No. 14-481

In the Supreme Court of the United States

NATIONAL HERITAGE FOUNDATION,

Petitioner,

v.

THE HIGHBOURNE FOUNDATION, JOHN R. BEHRMANN, AND NANCY BEHRMANN,

Respondents.

On Petition for Writ of *Certiorari* to the United States Court of Appeals for the Fourth Circuit

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BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the United States Court of Appeals for the Fourth Circuit erred in affirming, *en banc*, a District Court judgment holding that certain provisions in a chapter 11 bankruptcy plan of reorganization -- which released the debtor's third-party officers and directors from fraud liability and enjoined litigation against those officers and directors -- were unsupported by the factual record established at the chapter 11 plan confirmation hearing conducted by the Bankruptcy Court.

CORPORATE DISCLOSURE STATEMENT PURSUANT TO SUPREME COURT RULE 29.6

Pursuant to Supreme Court Rule 29.6, Respondents, John Behrmann, Nancy Behrmann and the Highbourne Foundation (collectively, "Respondents") make the following mandatory disclosures:

1. None of the Respondents is a publicly held corporation or other publicly held entity.

2. None of the Respondents is owed by a parent corporation.

3. None of the stock of the Respondents is owned by a publicly traded corporation or a publicly held entity.

4. None of the Respondents is a trade association.

5. This case arises out of a chapter 11 bankruptcy proceeding, *In re National Heritage Foundation, Inc.*, Case No. 09-10525-BFK pending in the United States Bankruptcy Court for the Eastern District of Virginia.

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INTRODUCTION

This factually-intensive case arises from the insistence of a chapter 11 debtor, National Heritage Foundation, Inc. ("NHF"), to include in its reorganization plan certain non-debtor third-party release and injunction provisions (the "Challenged Provisions") designed to insulate those in control of NHF from any individual liability for their fraud, defalcation, misconduct or other wrongdoing committed prior to the filing of NHF's chapter 11 bankruptcy petition.

The opinion that NHF asks the Court to review did not involve the issue of whether non-debtor releases -- whereby persons who have not filed bankruptcy petitions are nevertheless insulated from liability for certain pre-bankruptcy conduct -- are permissible under the Bankruptcy Code. Indeed, the Fourth Circuit previously decided that issue *in NHF's favor*, while emphasizing that such releases should be granted "cautiously and infrequently," in a prior appeal from which no review was sought.

Rather, the appeal below pivots on whether NHF presented sufficient evidence to support a non-debtor release at a confirmation hearing conducted in October of 2009. The United States Bankruptcy Court for the Eastern District of Virginia, the United States District Court for the Eastern District of Virginia, and the Fourth Circuit have all answered that question in the negative.

NHF now invites this Court to engage in appellate fact-finding and to locate in the evidentiary record that which all of the lower courts have held does not exist: specific factual circumstances and evidence to justify the extraordinarily broad and expansive Challenged Provisions. The lower courts have repeatedly held that the evidence presented by NHF is insufficient. Yet another review of the sparse record of this case will not change that result.

STATEMENT OF THE CASE

This garden-variety chapter 11 bankruptcy case is elevated to this High Court with hyperbole and fiction. The issue does not merit further review and NHF's petition for writ of *certiorari* should be denied.

On January 24, 2009, NHF filed a chapter 11 bankruptcy case allegedly as a result of being unable to post security to prevent execution upon a state court judgment exceeding $9 million. The judgment was entered against it for fraud in an action brought by the parents of a crippled child when they learned NHF had wrongfully changed the beneficiary of insurance policies to itself. App. 41. Respondents, who established charitable foundations with NHF unaware that NHF's officers and directors were using the donors' money to line their own pockets, are the holders of timely-filed claims in the NHF chapter 11 reorganization case.

On September 9, 2009, NHF filed its Third Amended Plan of Reorganization, a proposed chapter 11 plan which contained the extraordinary

Challenged Provisions. Specifically, the aim of the Challenged Provisions was to: (i) release NHF's directors and officers (and anyone else designated by NHF) from any liability for pre-petition acts of fraud, malfeasance, defalcation or other wrongdoing, and (ii) enjoin civil action against those persons. (Notably, the persons to whom NHF sought to extend such extraordinary protection were primarily the immediate family members of NHF's then CEO, John T. Houk II.)

