor.[7] Second, in exchange for the release, the third parties usually contribute funds to a settlement trust for the tort creditors.[8]

These benefits have long attracted mass tort debtors. In 1986, Johns-Manville used a third-party release when it filed for chapter 11 while entrenched

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1 *See* Jason W. Bank, *Nuts and Bolts of Evaluating Third-Party Releases in Chapter 11 Plans*, AM. BANKR. INST. J., Sept. 2018, at 12.

2 *Chapter 11 - Bankruptcy Basics*, U.S. COURTS, https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics (last visited Dec. 31, 2023) [hereinafter *Chapter 11 Basics*].

3 *See id.* Individuals can also seek relief under chapter 11. However, individuals typically prefer chapter 13 reorganization over chapter 11 because the latter has a more expensive filing fee, requires court approval for the debtor to retain counsel, does not provide the debtor a right to dismiss the case, and has stringent plan confirmation requirements. *Why File an Individual Chapter 11 Bankruptcy?*, FREEDOM L. FIRM, https://www.freedomlegalteam.com/why-file-an-individual-chapter-11-bankruptcy/ (last visited Dec. 31, 2023).

4 *See* Bank, *supra* note 1, at 12.

5 *Id.* at 13.

6 *See generally* Part II.E (discussing third-party releases that arose in various mass tort cases).

7 Michael S. Etkin & Nicole M. Brown, *Third-Party Releases?—Not So Fast! Changing Trends and Heightened Scrutiny*, 29 ASS'N INSOLVENCY & RESTRUCT. ADVISORS, no. 3, 2015, at 22.

8 *See* Clinton E. Cutler, *Is a Legislative Crackdown Coming on Third Party Releases in Bankruptcy Plans?*, FREDRIKSON RESTRUCT. REP. (Sept. 24, 2021), https://www.fredlaw.com/the_restructuring_report/is-a-legislative-crackdown-coming-on-third-party-releases-in-bankruptcy-plans/. Such enjoinments are also called "channeling injunctions." *Channeling Injunction*, POLSINELLI, https://devilsdictionary.polsinelli.com/term/channeling-injunction/ (last visited Dec. 31, 2023).

in asbestos litigation. At Johns-Manville's request, a bankruptcy court approved the company's plan that barred its creditors from pursuing claims against its insurer, Travelers.[9] In exchange, Travelers paid $80 million to a settlement trust for Johns-Manville's tort creditors.[10]

B. Mass Tort Debtors

Mass tort cases are huge undertakings. Defendants in these cases are often large corporations[11] facing thousands of claims and millions of dollars in potential liability.[12] Mass tort cases often arise from the sale of defective products,[13] but cases can also arise from systemic abuse[14] or from wrongful marketing.[15] In the last few years, defendants seeking to simplify these cases have avoided the traditional state and federal court mass tort proceedings, like class actions and multi-district litigation, by instead filing for chapter 11 bankruptcy.

In 2020, the Boy Scouts of America filed for chapter 11 in the wake of thousands of sexual abuse claims.[16] Weinstein Company Holdings entered chapter 11 after a flood of sexual misconduct claims were filed against its co-founder, Harvey Weinstein.[17] Johnson & Johnson turned to chapter 11 facing waves of personal-injury claims stemming from exposure to its asbestos-

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[9] MacArthur Co. v. Johns-Manville Corp., 837 F.2d 89, 90 (2d Cir. 1988).

[10] *See id.*; Phillip J. Loree Jr., Travelers Indemnity Co. v. Bailey*: United States Supreme Court Holds 1986 John-Manville Bankruptcy Court Injunction Bars Direct Asbestos-Related Claims Against The Travelers*, ARB. L. F. (July 8, 2009), https://loreelawfirm.com/blog/travelers-indemnity-co-v-bailey-united-states-supreme-court-holds-1986-john-manville-bankruptcy-court-injunction-bars-direct-asbestos-related-claims-against-the-travelers/.

[11] *Mass Tort Case Updates 2023*, CASE WORKS, https://yourcaseworks.com/mass-tort-updates/ (last visited Dec. 31, 2023).

[12] For example, when Purdue Pharma eventually filed for chapter 11 bankruptcy, it faced about 614,000 claims from individuals, municipalities, hospitals, tribes, and states. The company agreed to pay $4.5 billion to settle its liabilities. Jan Hoffman, *What to Know: Purdue Pharma Settlement*, N.Y. TIMES (Sept. 2, 2021), https://www.nytimes.com/interactive/2021/09/03/health/purdue-opioids-settlement.html.

[13] *See, e.g.*, *Johnson & Johnson Baby Powder and Its Long History of Mass Tort Cases*, ALERT COMMC'NS (Apr. 24, 2019), https://www.alertcommunications.com/blog/johnson-johnson-baby-powder-and-its-long-history-of-mass-tort-cases/.

[14] *See, e.g*, *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 518 (Bankr. D. Del. 2022).

[15] *E.g.*, *The Shift to Mass Tort Litigation—The Cause, The Crisis, The Critical Questions*, GALLAGHER (July 15, 2019), https://www.ajg.com/us/news-and-insights/2019/07/gallagher-mass-tort/.

[16] Specifically, 82,209 creditors filed proofs of claim asserting sexual abuse. Boy Scouts, 642 B.R. at 518.

[17] Spyglass Media Grp., LLC v. Bruce Cohen Prods. (*In re* Weinstein Co. Holdings, LLC), 997 F.3d 497, 502 (3d Cir. 2021).

containing products.[18] And Purdue Pharma filed for bankruptcy while facing individual claims and class actions—"a veritable tsunami of litigation"—alleging that it wrongfully marketed and distributed the drug OxyContin, thereby aggravating the national opioid crisis.[19]

The rush to chapter 11 makes a lot of sense: bankruptcy provides many benefits that other litigation arenas do not. For one, bankruptcy offers debtors a centralized forum to channel tort claims.[20] And mass tort debtors enjoy the protection of bankruptcy's automatic stay, which initiates instantly at the time of filing, freezing proceedings against those debtors.[21] Claimants may even get paid more in bankruptcy cases than in other proceedings like class actions.[22]

C. Problems with Third-Party Releases

Third-party releases are as problematic as they are popular. They raise concerns about the Bankruptcy Code's (the "Code") text and interpretation, bankruptcy policy, the constitutional right to due process, and the main focus of this Comment, the separation of powers.

1. The Bankruptcy Code is Ambiguous

Part I of this Comment explains that the Code neither expressly authorizes nor prohibits third-party releases. Courts have wrestled with various Code sections to assess if they permit releases, but disagreement has split the circuits.[23]

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[18] Jamie Smyth, *J&J Put Newly Created Subsidiary into Bankruptcy Over Talc Claims*, FIN. TIMES (Oct. 14, 2021), https://www.ft.com/content/c82423d4-6728-4292-9653-44b87ebd7a94 ("J&J faces tens of thousands of legal cases from people who allege its cosmetic talc caused cancer."). Technically, Johnson & Johnson did not file for bankruptcy. Instead, it performed a "divisional merger" under Texas law, a process by which it formed a new business entity (called LTL Management), then allocated its asbestos liability to that entity. The new entity then filed for bankruptcy. *In re* LTL Mgmt., LLC, 637 B.R. 396 (Bankr. D.N.J. 2022) (denying tort claimants' motion to dismiss that argued LTL Management's bankruptcy was filed in bad faith), *rev'd*, 64 F.4th 84 (3d Cir. 2023); *see* Samir D. Parikh, *Mass Exploitation*, 170 U. PA. L. REV. ONLINE 53, 58–59 (2022) (explaining and criticizing divisional mergers like Johnson & Johnson's).

[19] *In re* Purdue Pharma, L.P., 635 B.R. 26 (S.D.N.Y. 2021). Claimants in Purdue's case included persons that OxyContin directly harmed, as well as dozens of sovereign states. *See id.* at 45–46.

[20] *See* 28 U.S.C. § 157(b)(5).

[21] 11 U.S.C. § 362(a).

[22] Thomas J. Salerno & Clarissa C. Brady, *In Defense of Third-Party Releases in Chapter 11 Cases: Part II*, AM. BANKR. INST. J., May 2022, at *2–3; *but cf.* Vincent S.J. Buccola & Joshua C. Macey, *Claim Durability and Bankruptcy's Tort Problem*, 38 YALE J. ON REGUL. 766, 773 (2021) (discussing tort creditors general under-compensation in chapter 11 bankruptcy).

[23] *See* Part I.B.

Virtually every circuit has a different approach for analyzing whether the Code allows for releases.[24]

2. *Third-Party Releases Stifle Bankruptcy Policy*

Chapter 11 gives debtors flexibility in reorganizing claims against them.[25] Businesses that face financial hardship can liquidate assets, pay off creditors, and wind up their companies.[26] But the central belief underpinning chapter 11 is that businesses are worth more alive than dead, worth more as a going concern than liquidated, and that all affected parties benefit from a business's survival rather than its demise.[27] That central belief manifests itself in the "fresh start" policy that lies at the heart of bankruptcy law.[28] The Code attempts to embody this fresh start policy by helping bankrupt debtors emerge anew from financial hardship.[29]

But third-party releases allow mass tort debtors to also reorganize claims against third parties who are not in bankruptcy. Third-party releases thus pose a policy conundrum to bankruptcy courts. On one hand, releases can bolster a mass tort debtor's "fresh start" by inducing its affiliated third parties to fund the debtor's tort settlement trust.[30] On the other hand, releases give non-debtor third parties their own "fresh start" by extinguishing creditors' claims against them.[31] The worry is that releases have a tenuous link to bankruptcy policy because they extinguish these third-party claims that are asserted neither by nor against the bankrupt debtor.[32]

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24 *See id.*

25 CHARLES J. TABB & RALPH BRUBAKER, BANKRUPTCY LAW: PRINCIPLES, POLICIES, AND PRACTICE 742 (5th ed. 2021).

26 *See* Will Kenton, *What is Liquidation?*, INVESTOPEDIA (Sept. 23, 2022), https://www.investopedia.com/terms/l/liquidation.asp. Chapter 7 of the Code provides a federal statutory mechanism for debtors, including businesses, to liquidate assets and pay creditors. *See Chapter 7 - Bankruptcy Basics*, U.S. COURTS, https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics (last visited Dec. 31, 2023) [hereinafter *Chapter 7 Basics*].

27 Charles J. Tabb, *What's Wrong With Chapter 11?*, 71 SYRACUSE L. REV. 557, 560 (2021).

28 *See generally* Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393 (1985) (discussing the goals of and purposes for bankruptcy law).

29 *Id.*

30 *See* Cutler, *supra* note 8.

31 *See* Lindsey D. Simon, *Bankruptcy Grifters*, 131 YALE L.J. 1154, 1169 (2022).

32 *See id.* at 1202.

3. *Third-Party Releases Violate Due Process*

Third-party releases can be broad, and bankruptcy courts often approve them without all creditors' consent (releases approved this way are "nonconsensual").[33] Consider a hypothetical: ABC Corp. files for chapter 11 bankruptcy. In its plan, ABC includes a release that states, "All creditors agree to waive all claims under federal securities laws against ABC Corp.'s directors and officers."[34] Creditors voting on ABC's plan could likely determine which claims they are waiving against whom.

If only the real world were so simple. In many mass tort cases, merely reading a third-party release becomes a "herculean undertaking."[35] The chapter 11 plan in *In re Boy Scouts* enjoined sex abuse creditors from bringing claims "known or unknown, foreseen or unforeseen" against various third-party insurers, banks, law firms, mediators, and local troop councils.[36] And the plan in *In re Purdue Pharma* barred creditors' claims predicated on fraud, misrepresentation, and dozens of other bases under state and federal law against a "universe" of third parties, including the debtor's owners, the Sackler family.[37]

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[33] Ralph Brubaker, *Mandatory Aggregation of Mass Tort Litigation in Bankruptcy*, 131 YALE L.J. F. 960, 984–85 (2022) ("[N]ondebtor releases thus raise grave due process concerns.").

[34] This hypothetical release is based on a portion of the opinion in Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641, 670 (E.D. Va. 2022).

[35] *Id.* at 669.

[36] *See* Third Modified Fifth Amended Chapter 11 Plan of Reorganization for Boy Scouts of Am. and Del. BSA, LLC at Art. I(A) ¶ 50, Art. I(A) ¶ 245, Art. IX(B) ¶ 3, Art. X(J)(1)(a), *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 575 (Bankr. D. Del. 2022) (No. 20-10343), 2022 WL 2473402. Perpetrators were not released. *See In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 595 (Bankr. D. Del. 2022) ("To be perfectly clear, Perpetrators are not receiving releases.").

[37] For the sake of illustration: The proposed chapter 11 plan in *Purdue Pharma* contained "releases," i.e., claims that the "Releasing Parties" waived against the "Released Parties." Substituting the plan's definitions of those terms yields the following dizzying result: "All Holders of Claims against [Purdue and] . . . each of their Related Parties" must "conclusively, absolutely, unconditionally, irrevocably, fully, finally, forever and permanently release[] . . . any and all Claims" predicated on "fraud, negligence, gross negligence, recklessness, reckless disregard, deliberate ignorance, public or private nuisance, breach of fiduciary duty, avoidance, willful misconduct, veil piercing, alter-ego theories of liability, unjust enrichment, disgorgement, restitution, contribution, indemnification, right of subrogation and joint liability" that are "based on or relating to, or in any manner arising from, in whole or in part," against any of Purdue's "predecessors, successors, assigns, Subsidiaries, affiliates, managed accounts or funds, past, present and future officers, board members, directors, principals, agents, servants, independent contractors, co-promoters, third-party sales representatives, medical liaisons, members, partners (general or limited), managers, employees, subcontractors, agents, advisory board members, financial advisors, attorneys and legal representatives, accountants, investment bankers, [and others]." *See* Fifth Amended Joint Chapter 11 Plan of Reorganization of Purdue Pharma L.P. and its Affiliated Debtors, at Art. I (§ 1.1), Art. X (§ 10.6), *In re* Purdue Pharma L.P., 633 B.R. 53 (Bankr. S.D.N.Y. 2021) (No. 19-23649), 2021 WL 9316358, at *99–103.

When bankruptcy courts approve broad third-party releases, it is hard to assess which parties are losing claims, which claims they are losing, and against whom the parties are losing the claims.[38] A concern is that when releases are broad and ambiguous, creditors receive inadequate notice of the claims being waived, a fundamental due process requirement.[39]

Third-party releases implicate another due process right: a meaningful opportunity to be heard. Creditors lose the opportunity to litigate their released claims because confirmed releases act as a forced settlement.[40] And even when releases are consensual and creditors agree to them, courts disagree on what actions qualify as consent in this context.[41]

4. *Third-Party Releases Violate the Separation of Powers*

These other worries notwithstanding, this Comment focuses on third-party releases and the separation of powers. Congress derives its powers from Article I, including the power to create bankruptcy courts.[42] And the federal judiciary wields the Article III "judicial Power of the United States."[43] The prototypical exercise of Article III power is deciding common law-type tort claims between parties.[44] So, when Article I bankruptcy courts approve third-party releases, those courts may impermissibly exercise Article III "judicial Power" by deciding common law-type tort claims between non-debtors.[45] To be sure, when bankruptcy courts confirm chapter 11 plans that contain releases, district courts treat the plans (and the releases) as final judgments on appeal and in subsequent litigation[46] and defer to the bankruptcy courts' findings of fact.[47]

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38 United States Trustee's Objection to Confirmation of the Second Modified Fifth Amended Plan of Reorganization for Boy Scouts of America and Delaware BSA, LLC at 11, *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504 (Bankr. D. Del. 2022) (No. 20-10343).

39 Mullane v. Cent. Hanover Bank & Tr. Co., 339 U.S. 306, 313–15 (1950).

40 *See id.* at 309, 314; U.S. v. Ward Baking Co., 376 U.S. 327, 334–35 (1964).

41 *Compare In re* Chassix Holdings, Inc., 533 B.R. 64, 79–80, 82 (Bankr. S.D.N.Y. 2015) (holding that creditors' affirmative opt-in is necessary for consent to releases), *with In re* Indianapolis Downs, LLC, 486 B.R. 286, 304–06 (Bankr. D. Del. 2013) (holding that creditors who failed to opt-out of releases were deemed to consent to them). *See generally* Dorothy Coco, Comment, *Third-Party Bankruptcy Releases: An Analysis of Consent Through the Lenses of Due Process and Contract Law*, 88 FORDHAM L. REV. 231 (2019) (discussing jurisdictional interpretations of consent).

42 *See* U.S. CONST. art. I, § 8, cl. 4 ("Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States.").

43 U.S. CONST. art. III, § 1.

44 U.S. CONST. art. III, § 1; *see* Stern v. Marshall, 564 U.S. 462, 469 (2011).

45 *See In re* Purdue Pharma, L.P., 635 B.R. 26, 81–82 (S.D.N.Y. 2021).

46 *See* 8 COLLIER ON BANKRUPTCY ¶ 1141.01[4] (16th ed. 2017).

47 FED. R. BANKR. P. 8013.

Bankruptcy courts are bound by the Constitution.[48] The separation of Article I and Article III powers is part of "the necessary partition of power among the several departments as laid down in the constitution[.]"[49] Accordingly, when an Article I bankruptcy court evaluates third-party releases and determines that they require Article III power to approve, the bankruptcy court must not approve them.

The separation of powers is not merely a theoretical constitutional requirement, but a practical mechanism. Separating power is "inherently prophylactic,"[50] preventing usurpation of one branch's authority by another.[51] Separation of powers assumes that power accumulation in a single branch poses an existential threat to our legal system and to individual rights.[52] Unfettered third-party releases have already created a circuit split, tension in bankruptcy policies, and due process concerns—all problems that the separation of powers can mitigate.

Courts have yet to agree on a consistent separation of powers approach for third-party releases despite the Supreme Court's guidance in *Stern v. Marshall*.[53] To address this lack of uniformity, this Comment provides a separation of powers analysis that all bankruptcy courts can apply when confronted with third-party releases in mass tort cases.

Part I of this Comment dissects the Code and shows how bankruptcy courts approve third-party releases during chapter 11 plan confirmation, even if those releases are nonconsensual. Part I also examines the circuit split regarding whether the Code permits nonconsensual releases by surveying relevant Code provisions and judicial approaches.

Part II of this Comment analyzes the Supreme Court case *Stern v. Marshall*, which sets forth two principal separation of powers doctrines relevant to bankruptcy courts: the "public rights exception" and the "integral to the restructuring" test. Part II then summarizes various courts' application of *Stern* to third-party releases.

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48 *See* 28 U.S.C. § 453 (reciting oath that all judges must take before performing duties of their office, and noting that they must swear to "administer justice . . . *under the Constitution*") (emphasis added).

49 THE FEDERALIST NO. 51, at 1 (James Madison).

50 GARY LAWSON, FEDERAL ADMINISTRATIVE LAW 102 (9th ed. 2021).

51 *Id*.

52 *See id.* ("The concept of a prophylactic is that it prevents the creation of a critical situation by proceeding on the assumption that it will be impossible to determine, in the individual instance, the existence of a real threat to the values sought to be fostered.").

53 Stern v. Marshall, 564 U.S. 462 (2011).

Finally, Part III of this Comment proposes a framework for bankruptcy courts to employ when assessing their constitutional authority to confirm plans with broad third-party releases. Bankruptcy courts should examine each released claim individually using *Stern*'s public rights exception. Further, bankruptcy courts should presume that releases are unconstitutional until the debtor proves otherwise. This framework best protects constitutional sanctity, serves bankruptcy policy, and mitigates due process risks.

I. THIRD-PARTY RELEASES: THE BANKRUPTCY CODE AND THE CIRCUIT SPLIT

To understand how bankruptcy courts approve third-party releases over dissenting creditors, one must read the relevant Code provisions. The Code's ambiguities explain why the circuits are split on the permissibility of nonconsensual releases. Part I.A walks through chapter 11 plan confirmation and shows how third-party releases can get baked into a confirmed plan. Part I.B discusses the circuit split regarding whether the Code permits nonconsensual releases. Part I.B also surveys the relevant Code provisions and multifarious approaches that courts use when deciding the permissibility of releases.

A. Confirming a Chapter 11 Plan

A chapter 11 plan of reorganization is a legal document that dictates the financial structure and all obligations of a reorganized debtor.[54] Congress intended chapter 11 to be a "flexible mechanism"—parties can negotiate and include just about any provision they want in their plan, as long as the parties agree.[55] Chapter 11 allows debtors to keep assets, restructure debts, and pay those debts at some agreed annuity and interest rate. And it also allows debtors to liquidate assets and distribute the proceeds to creditors in some agreed upon manner.[56]

Creditors vote on whether to approve a plan.[57] Under the Code, plans must group claims into classes for voting purposes and must provide the same

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54 TABB & BRUBAKER, *supra* note 25, at 741.

55 *Id.* at 742.

56 *See Chapter 11 Basics*, U.S. COURTS, *supra* note 2 (noting that because "[i]n a chapter 11 case, a liquidating plan is permissible," that chapter 11 "permits the creditors to take a more active role in fashioning the liquidation of the assets and the distribution of the proceeds than in a chapter 7 case.") (last visited Dec. 31, 2023).

57 *See* 11 U.S.C § 1126. Interestingly, "the Code does not provide a mechanism to force creditors to vote, nor does it clearly spell out the consequences of not voting." Mark G. Douglas & Joseph M. Tiller, *Failure of*

treatment for claims of the same class.[58] Claims of the same class must be "substantially similar" to one another.[59] For example, the plan in *Boy Scouts* grouped all claims and equity interests into ten classes based on substantial similarity.[60] Class 8 comprised individual tort claims based on sexual abuse.[61] Class 9 comprised contribution and indemnity claims that affiliated third-parties, like insurance companies and local councils, could assert against the debtor based on sexual abuse claims.[62]

Once claims are classified, a class is deemed to accept the plan when both (1) creditors in the class holding two-thirds of the value of claims accept, and (2) more than one-half of the number of claims in the class accepts.[63] Thus, third-party releases can get confirmed into a plan even if nearly one-third of the value of claims rejects them, or even if 49% of the claims in number rejects them. During the initial voting on the *Boy Scouts* plan, 26% of Class 8 claims and 30% of Class 9 claims both voted to reject the plan and its releases, but the bankruptcy court was still able to approve the releases because more than 50% of both classes voted to accept.[64]

Even if a class of claims votes to reject third-party releases, the bankruptcy court can invoke its "cramdown" power to confirm the plan over the dissenting creditors.[65] If at least one "impaired" class accepts the plan, the court can approve it so long as it does not "discriminate unfairly" and "is fair and equitable."[66] An impaired class contains creditors whose claims or interests will be legally altered under the proposed plan.[67] The *Boy Scouts* plan is, again, instructive: Classes 3 and 4 were impaired classes composed of commercial loan claims, and both classes voted to accept the plan. So, if Classes 8 and 9 had voted

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Creditor Class to Cast Vote on Chapter 11 Plan Does Not Equate to Acceptance, JONES DAY PUBL'NS (Aug. 1, 2008), https://www.lexology.com/library/detail.aspx?g=477275fa-6ff4-4be9-9454-f41970198a1c.

58 *See* 11 U.S.C. § 1123(a)(1)–(4).

59 11 U.S.C. § 1122(a). However, the Code does not require that all "substantially similar" claims be classified together. *Id.*

60 *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 535–36 (Bankr. D. Del. 2022).

61 *Id.* at 536.

62 *See id.*

63 11 U.S.C. § 1126(c). This Code section also makes clear that only affirmative votes count towards or against the approval requirements—abstentions are ignored.

64 *See* Boy Scouts, 642 B.R. at 538 t.3.

65 *See* 11 U.S.C. § 1129(b)(1).

66 *See* 11 U.S.C. § 1129(a)(8), (a)(10), (b)(1).

67 *See* 11 U.S.C. § 1124. Actually, classes are *presumed* impaired unless a proposed plan "leaves unaltered the legal, equitable, and contractual rights" of the claim- or interest-holders of a class.

to reject the releases in the plan, the bankruptcy court could still have approved the releases because at least one impaired class accepted the plan.

The catch-all limitation on plan confirmation is section 1129(a)(1). It states that a bankruptcy court can confirm a plan only if "the plan complies with the applicable provisions of [the Code]."[68] The circuits are split as to whether third-party releases do in fact comply with all the applicable Code provisions.

B. The Circuit Split

The Second,[69] Third,[70] Fourth,[71] Sixth,[72] Seventh,[73] Ninth,[74] and Eleventh[75] Circuits maintain that the Code permits bankruptcy courts to grant nonconsensual third-party releases in limited circumstances. The Fifth[76] and Tenth[77] Circuits say that the Code prohibits nonconsensual third-party releases.[78] The circuits look to different Code provisions in their reasoning, and

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68 11 U.S.C. § 1129(a)(1).

69 *E.g.*, Deutsche Bank AG, London Branch v. Metromedia Fiber Network, Inc. (*In re* Metromedia Fiber Network, Inc.), 416 F.3d 136, 142 (2d Cir. 2005) (quoting New Eng. Dairies, Inc. v. Dairy Mart Convenience Stores, Inc., (*In re* Dairy Mart Convenience Stores, Inc.), 351 F.3d 86, 92 (2d Cir. 2003)) (acknowledging that "section 105(a) does not allow the bankruptcy court to create substantive rights that are otherwise unavailable under applicable law," but did not cite any applicable law justifying the third-party releases at issue) (quotation marks omitted).

70 *E.g.*, Gillman v. Cont'l Airlines (*In re* Cont'l Airlines), 203 F.3d 203, 214 (3d Cir. 2000).

71 *E.g.*, Nat'l Heritage Found., Inc. v. Highbourne Found. (*In re* Nat'l Heritage Found., Inc.), 760 F.3d 344, 347 (4th Cir. 2014).

72 *E.g.*, Class Five Nev. Claimants v. Dow Corning Corp. (*In re* Dow Corning Corp.), 280 F.3d 648, 657–58 (6th Cir. 2002) (relying on section 105(a) and section 1123(b)(6) to grant releases, and noting that section 524(e) merely "explains the *effect* of a debtor's discharge" but "does not prohibit the release of a non-debtor") (emphasis added).

73 *E.g.*, Airadigm Commc'ns, Inc. v. FCC (*In re* Airadigm Commc'ns, Inc.), 519 F.3d 640, 657 (7th Cir. 2008).