On October 15, 2009, the Bankruptcy Court[1] (J. Stephen Mitchell) conducted a brief confirmation hearing at which NHF offered scant evidence in support of the Challenged Provisions. In fact, NHF offered only a single witness, Ms. Janet Ridgely, who testified briefly at the hearing. No other evidence was offered in support of the Challenged Provisions.[2] Judge Mitchell was not persuaded and rejected confirmation of the Challenged Provisions.

Having failed to convince the Bankruptcy Court to confirm the Reorganization Plan, the following morning NHF filed an "Exhibit" to the

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[1] United States Bankruptcy Court for the Eastern District of Virginia Case No. 09-10525.

[2] NHF's representation to this Court that there was an extensive two-day evidentiary hearing in connection with the confirmation of the Reorganization Plan is materially inaccurate. Ms. Ridgely was the only witness who testified, and her brief testimony was all that occurred on October 15, 2009. The balance of the hearing before the Bankruptcy Court on October 15 and 16, 2009, was dedicated to non-evidentiary matters and arguments of counsel.

Reorganization Plan which narrowed the reach of the Challenged Provisions but continued to provide complete insulation for Ms. Ridgley and the Houk family. Later that day, October 16, 2009, Judge Mitchell entertained further argument in respect of the Challenged Provisions during which Respondents renewed and continued their objections.

Judge Mitchell acknowledged that the Challenged Provisions were "problematic" and that they are "disfavored." He described the Challenged Provisions as a "close case," but he overruled Respondents' objections and confirmed the Reorganization Plan as amended by the "Exhibit" filed only a few hours earlier. In so doing, Judge Mitchell signed -- without amendment, revision or comment -- the exact form of Confirmation Order tendered by NHF's counsel.[3] Respondents appealed to the District Court,[4] which on August 17, 2010 entered a one-page Order affirming the Bankruptcy Court's Confirmation Order. Respondents then appealed to the Fourth Circuit ("*NHF I*").

On December 9, 2011, the Fourth Circuit entered its Opinion in *NHF I* in which it reversed and vacated the judgment affirming the Bankruptcy Court Confirmation Order. *Behrmann v. National*

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[3] Judge Mitchell's execution of the Confirmation Order submitted by NHF's counsel is reported at *In re National Heritage Foundation, Inc.*, 2009 Bankr. LEXIS 4928 (Bankr. E.D. Va. October 16, 2009).

[4] United States District Court for the Eastern District of Virginia Case No. 10-1040.

Heritage Foundation, Inc., 663 F.3d 704 (4th Cir. 2011). The Circuit Court initially ruled that Respondents' argument that non-debtor releases are impermissible under the Bankruptcy Code was without merit. *Id.* at 710. However, the panel admonished that such provisions are appropriate only in "very limited circumstances." *Id.* at 711. The Court underscored that in order to sustain the Challenged Provisions, the Bankruptcy Court's findings of fact must justify legal conclusions that could not apply "just as well to any number of reorganizing debtors." *Id.* at 712-13. The Circuit Court remanded for the Bankruptcy Court to determine whether the evidentiary record established at the confirmation hearing on October 15, 2009 would support the "specific factual findings" necessary to uphold the Challenged Provisions. *Id.* at 713. No party sought review of the ruling in *NHF I*.

On remand to the Bankruptcy Court, Bankruptcy Judge Brian Kenney (who assumed responsibility for the bankruptcy case following the retirement of Judge Mitchell) conducted a status conference on March 6, 2012. At that status conference, NHF affirmed that it did not wish to present additional evidence, and ***expressly consented*** to the entry by Judge Kenney of findings based upon the record established at the October 15, 2009 confirmation hearing.

On August 27, 2012, after a thorough and detailed review of the record of the confirmation hearing, Judge Kenney entered an extensive and carefully-reasoned Memorandum Opinion (the

"August 27 Opinion")[5] and a corresponding Order focusing upon the Challenged Provisions. Judge Kenny carefully detailed the scant evidence presented at the confirmation hearing in support of the Challenged Provisions. In his exhaustive August 27 Opinion, Judge Kenney determined that the record of the confirmation hearing did ***not*** support the non-debtor release provision contained in the Reorganization Plan. He further determined that to the extent the Reorganization Plan also contained an injunctive provision implementing the non-debtor release provision, the injunction provision also could not stand. Accordingly, Judge Kenney found that the Challenged Provisions are unenforceable.