74 *See, e.g.*, Blixeth v. Credit Suisse, 961 F.3d 1074, 1081–85 (9th Cir. 2020). To be fair, the *Blixeth* court did not approve third-party releases, which absolve third parties of liability arising from their prepetition and postpetition conduct. Rather, the *Blixeth* court approved "exculpatory clauses," another type of non-debtor release that absolves estate fiduciaries of liability arising from their postpetition conduct. However, bankruptcy courts in the Ninth Circuit have since expanded *Blixeth* to cover third-party releases. *See, e.g.*, *In re* PG&E Corp., 617 B.R. 671, 683–84 (Bankr. N.D. Cal. 2020).

75 *E.g.*, SE Prop. Holdings, LLC v. Seaside Eng'g & Surveying, Inc. (*In re* Seaside Eng'g & Surveying, Inc.), 780 F.3d 1070, 1078 (11th Cir. 2015).

76 *See, e.g.*, Bank of N.Y. Tr. Co. v. Off. Unsecured Creditors' Comm. (*In re* Pac. Lumber Co.), 584 F.3d 229, 252 (5th Cir. 2009).

77 *See, e.g.*, Landsing Diversified Props.–II v. First Nat'l Bank & Tr. Co. of Tulsa (*In re* W. Real Est. Fund, Inc.) 922 F.2d 592, 600 (10th Cir. 1990).

78 The First, Eighth, and D.C. Circuits have not ruled on the statutory issue. *See* Monarch Life Ins. Co. v. Ropes & Gray, 65 F.3d 973, 979–80 (1st Cir. 1995); Murray Ky. Energy, Inc. v. Ceralvo Holdings, LLC (*In re* Armstrong Energy, Inc.), 613 B.R. 529, 535 (8th Cir. 2020); *In re* AOV Indus., Inc., 792 F.2d 1140, 1153 (D.C. Cir. 1986).

those in the majority each apply different standards when deciding whether to grant releases.

1. Code Provisions Relevant to the Split

The Code neither expressly authorizes nor prohibits third-party releases. So, courts must wrestle with several ambiguous Code provisions in determining release permissibility. The first such provision is section 105(a), titled "Power of Court," which states that "[t]he court may issue *any order, process, or judgment that is necessary* or appropriate to carry out the provisions of this title."[79] Section 105(a) encapsulates the bankruptcy court's equitable powers,[80] and parties and judges have long cited it as authority for the court to fashion new remedies when the remedies at law are inadequate.[81] Circuits in the majority often rely on section 105(a) and the bankruptcy court's broad "principles and rules of equity jurisprudence" to approve third-party releases when needed for chapter 11 plan confirmation.[82]

Other circuits question such interpretations of section 105(a). Some circuits hold that bankruptcy courts cannot use their equitable powers under section 105(a) to fashion substantive rights not contained elsewhere in the Code.[83] Even the Second Circuit, which resides in the majority, has acknowledged that in the third-party release context, any equitable power that bankruptcy courts enjoy under section 105(a) must independently derive from some other Code provision.[84]

Putting the bankruptcy court's equitable powers aside, the Code grants debtors broad discretion in constructing chapter 11 plans. Section 1123(b), titled "Contents of Plan," allows debtors to equip plans with "any other appropriate provision not inconsistent with the applicable provisions of this title."[85] Because most circuits maintain that no Code provision expressly prohibits third-party

[79] 11 U.S.C. § 105(a) (emphasis added).

[80] Bank of Marin v. Eng., 385 U.S. 99, 103 (1966) ("[E]quitable principles govern the exercise of bankruptcy jurisdiction.").

[81] *In re* Chinichian, 784 F.2d 1440, 1443 (9th Cir. 1986).

[82] *E.g.*, SE Prop. Holdings, LLC v. Seaside Eng'g & Surveying, Inc. (*In re* Seaside Eng'g & Surveying, Inc.), 780 F.3d 1070, 1078 (11th Cir. 2015) (quoting Airadigm Commc'ns, Inc. v. FCC (*In re* Airadigm Commc'ns, Inc.), 519 F.3d 640, 659 (7th Cir. 2008)).

[83] *E.g.*, Yaquinto v. Ward (*In re* Ward), 978 F.3d 298, 303 (5th Cir. 2020).

[84] *See* Deutsche Bank AG, London Branch v. Metromedia Fiber Network, Inc. (*In re* Metromedia Fiber Network, Inc.), 416 F.3d 136, 142 (2d Cir. 2005).

[85] 11 U.S.C. § 1123(b)(6).

releases, they reason that releases are "not inconsistent" with the Code and so section 1123(b) allows debtors to add releases to their plans.[86]

But the minority of circuits says that such releases are "inconsistent" with the Code, that is, that there are other Code provisions that prohibit third-party releases. In particular, section 524(e), titled "Effect of Discharge," states that the "discharge of a debt of the debtor *does not affect the liability of any other entity* on, or the property of any other entity for, such debt."[87] The Fifth Circuit explained that under section 524(e), chapter 11 reorganization can release only the debtor from liability on claims, not co-liable third parties.[88] To reconcile section 524(e) with third-party releases, circuits in the majority maintain that "discharge" is a bankruptcy term of art that is distinct from a "release."[89] To the majority, section 524(e) merely explains the effect of a debtor's discharge but does not prohibit the release of a non-debtor.[90]

Even so, the minority reasons that another Code provision implies a prohibition on third-party releases: section 524(g). That section expressly authorizes nonconsensual third-party releases, but *only* in cases involving asbestos.[91] Congress added this asbestos-only provision in the Bankruptcy Reform Act of 1994, effectively codifying the releases that Johns-Manville used in its chapter 11 bankruptcy to bar asbestos claimants from suing its insurers.[92] The argument goes that under the statutory canon of construction "*expressio unius*," Congress expressly authorizing releases in asbestos cases implies that Congress prohibited releases in all other cases.[93]

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[86] Class Five Nev. Claimants v. Dow Corning Corp. (*In re* Dow Corning Corp.), 280 F.3d 648, 657 (6th Cir. 2002).

[87] 11 U.S.C. § 524(e) (emphasis added).

[88] Bank of N.Y. Tr. Co. v. Official Unsecured Creditors' Comm. (*In re* Pac. Lumber Co.), 584 F.3d 229, 252 (5th Cir. 2009).

[89] *See Dow Corning Corp.*, 280 F.3d at 657.

[90] *Id.*

[91] *See* 11 U.S.C § 524(g).

[92] *See* 140 CONG. REC. S14461 (1994) (statement of Sen. Brown); *A Look Back at Mass Tort Bankruptcy Cases in 2019 – Asbestos and Beyond*, CROWELL, at *2 (Jan. 22, 2020), https://www.crowell.com/NewsEvents/AlertsNewsletters/all/A-Look-Back-at-Mass-Tort-Bankruptcy-Cases-in-2019-Asbestos-and-Beyond.

[93] *In re* Purdue Pharma L.P., 635 B.R. 26, 92 (S.D.N.Y. 2021) ("The language of the statute plainly indicates that Congress believed that Section 524(g) created an exception to what would otherwise be the applicable rule of law."). The canon's full name is "*expressio unius est exclusio alterious*," a Latin term that literally means "the expression of one thing is the exclusion of the other." *See* ANTONIN SCALIA & BRYAN A. GARNER, READING LAW: THE INTERPRETATION OF LEGAL TEXTS 99 (2012).

When Congress enacted section 524(g), it included a rule of construction that some courts believe undermines the asbestos-only *expressio unius* argument.[94] The rule of construction comes from a note in the Bankruptcy Reform Act of 1994. The note states that nothing in section 524(g) "shall be construed to modify, impair, or supersede any other authority the court has to issue injunctions in connection with an order confirming a plan of reorganization."[95] Therefore, some courts hold that section 524(g)'s rule of construction means that Congress implied nothing as to third-party releases' permissibility in non-asbestos contexts.[96]

2. *Judicial Approaches in the Majority*

Although the majority says that the Code permits nonconsensual third-party releases, courts are all over the map when deciding whether to grant them in a given case. Virtually every circuit analyzes the issue differently.[97] These judicial approaches are manifold, likely because bankruptcy courts' underlying authority for granting releases derives from the nebulous "equitable powers" under section 105(a).[98]

Several circuits and many bankruptcy courts have cited the five-factor approach that the U.S. Bankruptcy Court for the Western District of Missouri set forth in the 1994 case *In re Master Mortgage*.[99] The *Master Mortgage* factors instruct that nonconsensual third-party releases are appropriate when:

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94 *See In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 594–95 (Bankr. D. Del. 2022).

95 Bankruptcy Reform Act of 1994, Pub. L. No. 103-394 § 111(b).

96 Boy Scouts, 642 B.R. at 594–95 (Bankr. D. Del. 2022).

97 *See, e.g.*, Gillman v. Cont'l Airlines (*In re* Cont'l Airlines), 203 F.3d 203, 214 (3d Cir. 2000) (acknowledging that "[t]he hallmarks of permissible non-consensual releases" are "fairness, [and] necessity to the reorganization"); Airadigm Commc'ns, Inc. v. FCC (*In re* Airadigm Commc'ns, Inc.), 519 F.3d 640, 657 (7th Cir. 2008) (holding that release permissibility analysis is "fact intensive and depends on the nature of the reorganization"); Class Five Nev. Claimants v. Dow Corning Corp. (*In re* Dow Corning Corp.), 280 F.3d 648, 658 (6th Cir. 2002) (applying a seven-factor balancing test to assess release permissibility); SE Prop. Holdings, LLC v. Seaside Eng'g & Surveying, Inc. (*In re* Seaside Eng'g & Surveying, Inc.), 780 F.3d 1070, 1079–81 (11th Cir. 2015) (applying the exact same seven-factor balancing test from *Dow Corning* but adding other "additional considerations" to the analysis).

98 Etkin & Brown, *supra* note 7, at 23 (noting that "[t]he crux of the debate" as to third-party releases "often turns on how courts perceive the breadth of their section 105(a) equitable powers").

99 168 B.R. 930, 934–35 (Bankr. W.D. Mo. 1994); *see, e.g.*, Eastman Kodak Co. v. Atlanta Retail, Inc. (*In re* Atlanta Retail, Inc.), 456 F.3d 1277, 1290 (11th Cir. 2006) (applying *Master Mortgage*'s reasoning to the third-party releases at issue); Monarch Life Ins. Co. v. Ropes & Gray, 65 F.3d 973, 979–80 (1st Cir. 1995) (citing *Master Mortgage* as an important case in third-party release analysis, and noting its factors); Gillman v. Cont'l Airlines (*In re* Cont'l Airlines), 203 F.3d 203, 213 n.9 (3d Cir. 2000) (citing *Master Mortgage*).

> (i) an identity of interests exists between the debtor and the third-party; (ii) the third-party has contributed substantial assets to the reorganization; (iii) the release is essential to the reorganization; (iv) a substantial majority of the creditors agree to the release; and (v) the plan provides a mechanism to pay for substantially all claims of the class(es) affected by the release.[100]

Some circuits employ similar multi-factor balancing tests when confronted with nonconsensual third-party releases.[101] The Sixth Circuit laid out a seven-factor test in *In re Dow Corning* that has the same five factors from *Master Mortgage*, but with two additional factors: (vi) whether the plan allows non-settling claimants to recover in full, and (vii) whether the bankruptcy court found specific facts that support its conclusions.[102] The Eleventh Circuit took the analysis a step further in *In re Seaside Engineering & Surveying, Inc.* by implementing the seven *Dow Corning* factors, but then adding its own "additional considerations."[103]

Other circuits in the majority reject the multi-factor approach. For example, in *In re Continental Airlines*, the Second Circuit declined to establish a rule or test for permitting third-party releases.[104] Instead, the court said that the two "hallmarks of permissible non-consensual releases" were "fairness" and "necessity to the reorganization."[105] The Fourth Circuit also outright declined to establish a permissibility test in *Behrmann v. National Heritage Foundation*, instead charging bankruptcy courts with deciding which factors are relevant in a given case.[106]

II. BANKRUPTCY AND THE SEPARATION OF POWERS: *STERN V. MARSHALL*

Third-party releases extinguish creditors' claims against third parties.[107] In other words, releases alter the legal rights and obligations between non-debtors.[108] This poses a separation of powers problem. Article I bankruptcy

[100] Although the *In re Master Mortgage* court did not articulate these five factors in this manner verbatim, the court discussed and applied each factor at length. *See generally* Master Mort., 168 B.R. 930.

[101] *Dow Corning Corp.*, 280 F.3d at 658.

[102] *Id.*

[103] SE Prop. Holdings, LLC v. Seaside Eng'g & Surveying, Inc. (*In re* Seaside Eng'g & Surveying, Inc.), 780 F.3d 1070, 1079–81 (11th Cir. 2015).

[104] Gillman v. Cont'l Airlines (*In re* Cont'l Airlines), 203 F.3d 203, 214 (3d Cir. 2000).

[105] *Id.* The Second Circuit noted that specific factual findings to support the two hallmarks were also essential for releases to pass muster.

[106] Behrmann v. Nat'l Heritage Found., 663 F.3d 704, 712 (4th Cir. 2011).

[107] *See* Bank, *supra* note 1, at 12.

[108] *See id.*

courts approve releases during plan confirmation, yet altering legal rights and obligations between non-debtors is a central Article III judicial function.[109] Article I bankruptcy courts are created not by the Constitution but by Congress, and their judges enjoy neither tenure during good behavior nor salary protection.[110] This gives bankruptcy judges less insulation from congressional influence and invites them to make decisions they ought not make. When bankruptcy courts exercise Article III power, they chip away at Article III courts' authority, which can "create new boundaries from which legions of power can seek new territory to capture."[111]

A bankruptcy court's power to approve third-party releases hinges on its statutory and constitutional authority to enter final judgments on the releases. Part II.A outlines bankruptcy courts' statutory jurisdiction and distinguishes "core" from "non-core" proceedings. Part II.B discusses how the core versus non-core designation affects the bankruptcy court and the parties in a case. Part II.C highlights the statutory limits on bankruptcy courts' power to enter a final judgment. Part II.D analyzes *Stern v. Marshall*, which imposes constitutional limits on bankruptcy courts' authority to enter final judgment by setting forth two related doctrines: the "public rights exception" and the "integral to the restructuring" test. Finally, Part II.E compares how various courts have interpreted and applied these two related doctrines in the context of third-party releases.

A. Bankruptcy Jurisdiction and the Core v. Non-Core Distinction

A bankruptcy court's ability to approve third-party releases depends on the court's jurisdiction and power to enter judgment. District courts have original, non-exclusive jurisdiction over all civil proceedings under the Code.[112] But every district court in the country has referred most of that jurisdiction to bankruptcy courts,[113] which act as units of the district court.[114] Once a case lands in bankruptcy court, every proceeding before it is designated either "core" or

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[109] *See* Stern v. Marshall, 564 U.S. 462, 494–95 (2011).

[110] *Compare* U.S. CONST. art. I § 8, *with* U.S. CONST. art. III § 1.

[111] *Stern*, 564 U.S. at 502–03 (quoting Reid v. Covert, 354 U.S. 1, 39 (1957) (plurality opinion)).

[112] 28 U.S.C. § 1334(b).

[113] *See* 28 U.S.C. § 157(a); Schulman v. Cal. Water Res. Control Bd. (*In re* Lazar), 200 B.R. 358, 366 (Bankr. C.D. Cal. 1996) ("[E]ach district is authorized to adopt a general order of reference to send all bankruptcy cases to the bankruptcy judges for the district, and in fact all districts (including this district) have so ordered.").

[114] 28 U.S.C. § 151.

"non-core."[115] "It is the bankruptcy court's responsibility to determine whether each claim before it is core or non-core."[116]

In core proceedings, bankruptcy judges have the power to "enter appropriate orders and judgments," subject only to appellate review.[117] Once a bankruptcy judge has entered a final judgment or order, the parties can appeal it to the district court for the judicial district in which the bankruptcy judge is serving.[118] On that appeal, the bankruptcy court's legal conclusions are reviewed de novo[119] but its findings of fact cannot be set aside unless clearly erroneous.[120]

Non-core proceedings are different. If a non-core proceeding arises in a bankruptcy case, then (assuming it is related to the case)[121] the bankruptcy court may hear it but may not enter a final judgment or order on it.[122] Instead, the bankruptcy court must submit proposed findings of fact and conclusions of law to the district court, which then reviews both de novo.[123] Then, the district judge enters a final judgment or order.[124] Thus, in non-core proceedings the district court's standard of review is "far less deferential,"[125] and bankruptcy judges have a "restricted jurisdiction [that] is akin to that of a federal magistrate."[126]

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115 *E.g.*, *In re* Purdue Pharma, L.P., 635 B.R. 26, 79 (S.D.N.Y. 2021).

116 Exec. Benefits Ins. Agency v. Arkison, 573 U.S. 25, 33 (2014).

117 28 U.S.C. § 157(b)(1).

118 28 U.S.C. § 158(a). Interestingly, Title 28 also allows parties to appeal final judgments and orders from the bankruptcy court to an appellate panel of three bankruptcy judges, or even directly to a court of appeals, provided that certain other statutory requirements are met. *See* 28 U.S.C § 158(b)(1), (d)(1).

119 Rubenstein v. Ball Bros., Inc. (*In re* New Eng. Fish Co.), 749 F.2d 1277, 1280 (9th Cir. 1984).

120 FED. R. BANKR. P. 7052. The Federal Rules of Bankruptcy Procedure reflect the normal standard of review on appeals in district court litigation. FED. R. CIV. P. 52(a)(6).

121 Non-core proceedings come in two flavors: those that are "related to" a Title 11 case, and those that are not. 28 U.S.C. § 157(c)(1). Courts have broadly defined non-core proceedings that are "related to" a Title 11 case as those whose "outcome . . . could conceivably have *any* effect on the estate being administered in bankruptcy." Pacor, Inc. v. Higgins, 743 F.2d 984, 994 (3d Cir. 1984) (emphasis added); *see also* Celotex Corp. v. Edwards, 514 U.S. 300, 308 (1995) (affirming this "related to" definition from *Pacor*). If a non-core proceeding falls short of this definition, it is therefore not "related to" the bankruptcy case and there is no bankruptcy jurisdiction to hear it at all. *See* 28 U.S.C. § 1334(b).

122 28 U.S.C. § 157(c)(1). However, the bankruptcy court can enter final judgment on non-core matters if the parties consent. To do so, parties must be made aware of the need for consent and the right to refuse it, but still voluntarily appear to try their case in bankruptcy court. Wellness Int'l Network, Ltd. v. Sharif, 575 U.S. 665, 685 (2015).

123 The district court only reviews de novo "those matters to which any party has specifically and timely objected." 28 U.S.C. § 157(c)(1).

124 *Id.*

125 *In re* Purdue Pharma, L.P., 635 B.R. 26, 79 (S.D.N.Y. 2021).

126 TABB & BRUBAKER, *supra* note 25, at 861.

B. Effects of the Core v. Non-Core Distinction

Several repercussions arise from a bankruptcy court's finding that a given proceeding, like chapter 11 plan confirmation, is core or non-core. The main difference between core and non-core proceedings is that in the former, the bankruptcy court can enter a final judgment and its findings of fact get deference on appeal, while in the latter, it cannot enter a final judgment and its findings of fact get no deference.[127] This simple distinction influences a case's efficiency, and affected litigants have limited means of challenging the decision.

As to case efficiency, in non-core proceedings the district court must be the one to enter final judgment. The district court may do so either by de novo review of the bankruptcy court's findings or by preemptively "withdrawing" jurisdiction from the bankruptcy court on a motion or sua sponte.[128] Either way, when non-core proceedings splinter off from the bankruptcy case to district court, it can engender delays, costly withdrawal motions, and confusion as interconnected matters progress in two forums.[129] When Congress created bankruptcy jurisdiction, it believed that having a single court decide all cases based on the same circumstances would be most efficient.[130]

As to litigants' ability to challenge a core or non-core determination, bankruptcy courts can enter final judgments on core matters, which are afforded preclusive effect against later litigants.[131] And bankruptcy courts cannot enter final judgments on non-core matters.[132] Yet most circuits hold that bankruptcy court orders on proceedings that are later deemed non-core get preclusive effect when litigants collaterally attack those orders.[133] Thus, if a party wants to

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[127] *See* 28 U.S.C. § 157(b)(1), (c)(1); FED. R. BANKR. P. 7052; FED. R. CIV. P. 52(a)(6); Rubenstein v. Ball Bros., Inc. (*In re* New Eng. Fish Co.), 749 F.2d 1277, 1280 (9th Cir. 1984).

[128] *See* 28 U.S.C. § 157(d). An overwhelming majority of courts hold that a district court's withdrawal authority is permissive, not mandatory. 1 COLLIER ON BANKRUPTCY ¶ 3.04[1][b] (16th ed. 2022). To save time in non-core proceedings, a district court may be more likely to withdraw jurisdiction and adjudicate matters itself because otherwise it would have to do a subsequent de novo review of the bankruptcy court's findings. Orion Pictures Corp. v. Showtime Networks, Inc. (*In re* Orion Pictures Corp.), 4 F.3d 1095, 1101 (2d Cir. 1993).

[129] *See* Brief of Petitioner at 35–36, Stern v. Marshall, 564 U.S. 462 (2011) (No. 10-179), 2010 WL 4688124; *see also* Brief for the United States as Amicus Curiae Supporting Petitioner at 29–30, Stern v. Marshall, 564 U.S. 462 (2011) (No. 10-179), 2010 WL 4717271.

[130] Fang Operators v. Carpenter (*In re* Fang Operators), 158 B.R. 643, 647 (Bankr. N.D. Tex. 1993).

[131] *Cf.* Grella v. Salem Five Cent Sav. Bank, 42 F.3d 26, 30 (1st Cir. 1994).

[132] 28 U.S.C. § 157(c)(1).

[133] *See, e.g.*, Plotner v. AT&T Corp., 224 F.3d 1161, 1172–74 (10th Cir. 2000); Robertson v. Isomedix, Inc. (*In re* Int'l Nutronics, Inc.), 28 F.3d 965, 969–70 (9th Cir. 1994); Sanders Confectionery Prods., Inc. v. Heller Fin., Inc., 973 F.2d 474, 483 (6th Cir. 1992); Sure-Snap Corp. v. State St. Bank & Tr. Co., 948 F.2d 869, 873–77 (2d Cir. 1991).

challenge some bankruptcy court order on the grounds that its operative proceeding is non-core, they must appeal that order during the case or risk forfeiting the chance to ever challenge it.[134]

To add insult to injury, litigants' power to challenge a core or non-core determination often worsens in complex chapter 11 bankruptcies due to the "equitable mootness" doctrine.[135] If applicable, equitable mootness blocks appellate review of a chapter 11 plan confirmation to "prevent a court from unscrambling complex bankruptcy reorganizations when the appealing party should have acted before the plan became extremely difficult to retract."[136] So, when a debtor confirms a chapter 11 plan, objecting parties may be unable to appeal plan confirmation even if the plan has non-core aspects to it.[137]

C. Statutory Definitions of Core and Non-Core Proceedings

Understanding the core versus non-core distinction is the first step in gauging a bankruptcy court's power, but other questions arise. Who decides which matters are core or non-core? How do they do so? As noted, the bankruptcy court determines whether each claim before it is core or non-core,[138] but Congress has enacted other statutory guidance for that determination.

Title 28 of the United State Code pertains to the "Judiciary and Judicial Procedure," and Part IV of that title addresses "Jurisdiction and Venue."[139] There, Congress included a non-exhaustive list of core proceedings that bankruptcy courts may hear and enter final judgment on.[140] According to the statute, core proceedings include "matters concerning the administration of the estate," "counterclaims by the estate against persons filing claims," and, most

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[134] A bankruptcy court's determination of whether a proceeding is core or non-core is an appealable interlocutory order. 1 COLLIER ON BANKRUPTCY ¶ 3.02[6][a] (16th ed. 2022). The fact that such determinations are appealable notwithstanding, creditors seeking to appeal them must have appropriate appellate standing. Unlike in normal civil litigation, which typically concerns only a plaintiff and a defendant, bankruptcy orders can affect numerous parties in a case. Appellate standing in bankruptcy thus requires that an entity be one whose "rights or interests are 'directly and adversely affected pecuniarily' by the order or decree of the bankruptcy court." *In re* El San Juan Hotel, 809 F.2d 151, 154 (1st Cir. 1987) (quoting Fondiller v. Robertson (*In re* Fondiller), 707 F.2d 441, 442 (9th Cir. 1983)).

[135] *In re* One2One Commc'ns, LLC, 805 F.3d 428, 434 (3d Cir. 2015).

[136] *Id.* (quoting Nordhoff Invs., Inc. v. Zenith Elecs. Corp., 258 F.3d 180, 185 (3d Cir. 2001)).

[137] *See generally In re* Millennium Lab Holdings, LLC, 945 F.3d 126 (3d Cir. 2019) (dismissing appeal of plan confirmation as equitably moot even though appellant challenged plan as having non-core aspects to it).

[138] Exec. Benefits Ins. Agency v. Arkison, 573 U.S. 25, 33 (2014).

[139] 28 U.S.C. §§ 1 *et seq.*

[140] 28 U.S.C. § 157(b).

notably, "confirmation of plans."[141] So, if a bankruptcy court confirms a chapter 11 plan, such confirmation will be a core proceeding under the statute.[142]

But most of Title 28's jurisdictional grants do not apply to third-party releases. This is because releases involve claims that are asserted neither by nor against the bankruptcy estate.[143] Because releases arise in chapter 11 plans, courts typically use the "confirmation of plans" clause as the requisite statutory authorization to approve the releases.[144]

D. Constitutional Limits on the Core v. Non-Core Inquiry: Stern v. Marshall

Statutory authorization does not always carry the day. True, a bankruptcy court's authority to approve third-party releases depends on its statutory power to enter judgment on them. But the Constitution often requires more; the Supreme Court imposed separation of powers limits on bankruptcy court authority in *Stern v. Marshall*.[145]

Stern's facts are somewhat dramatic. The debtor, Vickie Lynn Marshall,[146] was the widow of one of the richest men in Texas. The creditor, E. Pierce

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141 28 U.S.C. § 157(b)(2)(A), (C), (L).

142 *Cf.* 1 COLLIER ON BANKRUPTCY ¶ 3.02[3][a] (16th ed. 2022).

143 For example, Title 28 states that core proceedings include "allowance or disallowance of claims *against the estate*," "counterclaims *by the estate*," "orders to turn over *property of the estate*," and "proceedings affecting the liquidation of *assets of the estate* . . . ." § 157(b)(2)(B), (C), (E), (O) (emphasis added).

144 *See, e.g.*, *In re* Charles St. Afr. Methodist Episcopal Church of Bos., 499 B.R. 66, 99 (Bankr. D. Mass. 2013).

145 564 U.S. 462 (2011).

146 Readers may know Vickie Lynn Marshall by her stage name, Anna Nicole Smith. Smith was a supermodel who rose to stardom as a "Playmate" for the men's entertainment magazine, *Playboy*. She married billionaire James Howard Marshall in 1994 when she was twenty-six years old; Marshall was eighty-nine at the time. Unsurprisingly, the couple's massive gap in wealth (and in age) stirred controversy, especially among members of the Marshall family who were poised to inherit James's fortune. James Marshall died in 1995, and this legal battle for his inheritance ensued. *See generally The Life and Death of Anna Nicole Smith*, INSIDER (May 17, 2023, 8:15 PM), https://www.insider.com/anna-nicole-smith-life-death-2023-5.

Smith died in 2007 in the middle of the decade-long litigation for James's estate. In 2011, *Stern v. Marshall* made its second trip up to the Supreme Court. Perhaps the years of fighting, the winding procedural history, and the death of the original parties all unsettled Chief Justice John Roberts, who began the *Stern* opinion with a Dickens quote:

> This suit has, in course of time, become so complicated, that . . . no two . . . lawyers can talk about it for five minutes, without coming to a total disagreement as to all the premises. Innumerable children have been born into the cause: innumerable young people have married into it; and, sadly, the original parties have died out of it. A long procession of judges has come in and gone out during that time, and still the suit drags its weary length before the Court.

Stern v. Marshall, 564 U.S. 462, 468 (2011) (quoting CHARLES DICKENS, BLEAK HOUSE, *reprinted in* 1 WORKS OF CHARLES DICKENS 4–5 (1891)).

Marshall, was the man's son.[147] Before Vickie filed for bankruptcy, she publicly accused Pierce of fraudulently inducing her husband to exclude her from her husband's will.[148] After Vickie filed bankruptcy, Pierce filed a proof of claim for defamation to recover damages from Vickie's estate based on her public accusations.[149] Vickie counterclaimed for tortious interference under Texas law, alleging that Pierce "wrongfully prevented" her husband from taking the necessary steps to provide her with half of his property.[150]

The bankruptcy court concluded that Vickie's counterclaim was a core proceeding and entered final judgment in her favor for $425 million.[151] On appeal, the Supreme Court agreed that the counterclaim was a statutorily core proceeding but held that the bankruptcy court lacked the constitutional authority to enter judgment on it.[152] Although Vickie's counterclaim fit into Title 28's definition of "counterclaims by the estate against persons filing claims," the Supreme Court held that the bankruptcy court's judgment on her counterclaim violated the separation of powers.[153]

Article III of the Constitution requires that "[t]he judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish."[154] And judges of Article III courts have unique characteristics, including that they hold their offices during good behavior and that their salaries cannot be diminished.[155] Thus, because Congress created bankruptcy courts under Article I,[156] it generally may not "withdraw from judicial cognizance any matter which, from its nature, is the subject of suit at the common law" and give it to bankruptcy courts.[157] In other words, Congress generally cannot vest bankruptcy courts with adjudicatory power over common law-type claims between parties.[158]

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147 *Stern*, 564 U.S. at 468–69.
148 *Id.* at 470.
149 *Id.*
150 *Id.*
151 *Id.* at 470–71.
152 *Id.* at 482.
153 *See id.*
154 U.S. CONST. art. III, § 1.
155 *Id.*
156 *See* U.S. CONST. art. I, § 8, cl. 4 ("Congress shall have Power . . . [t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States.").
157 *Stern*, 564 U.S. at 484 (quoting Murray's Lessee v. Hoboken Land & Improvement Co., 59 U.S. 272, 284 (1856)).
158 *See id.*

The *Stern* Court contrasted two general types of claims. First, there are claims that are a matter of "private right," which arise from the liability of one individual to another under the law.[159] The Constitution assigns the resolution of that type of claim to the judicial branch.[160] Second, there are claims involving "public rights," which arise between individuals and the government in connection with the executive or legislative branches' performance of their functions.[161] The Constitution allows Congress to assign the resolution of that type of claim to legislative courts, like bankruptcy courts.[162]

Two related doctrines apply in determining whether a bankruptcy court can constitutionally enter a final judgment in a proceeding. The first doctrine says that bankruptcy courts can enter judgment on proceedings that satisfy a two-part test called the "public rights exception."[163] The second doctrine says that bankruptcy courts can enter judgment on proceedings that are "integral to the restructuring of the debtor-creditor relationship."[164]

1. The Public Rights Exception

The *Stern* Court began with the history of the public rights exception. The Court conceived of the exception in an 1856 case, *Murray's Lessee v. Hoboken Land & Improvement Co.*. There, a plaintiff claimed that a Treasury Department land sale was void because such sales were Article III judicial acts that were not assignable to the executive.[165] The *Murray's Lessee* Court held that Congress could assign judicial land sale power to the Treasury Department as a matter of "public right" because the plaintiff could not challenge the sale without Congress's approval. Congress would have to waive federal sovereign immunity.[166] At its inception then, the public rights exception meant Congress could "set the terms of adjudicating a suit when the suit could not otherwise proceed at all."[167]

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159 *Id.* at 489 (2011). The court also described private right claims as those "made of 'the stuff of the traditional actions at common law tried by the courts at Westminster in 1789'" that are "brought within the bounds of federal jurisdiction." *Id.* at 484 (quoting N. Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50, 90 (1982) (Rehnquist, J., concurring)).

160 *Stern*, 564 U.S. at 484.

161 *Id.* at 485.

162 *See id.*

163 *See id.* at 492, 499.

164 *Id.* at 497 (quoting Langenkamp v. Culp, 498 U.S. 42, 44 (1990) (per curiam)).

165 *Id.* at 488 (citing Murray's Lessee v. Hoboken Land & Improvement Co., 59 U.S. 272, 274–75 (1856)).

166 *Murray's Lessee*, 59 U.S. at 83–84.

167 *Stern*, 564 U.S. at 489.

The *Stern* Court clarified that it has "rejected the limitation of the public rights exception to actions involving the Government as a party."[168] Instead, as the exception evolved, it came to be limited to "cases in which the claim at issue [1] derives from a federal regulatory scheme, or [2] in which resolution of the claim by an expert Government agency is deemed essential to a limited regulatory objective . . . ."[169] After stating the exception's modern understanding, the Court elaborated that "it is still the case that what makes a right 'public' rather than private is that the right is integrally related to particular Federal Government action."[170] At this point, the reader would be right to be confused. Courts feel similarly.

To frame the public rights exception in the bankruptcy context, the *Stern* Court discussed its most recent application of the doctrine in the 1989 case, *Granfinanciera, S.A. v. Nordberg*.[171] There, a bankruptcy court approved a chapter 11 plan that vested the trustee with fraudulent conveyance actions against non-creditors.[172] The *Granfinanciera* Court found the fraudulent conveyance actions beyond the public rights exception's scope because such claims were not "closely intertwined with a federal regulatory program Congress has power to enact."[173] The exception did not apply because the fraudulent conveyance actions against non-creditors resembled "state law contract claims brought . . . to augment the bankruptcy estate," rather than resembling "creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res."[174]

The *Stern* Court reasoned that a bankruptcy court cannot adjudicate a matter just because that matter affects the bankruptcy case.[175] Rather, the public rights exception must apply. The key question for bankruptcy courts assessing their constitutional authority to adjudicate a claim must be "whether the action at issue [1] stems from the bankruptcy itself or [2] would necessarily be resolved in the claims allowance process."[176]

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168 *Id.* at 490.
169 *Id.*
170 *Id.* at 490–91.
171 492 U.S. 33 (1989).
172 Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 36 (1989). In *Granfinanciera*, the trustee alleged that the non-creditors had received $1.7 million from the debtor's corporate predecessor.
173 *Stern*, 564 U.S. at 492 (quoting *Granfinanciera*, 492 U.S. at 54–55).
174 *Id.* (quoting *Granfinanciera*, 492 U.S. at 54–55).
175 *Id.* at 499 ("Congress may not bypass Article III simply because a proceeding may have *some* bearing on a bankruptcy case . . . .").
176 *Id.*

To illustrate this two-part bankruptcy formulation of the public rights exception, the *Stern* Court discussed two of its other cases: *Katchen v. Landy*[177] and *Langenkamp v. Culp*.[178] Both cases involved a dispute of a bankruptcy court's authority to adjudicate voidable preference actions, claims under the Code that the trustee asserts to avoid certain transfers to creditors made in anticipation of bankruptcy.[179] If a creditor receives such a transfer from the debtor and then files a claim in her bankruptcy, the Code requires the bankruptcy court to disallow that claim.[180]

The *Stern* Court reasoned that the preferential transfers in *Katchen* and *Langenkamp* "stem[med] from the bankruptcy itself" because the trustees in both cases were "asserting a right of recovery *created by federal bankruptcy law*."[181] That is, the trustee's right of recovery existed because of the Code and thus it "deriv[ed] from a federal regulatory scheme."[182]

Similarly, the preferential transfers from both cases would "necessarily be resolved in the claims allowance process" because the bankruptcy courts in those cases *had to decide* the preferential transfer issues before determining whether the creditors' claims would be allowed.[183] The bankruptcy court had to adjudicate the preference claim to allow or disallow a claim against the debtor's estate, and so "resolution of the [preference] claim by an expert Government agency [was] deemed essential to a limited regulatory objective."[184] Therefore, because the transfers passed the public rights exception, the bankruptcy courts in both cases had authority to adjudicate the preferential transfers.[185]

Applying the two-part framework to the facts of the case at hand, the *Stern* Court concluded that the bankruptcy court lacked constitutional authority to adjudicate Vickie's tortious interference counterclaim against Pierce.[186] First,

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177 382 U.S. 323 (1966).

178 498 U.S. 42 (1990) (per curiam).

179 *See Katchen*, 382 U.S. at 325; *Langenkamp*, 498 U.S. at 43; 11 U.S.C. § 547(b).

180 11 U.S.C. § 502(d).

181 *Stern*, 564 U.S. at 498–99.

182 *See id.* at 490–91.

183 *See id.* at 496 (quoting *Katchen*, 382 U.S. at 334) (noting that, in *Katchen*, once the bankruptcy court "determine[ed] whether and to what extent to allow the creditor's claim," adjudicating the preference action in an Article III court "would be a meaningless gesture"); *cf. id.* at 497 (quoting *Langenkamp*, 498 U.S. at 45) (noting that, in *Langenkamp*, when "the creditor has not filed a proof of claim, the trustee's preference action does *not* 'become[] part of the claims-allowance process . . . .'").

184 *Id.* at 490.

185 *See id.* at 496–97.

186 *Id.* at 499 ("Vickie has failed to demonstrate that her counterclaim falls within one of the 'limited circumstances' covered by the public rights exception . . . .").

Vickie's counterclaim did not stem from the bankruptcy itself—it asserted a right of recovery created by Texas law, not federal bankruptcy law.[187] Second, Vickie's counterclaim would not necessarily be resolved in the claims allowance process—the bankruptcy court did not have to decide it to allow Pierce's defamation claim.[188]

In its concluding remarks, the *Stern* Court emphasized that the public rights exception applies in "limited circumstances."[189] When the public rights exception arguably covers a given matter, the presumption is for an Article III court to resolve it.[190]

2. *The "Integral to the Restructuring" Test*

The *Stern* Court hinted at the possibility of a separate doctrine. The Court listed the two situations in which the public rights exception generally applies, but then immediately followed: "[i]n other words, it is still the case that what makes a right 'public' rather than private is that the right is *integrally related to particular Federal Government action*."[191]

In turn, when the Court applied the public rights doctrine to bankruptcy, it noted that bankruptcy courts can constitutionally adjudicate claims when those claims become "*integral to the restructuring* of the debtor-creditor relationship."[192] The Court did not elaborate on what criteria qualify a claim as "integral to the restructuring." However, the Court did note that the preference action from *Langenkamp* was integral because it had "become[] part of the claims-allowance process . . . ."[193] The *Langenkamp* preference action was integral because the action's resolution determined whether the creditor's claim would be allowed.[194] In contrast, if the creditor had not filed a claim in the bankruptcy, the preference action would not have been integral.[195] Courts disagree on whether the *Stern* Court's mention of "integral to the restructuring" changes the two-part public rights exception as applied to third-party releases.

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[187] *Id.* ("Vickie's claim, in contrast, is in no way derived from or dependent upon bankruptcy law; it is a state tort action that exists without regard to any bankruptcy proceeding.").

[188] *See id.* at 497–98.

[189] *Id.* at 499.

[190] *Id.*

[191] *Id.* at 490–91 (emphasis added).

[192] *Id.* at 497 (quoting Langenkamp v. Culp, 498 U.S. 42, 44 (1990) (per curiam)) (emphasis added).

[193] *Id.* (quoting *Langenkamp*, 498 U.S. at 45).

[194] *See id.*; 11 U.S.C. § 502(d).

[195] *See Stern*, 564 U.S. at 497.

E. Conflicting Constitutional Analyses of Third-Party Releases

Courts disagree on two inquiries regarding the constitutional analysis of third-party releases. First, they disagree on whether the entire chapter 11 plan is a single operative proceeding, or instead whether each individual release is a separate operative proceeding for analysis.[196] Second, in applying *Stern*, courts disagree on whether they should use the two-part public rights exception or the "integral to the restructuring" test.[197] And courts using the "integral to the restructuring" test disagree on *how* to apply it.[198]

1. Defining the Operative Proceeding

In *Stern*, the Court did not need to define an operative proceeding for constitutional analysis. No parties in the case disputed that the operative proceeding was Vickie's counterclaim.[199] But when courts face third-party releases in chapter 11 plans, they must decide whether the plan itself is a single operative proceeding or whether each proposed release constitutes a separate proceeding requiring analysis.

The U.S. Bankruptcy Court for the District of Massachusetts took the former approach in *In re Charles St. African Methodist Episcopal Church of Boston.*[200] In the case, an incorporated church congregation filed for chapter 11 bankruptcy, and the bankruptcy court ruled that it had the constitutional authority to approve the church's plan that contained third-party releases.[201] One party argued that the court should define each release as a separate operative proceeding for constitutional analysis because "approval of [a] release is tantamount to adjudication" of its underlying state law dispute between non-debtors.[202]

The court disagreed. Instead, it defined the operative proceeding as the entire chapter 11 plan, reasoning that "[c]onfirmation of a plan is not an adjudication

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196 *Compare* Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641, 669 (E.D. Va. 2022) (requiring the bankruptcy court to treat each individual release as a separate operative proceeding), *with In re* Charles St. Afr. Methodist Episcopal Church of Bos., 499 B.R. 66, 99 (Bankr. D. Mass. 2013) (holding that only the chapter 11 plan itself was an operative proceeding).

197 *Compare In re* Purdue Pharma, L.P., 635 B.R. 26, 81 (S.D.N.Y. 2021) (applying the two-part public rights exception), *with In re* Millennium Lab Holdings II, LLC, 945 F.3d 126, 137–38 (2019) (applying only the "integral to the restructuring" test).

198 *See* Purdue Pharma, 635 B.R. at 81 (criticizing another court's interpretation of "integral to the restructuring").

199 *Stern*, 564 U.S. 462.

200 Charles St. Episcopal Church, 499 B.R. 66.

201 *Id.* at 99.

202 *Id.*

of the various disputes it touches upon . . . ."[203] The court said that the only matter before it was plan confirmation—the underlying claims between third parties were not truly in controversy.[204] Thus, the court concluded that it had the constitutional authority to approve the plan under the public rights exception from *Stern*.[205] The plan "stem[med] from the bankruptcy itself" because the plan could only exist under the Code, pursuant to federal bankruptcy law.[206]

The U.S. District Court for the Eastern District of Virginia took a different approach in *Patterson v. Mahwah Bergen Retail Group, Inc.*[207] A bankruptcy court had previously confirmed a corporation's plan that contained third-party releases, which absolved swaths of non-debtors' liability on creditors' claims.[208]

On appeal, the *Patterson* court vacated the plan. It held that the bankruptcy court lacked constitutional authority to approve the releases because it "did not parse the content of the claims that it purported to release to determine if each claim constituted a core claim [or] a non-core claim . . . ."[209] The *Patterson* court reasoned that the central teaching of *Stern* is that courts should focus on the content of a proceeding rather than its category.[210] In *Stern*, the Supreme Court did not label all counterclaims as core or non-core but analyzed the content of the counterclaim at issue to determine whether the bankruptcy court could constitutionally enter judgment on it.[211]

The *Patterson* court explained that Title 28 granted the bankruptcy court jurisdiction to confirm the chapter 11 plan.[212] But the content of that plan included third-party releases that absolved non-debtors of liability on creditors'

203 *Id.*
204 *See id.*
205 *Id.*
206 *See id.* at 99–100 (quoting Stern v. Marshall, 564 U.S. 462, 499 (2011)).
207 636 B.R. 641 (E.D. Va. 2022).
208 To illustrate, the plan provided that "Releasing Parties" had to "Release" claims against the "Released Parties." Even with drastic abridgment, substituting the terms yields: "[E]ach of the Consenting Stakeholders; . . . all holders of Impaired Claims who voted to accept the Plan; . . . all holders of Impaired Claims who abstained from voting on the Plan or voted to reject the Plan but did not timely opt out . . . [and others]" are "deemed to have released . . . any and all Causes of Action, whether known or unknown, including any derivative claims" against the debtor, its affiliates, and those affiliates' "current and former directors, managers, officers, investment committee members, special or other committee members, equity holders . . . affiliated investment funds or investment vehicles, managed accounts or funds, predecessors, participants, successors, assigns, subsidiaries, Affiliates, partners, limited partners, general partners, principals, members, management companies, fund advisors or managers, employees, agents, [and others]." *Patterson*, 636 B.R. at 657–59.
209 *Id.* at 669.
210 *Id.*
211 *Id.*
212 *Id.* at 671; *see* 28 U.S.C. §157(b)(2)(L).

claims. Those releases "became *res judicata* for subsequent parties trying to bring the claims," meaning later parties would be barred from pursuing the released claims.[213] The bankruptcy court could not "bypass constitutional limitations" by categorizing the released claims as core just because they resided in a plan whose confirmation was otherwise core under Title 28.[214] Instead, the bankruptcy court should have analyzed the content of the plan at issue to determine whether it could constitutionally enter judgment on each individual release.[215]

The U.S. District Court for the Southern District of New York adopted similar reasoning in *Purdue Pharma*.[216] There, a privately-held pharmaceutical company filed for chapter 11 bankruptcy, and the bankruptcy court confirmed its plan.[217] The plan contained broad third-party releases that absolved a universe of the company's affiliated entities of liability on creditors' claims.[218] The *Purdue* court held that the bankruptcy court incorrectly "concluded that the 'operative proceeding' for purposes of *Stern* analysis was the confirmation proceeding, not the underlying third-party claim[s]."[219]

The *Purdue* court reasoned that under *Stern*, not every issue litigated under the "umbrella of a core proceeding" de facto becomes "constitutionally core."[220] And nonconsensual third-party releases are essentially final judgments against the claimants.[221] Therefore, when a claimant is otherwise entitled to adjudication by an Article III court, that party does not "forfeit[] that constitutional right" simply because "the matter is disposed of as part of a plan of reorganization in bankruptcy."[222]

The *Purdue* court held that the bankruptcy court incorrectly assumed that the third-party releases were constitutional because they were litigated in the umbrella of plan confirmation, a core proceeding and central aspect of chapter 11.[223] And once the bankruptcy court entered the third-party releases in Purdue's plan, the releases had "adjudication effects, which is a key attribute of a final

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213 *Patterson*, 636 B.R. at 670 (emphasis in original).
214 *See id.* at 671.
215 *Id.* at 669.
216 *See In re* Purdue Pharma, L.P., 635 B.R. 26 (S.D.N.Y. 2021).
217 *Id.* at 35.
218 *Id.* at 36.
219 *Id.* at 81.
220 *Id.* at 80.
221 *Id.* at 82.
222 *Id.* at 80.
223 *Id.*

judgment."[224] The claimants were entitled to have their third-party claims adjudicated by an Article III court, regardless of Purdue's bankruptcy.[225] That the bankruptcy court ordered the releases in the context of plan confirmation did not alter this.[226]

2. *Applying Stern's Doctrines to the Operative Proceeding*

As mentioned, defining the operative proceeding is only half the battle. After choosing the operative proceeding, courts disagree on (1) whether to apply the public rights exception or the "integral to the restructuring" test to the proceedings and (2) if applying the "integral to the restructuring" test, how to do so.

In *In re Millennium Lab Holdings*, the Third Circuit applied the "integral to the restructuring" test.[227] In the case, a diagnostic services company filed for chapter 11 bankruptcy and included third-party releases in its plan.[228] The releases barred the company's creditors from suing its former shareholders, who in exchange agreed to pay $325 million to a settlement trust for the creditors.[229] The bankruptcy court approved the plan over a creditor's objection.[230] That creditor appealed to the Third Circuit and argued that the bankruptcy court lacked constitutional authority to approve the releases under *Stern*.[231]

The Third Circuit affirmed the plan confirmation, deeming the company's releases "integral to the restructuring of the debtor-creditor relationship."[232] The court reasoned that *Stern*'s "integral to the restructuring" test subsumes its two-part public rights exception, meaning that a claim may violate the public rights exception but still be integral.[233] The Third Circuit stated that bankruptcy courts may constitutionally decide claims that neither "stem from the bankruptcy itself"

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224 *Id.* at 82.
225 *Id.*
226 *Id.*
227 945 F.3d 126 (3d Cir. 2019). The Third Circuit addressed only the *Stern* constitutionality question before dismissing the remainder of the appeal as equitably moot.
228 *Id.* at 130–31.
229 *Id.* at 131.
230 *Id.* at 132.
231 *Id.* at 133.
232 *Id.* at 129, 135 (quoting Stern v. Marshall, 564 U.S. 462, 497 (2011)). Remember that this language from *Stern* arose during the Supreme Court's discussion of the preferential transfers in *Langenkamp*.
233 *See* Millennium, 945 F.3d at 136.

nor "would necessarily be resolved in the claims allowance process," so long as those claims are somehow "integral."[234]

Without citing any reasoning from *Stern*, the Third Circuit applied the "integral to the restructuring" test to the third-party releases in the case and found them integral because they "were absolutely required to induce [the third parties] to pay the funds needed to effectuate Millennium's settlement."[235] In other words, approving the company's releases was constitutional because without them—and without the shareholders' $325 million settlement contribution—the company's reorganization would have been impossible.[236]

In *Boy Scouts*, the U.S. Bankruptcy Court for the District of Delaware followed the Third Circuit's holding from *Millennium*.[237] As discussed above, the Boy Scouts filed for chapter 11 bankruptcy in the wake of hundreds of sexual abuse claims.[238] The Boy Scouts included a dizzying number of releases in its plan, which enjoined its creditors from suing its insurers, banks, law firms, mediators, and local troop councils.[239] The court approved the releases over creditors' dissents, noting that bankruptcy courts have constitutional authority to approve releases that are integral to the debtor-creditor relationship.[240] The court provided no reasoning as to why the Boy Scouts' releases were integral, but simply concluded that under *Millennium*, "the granting of third-party releases is still permissible."[241]

Other courts disagree with *Millennium*. The *Purdue* court, for example, rejected the "integral to the restructuring" test.[242] There, a pharmaceutical company included broad third-party releases in its chapter 11 plan that enjoined creditors' "non-derivative" state-law claims against the company's shareholders.[243] "Non-derivative" claims are those where the shareholders' liability arises out of their *own* misconduct.[244] In contrast, "derivative" claims

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[234] *See Id.* at 136, 138 ("[T]he reason bankruptcy courts may adjudicate matters arising in the claims-allowance process is because those matters are integral to the restructuring of debtor-creditor relations, not the other way around.").
[235] *Id.* at 137.
[236] *See id.*
[237] *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504 (Bankr. D. Del. 2022).
[238] *Id.* at 525, 533; *see supra* text accompanying note 16.
[239] *See* Boy Scouts' Third Modified Fifth Amended Plan of Reorganization, *supra* note 36, at Art. I(A) ¶ 50, Art. I(A) ¶ 245, Art. IX(B) ¶ 3, Art. X(J)(1)(a).
[240] Boy Scouts, 642 B.R. at 588–89.
[241] *Id.* at 594.
[242] 635 B.R. 26 (S.D.N.Y. 2021).
[243] *Id.* at 85–86.
[244] *Id.* at 91.

are those where liability arises out of the *company's* misconduct and is imputed onto a party because of their status as a company manager.[245] Without providing any reasoning, the bankruptcy court confirmed the company's plan over dissenting creditors and followed *Millennium*'s holding that non-derivative third-party releases are constitutional if they are, somehow, "integral to the restructuring."[246]

The *Purdue* court vacated plan confirmation.[247] It criticized the bankruptcy court for applying the "integral to the restructuring" test rather than the public rights exception.[248] The court held that under *Stern*, bankruptcy courts can confirm third-party releases only if the underlying claims "[1] stem[] from the bankruptcy itself or [2] would necessarily be resolved in the claims allowance process."[249] The court noted that *Stern* precludes bankruptcy courts from entering judgment on claims that exist prior to and independent of the debtor's bankruptcy, like state-law claims between non-debtors.[250] The *Purdue* court concluded that the company's non-derivative releases failed both prongs of the public rights exception but noted that the bankruptcy court had the power to approve the derivative releases.[251]

III. SOLUTIONS MOVING FORWARD: APPLYING *STERN* TO THIRD-PARTY RELEASES

Third-party releases implicate bankruptcy's core policies, the Code, and the constitutional right to due process. So, why should bankruptcy courts analyze third-party releases using the separation of powers doctrine? There are two interrelated reasons.

245 *Id.* at 90–91 (quoting MacArthur Co. v. Johns-Manville Corp., 837 F.2d 89, 93 (2d Cir. 1988)). Derivative liability is not limited to a company's shareholders. Rather, derivative liability attaches to a company's managers, e.g., its directors, officers, or other persons that breach duties that they owe to their company. *See generally Shareholder Derivative Suit*, CORNELL L. SCH., https://www.law.cornell.edu/wex/shareholder_derivative_suit (last visited Dec. 31, 2023). Because Purdue is a closely-held company, its shareholders manage it. *See* Purdue Pharma, 635 B.R. at 40.

246 *See* Purdue Pharma, 635 B.R. at 81.

247 *Id.* at 118.

248 *Id.* at 81.

249 *Id.* (quoting Stern v. Marshall, 564 U.S. 462, 499 (2011)).

250 *See id.* at 80.

251 *Id.* at 80, 81.

The first reason is somewhat obvious: the Constitution mandates separation of powers and is the supreme law of the land.[252] Bankruptcy courts are duty bound to follow it.[253] Thus, if a party in a chapter 11 case proves that the bankruptcy court will violate the separation of powers by entering judgment on a matter, the court may not enter that judgment.[254] Mass tort debtors are increasingly proposing third-party releases.[255] Now more than ever, bankruptcy courts need concrete standards to determine whether entering judgment on releases violates the separation of powers.[256]

The second, more functional, reason to apply a separation of powers framework is that the doctrine solves other problems with third-party releases.[257] Without separation of powers, the judiciary transforms from a "guardian of individual liberty" into "wishful thinking."[258] As recent mass tort bankruptcies exemplify, third-party releases pose a danger to bankruptcy policy, statutory interpretation of the Code, and due process. This would not be so if separation of powers was applied appropriately.

As to bankruptcy policy, chapter 11's goal is to help debtors reorganize rather than liquidate, to continue operating rather than wind up.[259] True, when a debtor proposes releases in its plan, the released third parties often contribute funds that help the debtor reorganize.[260] But those same releases effectively reorganize the third parties too, and these third parties latch onto the debtor's bankruptcy and reap the benefits of bankruptcy law.[261] The separation of powers framework proposed below will ensure that releases have a close connection to the debtor's reorganization. That close connection will prevent releases from

252 *See* U.S. CONST. art. IV, cl. 2. *See generally Separation of Powers and Checks and Balances*, CONST. ANN., https://constitution.congress.gov/browse/essay/artI-S1-3-1/ALDE_00013290/ (last visited Dec. 31, 2023).

253 *See* 28 U.S.C. § 453 (reciting oath that all judges must take before performing duties of their office and noting that they must swear to "administer justice . . . *under the Constitution* . . . .") (emphasis added).

254 *See generally Stern*, 564 U.S. 462.

255 *See supra* notes 36–37 and accompanying text.

256 Regardless of their approaches, many courts recognize that third-party releases raise a separation of powers issue. *See generally In re* Millennium Lab Holdings II, LLC, 945 F.3d 126 (3d Cir. 2019); Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641 (E.D. Va. 2022); Purdue Pharma, 635 B.R. 26; *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504 (Bankr. D. Del. 2022); *In re* Charles St. Afr. Methodist Episcopal Church of Bos., 499 B.R. 66 (Bankr. D. Mass. 2013).

257 LAWSON, *supra* note 50, at 102.

258 *Stern*, 564 U.S. at 495.

259 *See* Tabb, *supra* note 27, at 560.

260 *See* Cutler, *supra* note 8.

261 *See* Simon, *supra* note 31, at 1202.

inappropriately reorganizing third parties and will limit the benefits of chapter 11 to debtors who have filed for it.

As discussed in Part I, the circuits split on whether the Code permits nonconsensual third-party releases. Most circuits say that the Code allows releases but cannot agree on why.[262] The majority of circuits rely on bankruptcy courts' nebulous equitable powers under section 105(a) to approve releases.[263] And no Code provisions directly address whether bankruptcy courts can approve releases in a given case, so each circuit uses different criteria to answer the question.[264] Separation of powers cannot answer whether the Code permits releases and cannot change the Code's text.[265] But separation of powers can at least give all the circuits a constitutional minimum that releases must meet for a bankruptcy court to approve them.

Finally, third-party releases raise due process problems. When releases are overbroad and nonconsensual, creditors may lose their rights to adequate notice and the opportunity to be heard.[266] Separation of powers cannot change the Code's chapter 11 cramdown provisions, which allow bankruptcy courts to confirm plans over dissenting creditors.[267] But the separation of powers framework proposed below will deter debtors from proposing overbroad releases and will protect creditors' right to adequate notice.

This Comment proposes the following framework. When a bankruptcy court faces third-party releases during chapter 11 plan confirmation, *Stern* requires the court to engage in constitutional analysis. In that analysis, the bankruptcy court should treat each proposed release as a separate operative proceeding rather than treating the plan as a single operative proceeding. Next, the bankruptcy court should apply the public rights exception to each proposed release. In so doing, the bankruptcy court should presume that it lacks constitutional authority to approve the releases, and the debtor should bear the burden of proving that the bankruptcy court can constitutionally enter judgment on the releases.

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[262] *See supra* Part I.B.2.

[263] *See supra* text accompanying notes 79–82.

[264] Etkin & Brown, *supra* note 7, at 26.

[265] Ultimately, Congress must clarify whether the Code permits third-party releases. In 2021, the House Committee on the Judiciary's Subcommittee on Antitrust, Commercial, and Administrative Law proposed legislation that would effectively bar nonconsensual third-party releases. But the legislation is still pending. *See generally* Nondebtor Release Prohibition Act of 2021, H.R. 4777, 117th Cong. (2021).

[266] Mullane v. Cent. Hanover Bank & Tr. Co., 339 U.S. 306, 313–14 (1950).

[267] *See supra* notes 65–67 and accompanying text.

A. *Third-Party Releases Require Constitutional Analysis Under* Stern

Bankruptcy courts must engage in constitutional analysis when assessing third-party releases. Title 28 of the United States Code grants bankruptcy courts statutory jurisdiction over "confirmation of plans."[268] The statute thus categorizes plan confirmation as a core proceeding.[269] Yet *Stern* requires that bankruptcy courts look beyond a proceeding's category and instead assess whether the proceeding's content complies with the separation of powers.[270]

Stern applies to claims that are "designated for final adjudication in the bankruptcy court as a statutory matter, but [are] prohibited from proceeding in that way as a constitutional matter . . . ."[271] In *Stern*, the Supreme Court expressly held that Vickie's counterclaim fell into Title 28's grant of bankruptcy jurisdiction and that her counterclaim was statutorily core.[272] Yet the Court engaged in constitutional analysis to determine whether the content of Vickie's counterclaim rendered it outside the bankruptcy court's adjudicative authority.[273]

During chapter 11 plan confirmation, bankruptcy courts must look beyond the "plan confirmation" label and instead evaluate plans' content for third-party releases.[274] Even when a plan is designated for final adjudication in the bankruptcy court as a statutory matter, releases may prohibit a plan's final adjudication as a constitutional matter.[275] Like the *Stern* Court, bankruptcy courts must engage in constitutional analysis to determine whether a plan's releases render the plan outside the bankruptcy court's adjudicative power.[276]

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[268] 28 U.S.C. § 157(b)(2)(L).

[269] *Id.*

[270] *See* Stern v. Marshall, 564 U.S. 462, 482 (2011) (holding counterclaim unconstitutional despite the bankruptcy court having statutory subject matter jurisdiction under Title 28); Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641, 669 (E.D. Va. 2022).

[271] *Patterson*, 636 B.R. at 668 (quoting Exec. Benefits Ins. Agency v. Arkison, 573 U.S. 25, 35–36 (2014)).

[272] *Stern*, 564 U.S. at 482.

[273] *Id.* at 482–501.

[274] 28 U.S.C. § 157(b)(2)(L); *Stern*, 564 U.S. at 482.

[275] *See Stern*, 564 U.S. at 482.

[276] If a bankruptcy court determines that third-party releases do, in fact, render a plan's confirmation outside the court's adjudicative power, the court has two options. First, it could reject confirmation entirely. Second, it could sever the troublesome releases and confirm the remaining plan, though this could frustrate the plan's effects. Severing could also "pull the rug" out from parties who voted for one plan but received another without notice. Thoughtful debtors can include non-severability clauses in their proposed plans to avoid this second result.

B. *Bankruptcy Courts Should Analyze Each Third-Party Release Individually, as Separate Operative Proceedings*

When bankruptcy courts engage in constitutional analysis, they should treat each third-party release as a separate operative proceeding rather than treating the entire chapter 11 plan as a single proceeding. Bankruptcy courts often fail to assess their constitutional authority to adjudicate each released claim in a plan.[277] They often fail to do so on the theory that the plan itself is the operative proceeding, rather than the released claims.[278] In the words of the *Charles St. Episcopal Church* court: "the matter before the Court is the confirmation of a plan, a unitary omnibus civil proceeding for the reorganization of all obligations of the debtor and disposition of all its assets. *Confirmation of a plan is not an adjudication of the various disputes it touches upon* . . . ."[279]

This reasoning misses the mark. When a bankruptcy court confirms a chapter 11 plan that contains third-party releases, it extinguishes those claims.[280] Plan confirmation is a statutorily "core" proceeding that acts as a final judgment.[281] As the *Purdue* court said, "[a] nonconsensual third-party release is essentially a final judgment against the claimant, in favor of the non-debtor, entered 'without any hearing on the merits.'"[282] A confirmed plan—and every release in it—has preclusive effect on later litigants.[283] Most circuits give preclusive effect even to plans that are retroactively deemed non-core or unconstitutional.[284]

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277 *See In re* Millennium Lab Holdings II, LLC, 575 B.R. 252, 271 (Bankr. D. Del. 2017) ("[T]he operative proceeding for purposes of a constitutional analysis is confirmation of a plan. Confirmation of a plan is not a 'claim' or 'counterclaim.' It is not an 'action' as the word is used in *Stern*."), *aff'd*, 591 B.R. 559 (D. Del. 2018), *aff'd*, 945 F.3d 126 (3d Cir. 2019); *In re* Purdue Pharma, L.P., 633 B.R. 53, 99–100 (Bankr. S.D.N.Y.) (holding that "a Chapter 11 *plan* that contains a third-party claims release" is "'constitutionally core' under *Stern*") (emphasis added) (quotations omitted), *vacated*, 635 B.R. 26 (S.D.N.Y. 2021).

278 *See* Millennium, 575 B.R. at 271–72.

279 *In re* Charles St. Afr. Methodist Episcopal Church of Bos., 499 B.R. 66, 99 (Bankr. D. Mass. 2013) (emphasis added).

280 *See* Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641, 671 (E.D. Va. 2022) (holding that "the Bankruptcy Court extinguished the Released Claims, which amounts to adjudication of the claim for *Stern* purposes."); *see also* Millennium, 945 F.3d at 137 n.10 (expressing doubt that bankruptcy courts can constitutionally adjudicate releases merely because they appear in a chapter 11 plan).

281 28 U.S.C. § 157(b)(2)(L).

282 Purdue Pharma, 635 B.R. at 82 (quoting *In re* Aegean Marine Petrol. Network Inc., 599 B.R. 717, 725 (Bankr. S.D.N.Y. 2019)).

283 *See* Grella v. Salem Five Cent Sav. Bank, 42 F.3d 26, 30 (1st Cir. 1994); *Patterson*, 636 B.R. at 671.

284 Though not all circuits have applied this reasoning to the collateral attack of a chapter 11 plan confirmation, they have applied the reasoning to other proceedings that were retroactively deemed non-core. *See, e.g.*, Plotner v. AT&T Corp., 224 F.3d 1161, 1172–74 (10th Cir. 2000); Robertson v. Isomedix, Inc. (*In re* Int'l Nutronics, Inc.), 28 F.3d 965, 969–70 (9th Cir. 1994); Sanders Confectionery Prods., Inc. v. Heller

Because each third-party release is a final judgment on its underlying claim, bankruptcy courts should follow the *Patterson* court's approach by treating each release as a separate operative proceeding for constitutional analysis.[285] Treating the entire chapter 11 plan as the sole operative proceeding makes little constitutional sense. Doing so would allow parties to manufacture a bankruptcy court's constitutional authority to adjudicate any otherwise non-core matter simply by inserting it into a plan.[286]

C. When Bankruptcy Courts Analyze Each Individual Release, They Should Apply the Public Rights Exception

Bankruptcy courts should analyze each release to see if the underlying claim either "[1] stems from the bankruptcy itself or [2] would necessarily be resolved in the claims allowance process."[287] Two principles require courts to use the public rights exception and not the "integral to the restructuring" test.

First, the public rights exception has precedential value. Although the exception has evolved, the Supreme Court has consistently used it to determine when other branches of government may exercise Article III power.[288] At its inception in 1856, the public rights exception meant that Congress could set the terms of adjudicating suits when those suits could not otherwise proceed at all.[289] It follows then, that the exception now applies to "cases in which the claim at issue derives from a federal regulatory scheme," like when the claim at issue "stems from the bankruptcy itself."[290] Congress can set the terms of adjudicating suits where the claims derive from the Code because without the Code, there would be no claims.

Other precedents employ the exception too. The Supreme Court has said that Article I courts can adjudicate suits where the claims at issue are "closely intertwined" with one of Congress's federal regulatory programs.[291] In bankruptcy, it is not enough that claims merely augment the estate to be

Fin., Inc., 973 F.2d 474, 483 (6th Cir. 1992); Sure-Snap Corp. v. State St. Bank & Tr. Co., 948 F.2d 869, 873–77 (2d Cir. 1991).

285 *See Patterson*, 636 B.R. at 669.

286 Purdue Pharma, 635 B.R. at 80.

287 Stern v. Marshall, 564 U.S. 462, 499 (2011).

288 *See* Murray's Lessee v. Hoboken Land & Improvement Co., 59 U.S. 272, 284 (1856); Crowell v. Benson, 285 U.S. 22, 50 (1932); N. Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50, 89–90 (1982) (Rehnquist, J., concurring); *cf.* Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 36, 51–52 (1989).

289 *Stern*, 564 U.S. at 489.

290 *Id.* at 490, 499.

291 *See Granfinanciera*, 492 U.S. at 54–55.

considered within a bankruptcy court's adjudicative authority.[292] Rather, as the *Granfinanciera* Court said, claims should resemble "creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res."[293] Thus, the public rights exception extends to claims that "would necessarily be resolved in the claims allowance process."[294]

Second, "integral to the restructuring" is not the standard that the Supreme Court outlined in *Stern*. In fact, "integral to the restructuring" is a mere description of claims that satisfy the public rights exception. In *Stern*, the Court articulated the two-part public rights exception then said *in the very next sentence* that "[i]n other words, it is still the case that what makes a right 'public' rather than private is that the right is *integrally related to particular Federal Government action*."[295] Saying that a claim satisfies the two-part test is synonymous with saying that a claim is integrally related to particular federal government action.[296]

The *Stern* Court traced the public rights exception's history.[297] Yet the *Stern* Court only once used the phrase "integral to the restructuring," during its discussion of *Langenkamp*.[298] The Court gave no criteria for assessing when claims are integral.[299] It said only that *Langenkamp*'s preference action was integral because that action had "become[] part of the claims-allowance process."[300] The preference action was integral because it satisfied the public rights exception. If "integral to the restructuring" were some new standard, the Supreme Court would be ignoring years of precedent for a "test" that it mentioned once, provided no criteria for, and found satisfied only when a claim also satisfied the public rights exception. There is no new standard.

The Third Circuit misinterpreted "integral to the restructuring" in *Millennium*. There, the court said the third-party releases in the case were integral because they were "absolutely required to induce [the third parties] to

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292 *Id.*
293 *Id.* at 56.
294 *See Stern*, 564 U.S. at 499.
295 *Id.* at 490–91 (emphasis added).
296 *See* Lynch v. Lapidem Ltd. (*In re* Kirwan Offs. S.A.R.L), 592 B.R. 489, 510–11 (S.D.N.Y. 2018) (applying the two-part test to determine whether the third-party releases at issue were "constitutionally core, *i.e.*, ones that are . . . 'integral to the restructuring of the debtor-creditor relationship.'").
297 *See Stern*, 564 U.S. at 488–93 (2011).
298 *Id.* at 497.
299 *See id.*
300 *Id.* (quoting Langenkamp v. Culp, 498 U.S. 42, 45 (1990) (per curiam)).

pay the funds needed to effectuate Millennium's settlement . . . ."[301] But the Supreme Court never mentioned inducing third parties. The Third Circuit's interpretation sidesteps the Supreme Court's separation of powers jurisprudence. Moreover, such an interpretation conflicts with bankruptcy's "fresh start" principle, which encourages the law to help debtors, not third parties, emerge anew from financial hardship.[302] If third parties would like to receive the benefits of bankruptcy, they must file a petition themselves.

And the Third Circuit's interpretation is overbroad because it allows bankruptcy courts to approve third-party releases simply because reorganization financers demand them.[303] Recent mass tort bankruptcies exemplify this phenomenon. In *Boy Scouts*, the bankruptcy court followed *Millennium*, gave no reasoning, and found the releases in the case integral because the released insurers and troop councils paid $2.4 billion to a forced settlement trust.[304] And in *Purdue*, the bankruptcy court followed *Millennium*, again gave no reasoning, and found the releases at issue integral because the released parties paid $4.325 billion to a forced settlement trust.[305] This process sacrifices constitutionality for function. It cannot continue.

For a third-party release to pass constitutional muster, its underlying claim must either (1) stem from the bankruptcy itself or (2) necessarily be resolved in the claims-allowance process.[306] Releases will rarely, if ever, stem from the bankruptcy itself because the underlying claims rarely assert rights of recovery created by the Code.[307] Released third-party claims normally derive from state law rights of recovery, like tort actions.[308] Even when a released claim asserts a federal law cause of action, the Code must create that cause of action for it to

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301 *In re* Millennium Lab Holdings II, LLC, 945 F.3d 126, 137 (3d Cir. 2019) ("Restructuring in this case was only possible because of the release provisions.").

302 *See generally* Jackson, *supra* note 28.

303 *See* Millennium, 945 F.3d at 139 (addressing the appellant's "floodgate" argument that the "integral to the restructuring" standard is overbroad). The Third Circuit itself conceded that the appellant's arguments concerning the overbreadth of its "integral to the restructuring" interpretation were not without force.

304 *See In re* Boy Scouts of America and Del. BSA, LLC, 642 B.R. 504, 594, 602 (Bankr. D. Del. 2022).

305 *See In re* Purdue Pharma, L.P., 635 B.R. 26, 69–70 (S.D.N.Y. 2021).

306 Stern v. Marshall, 564 U.S. 462, 499 (2011).

307 *See id.* ("Vickie's claim, in contrast, is in no way derived from or dependent upon bankruptcy law; it is a state tort action . . . .").

308 *See, e.g.*, *supra* notes 186–87 and accompanying text.

pass this prong.[309] The preference actions from *Katchen* and *Langenkamp* exemplify Code-derived causes of action that stem from the bankruptcy.[310]

For releases to be necessarily resolved in the claims-allowance process, the bankruptcy court would have to decide the underlying third-party claim to determine whether a creditor's claim against the debtor is allowed.[311] This prong is met when a released claim is "closely intertwined" with a creditor's claim against the debtor.[312] Suppose a release is "derivative," like those from *Purdue*.[313] In that situation, the third-party claim arises out of the debtor's misconduct and is imputed onto the third party only by the third party's status.[314] If a bankruptcy court allowed a creditor's claim against the debtor based on the debtor's misconduct, the court would necessarily decide the third-party claim derivative of the same misconduct.[315] Thus, derivative releases are necessarily resolved in the claims-allowance process.

D. In Applying the Public Rights Exception, Bankruptcy Courts Should Presume That They Cannot Approve Third-Party Releases

Although the public rights exception should apply, its implementation is tricky. If each third-party release constitutes a separate operative proceeding, how should a bankruptcy court separate the releases to analyze them using the public rights exception? As discussed above, mass tort bankruptcies can arise in various contexts, including the sale of defective products,[316] systemic abuse[317] or wrongful marketing.[318] Mass tort debtors often propose sweeping releases in their chapter 11 plans that enjoin many types of claims against many entities. A bankruptcy court seeking to parse out individual releases for constitutional analysis would likely find the task impossible.

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309 *See Stern*, 564 U.S. at 499 (holding that federal causes of action "stem[med] from the bankruptcy itself" because the Code created them).

310 *See* Katchen v. Landy, 382 U.S. 323, 336–40 (1966); Langenkamp v. Culp, 498 U.S. 42, 44–45 (1990) (per curiam).

311 *See Stern*, 564 U.S. at 496–97 (noting that, in *Katchen*, once the bankruptcy court "determine[d] whether and to what extent to allow the creditor's claim," adjudicating the preference action in an Article III court "would be a meaningless gesture").

312 *See* Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 54–55 (1989).

313 *See In re* Purdue Pharma, L.P., 635 B.R. 26, 90 (S.D.N.Y. 2021).

314 *Id.* at 90–91.

315 *See Stern*, 564 U.S. at 496.

316 *See, e.g.*, ALERT COMMC'NS, *supra* note 13.

317 *See, e.g.*, *In re* Boy Scouts of Am. and Del. BSA, LLC, 642 B.R. 504, 518 (Bankr. D. Del. 2022).

318 *See, e.g.*, GALLAGHER, *supra* note 15.

When a mass tort debtor includes releases in its plan, the bankruptcy court should presume that it lacks the constitutional authority to approve the releases until the debtor proves otherwise. The Supreme Court would approve of such a presumption.[319] And applying the presumption would both conserve bankruptcy resources and deter mass tort debtors from proposing overbroad releases.

First, the Supreme Court said in *Stern* that the public rights exception only applies in limited circumstances.[320] When bankruptcy courts confront matters that are arguably covered by the exception, the *Stern* Court said, the presumption is for Article III courts to resolve them.[321] So, when a bankruptcy court analyzes third-party releases, it should keep in mind that it may only enter final judgment on them in limited circumstances; otherwise, bankruptcy courts should send the releases to an Article III court for resolution.[322]

Second, the presumption of unconstitutionality will conserve bankruptcy resources. In mass tort cases, parsing through releases is a "herculean undertaking" for bankruptcy courts.[323] The *Patterson* court reasoned that broad and convoluted releases are constitutionally suspicious, and bankruptcy courts lack authority to approve them.[324] Adding the presumption will save bankruptcy courts from attempting the impossible.

Third, the presumption of unconstitutionality will deter mass tort debtors from proposing overbroad third-party releases, which have been criticized as due process threats.[325] Debtors will know that if they fail to overcome the presumption of unconstitutionality, bankruptcy courts will be unable to confirm the debtors' chapter 11 plans. Once the bankruptcy court determines that it cannot enter final judgment on plan confirmation, it will send the proceeding to the district court, which must review the bankruptcy court's findings of fact and conclusions of law de novo.[326]

Debtors will likely want to avoid sending chapter 11 plan confirmation to the district court because doing so is inefficient. Bankruptcy courts are

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319 *See Stern*, 564 U.S. at 499.

320 *Id.*

321 *Id.*

322 *Id.* (quoting N. Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50, 69 n.23 (1982) (plurality opinion)) (noting that "matters that arguably fall within the scope of the 'public rights' doctrine" should have a "presumption [that] is in favor of Art. III courts").

323 Patterson v. Mahwah Bergen Retail Grp., Inc., 636 B.R. 641, 669 (E.D. Va. 2022).

324 *See id.*

325 Brubaker, *supra* note 33, at 985.

326 28 U.S.C. § 157(c)(1).

reorganization experts that have more experience with plan confirmation proceedings than district courts.[327] Moreover, when plan confirmation splinters off from the rest of the bankruptcy case, it can engender delays, costly withdrawal motions, and confusion for the parties.[328]

To avoid such problems, savvy debtors will make their third-party releases clear and constitutional under *Stern* before inserting releases into their plans. And if a debtor decides that its overbroad releases are important enough to warrant disconnecting plan confirmation from their bankruptcy, the debtor may do so. Debtors may argue that withdrawing to the district court imposes undue delays and costs on bankruptcy. But they may propose constitutional releases to avoid such withdrawal. "[T]he fact that a given law or procedure is efficient, convenient, and useful in facilitating functions of government, standing alone, will not save it if it is contrary to the Constitution."[329]

CONCLUSION

Third-party releases create many problems. Releases have split the circuits on the Code's interpretation, puzzled courts with juxtaposing policy considerations, and threatened creditors' due process rights. A uniform and constitutional separation of powers framework would alleviate many of these problems. The proposed framework is uniform because all bankruptcy courts can apply it; it is constitutional because it reflects the Supreme Court's separation of powers jurisprudence. The framework would alleviate problems with releases in three ways. First, the framework gives every circuit in the majority[330] a minimum standard that releases must meet for bankruptcy court approval, no matter the circuit's Code interpretation. Second, analyzing each individual release helps bankruptcy courts decide if each is closely intertwined with the debtor's bankruptcy, serving bankruptcy's fresh start policy. Third, the presumption of unconstitutionality encourages debtors to propose narrow releases that give creditors fair notice of the claims that they will lose.

[327] *See generally* Craig A. Gargotta, *Who Are Bankruptcy Judges and How Did They Become Federal Judges?*, FED. LAW. (Apr. 2018), https://www.fedbar.org/wp-content/uploads/2018/04/Bankruptcy-Brief-pdf-1.pdf (discussing bankruptcy judges' history and their importance for competent application of bankruptcy law).

[328] *See In re* Fang Operators, Inc., 158 B.R. 643, 647 (Bankr. N.D. Tex. 1993) (acknowledging concerns of sending matters from bankruptcy to district court, but not directly addressing plan confirmation).

[329] Stern v. Marshall, 564 U.S. 462, 501 (2011) (quoting INS v. Chadha, 462 U.S. 919, 944 (1983)).

[330] Of course, this framework will only unify those circuits in the majority. The minority of circuits will reject all third-party releases on statutory grounds, obviating the need for this framework.

This solution may burden chapter 11 debtors, especially in mass tort cases. The framework requires debtors to propose clear third-party releases such that the bankruptcy court can analyze all underlying claims. Failure to do so can stop plan confirmation and require sending the proceeding to the district court. But the current practice of third-party releases burdens everyone else in the bankruptcy system. Without the proposed presumption, debtors can request broad releases and leave bankruptcy courts to decipher them. Such broad releases require significant bankruptcy resources to analyze and increase the risk of bankruptcy courts misapplying other prongs of the separation of powers framework, harming creditors.

Further, this solution may hamper reorganization funding. Debtors could no longer release all third parties from liability on all claims and receive settlement money in exchange. But this framework does not prevent all third-party releases—only the unconstitutional ones. If a release satisfies this framework, like a derivative release, then the debtor can still seek reorganization funding from that released third party.

Third-party releases have several valid criticisms, and the separation of powers provides a valuable and underused tool for addressing them. The doctrine's proper implementation solves more than one may expect at first blush. By forcing debtors to prove the constitutionality of their releases, the doctrine induces fair play and uses plan confirmation as the carrot. But to harmonize releases with the Code and with the Constitution the bankruptcy community must give *Stern* another look.

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