NHF appealed the Bankruptcy Court's August 27 Opinion and corresponding Order to the District Court.[6] On April 3, 2013, the District Court entered its twenty-page Memorandum Opinion (the "April 3 Opinion"),[7] in which District Court (Judge Anthony Trenga) also found upon *de novo* factual review that the Challenged Provisions were unsupported by the evidentiary record established at the confirmation hearing. After an exhaustive review of the relevant facts and controlling law, the District Court found and

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[5] Judge Kenney's August 27 Opinion is reported at *In re National Heritage Foundation, Inc.*, 478 B.R. 216 (Bankr. E.D. Va. 2012).

[6] United States District Court for the Eastern District of Virginia Case No. 12-cv-01329.

[7] Judge Trenga's April 3 Opinion is reported at *National Heritage Foundation, Inc. v. Behrmann*, 2013 U.S. Dist. LEXIS 49081 (E.D. Va. April 3, 2013).

concluded that: (1) the Bankruptcy Court did not exceed the mandate on remand, (2) the findings of fact that formed the factual basis for the Bankruptcy Court's decision were not clearly erroneous and were, in fact, fully supported by the record, and (3) applying the applicable law *de novo* to the findings of the Bankruptcy Court, the Challenged Provisions were not warranted as part of the Reorganization Plan.

NHF then appealed to the Fourth Circuit ("*NHF II*").

On July 25, 2014, the Fourth Circuit entered its Opinion in *NHF II*, in which it affirmed Judge Trenga's April 3 Opinion and determined that those provisions are unsupported by the evidence adduced at the confirmation hearing.

The Fourth Circuit reiterated in *NHF II* that non-debtor releases should be approved "cautiously and infrequently" and only under "appropriate circumstances." To determine whether such circumstances exist, the Fourth Circuit applied its precedent and the six substantive factors enumerated by the Sixth Circuit in *Class Five Nevada Claimants v. Dow Corning Corp.*, 280 F.3d 648 (6th Cir. 2002), *cert. denied*, 538 U.S. 816 ("*Dow Corning*"). The Fourth Circuit engaged in an exhaustive review of the NHF Reorganization Plan, in which it applied the *Dow Corning* factors and found that of six enumerated, only one factor weighed in favor of approval of the Challenged Provisions. Accordingly, the Fourth Circuit affirmed (*en banc*) Judge Trenga's April 3 Opinion and, in doing so, became the fourth

Court to find -- after exhaustive review -- that the Challenged Provisions were impermissibly broad and unenforceable in light of the scant evidence provided by NHF.

In sum, the lower courts have resoundingly held that the Challenged Provisions are not warranted or appropriate given the unremarkable nature of NHF's case:

- The Fourth Circuit held in 2011, that the Challenged Provisions were not supported by the record before it. *Behrmann*, 663 F.3d at 710-12.

- The Bankruptcy Court, on remand and after *de novo* review, found that the Challenged Provisions were not supported by the evidence. *In re National Heritage Foundation, Inc.*, 478 B.R. at 230.

- The District Court, upon *de novo* review, affirmed the judgment that the Challenged Provisions were not supported by the evidence. *National Heritage Foundation, Inc.*, 2013 U.S. Dist. LEXIS 49081, *7 (E.D. Va. April 3, 2013).

- The Fourth Circuit, after yet another review, affirmed and again held that the Challenged Provisions

were not supported by the evidence. App. 1-17.

On October 23, 2014, NHF filed its "Petition for a Writ of Certiorari" (the "Petition") with this Court requesting yet *another* review by this Court of the evidentiary record of the October 15-16, 2009 confirmation hearing. The Petition should be denied because the issues sought for review by NHF are fact based and have been resoundingly rejected by the lower courts numerous times.

REASONS FOR DENYING THE PETITION

This is an ordinary, fact-bound chapter 11 case. The case hinges upon the adequacy of evidence presented by a debtor to support extraordinary non-debtor releases as a component of its plan of reorganization. The request for *certiorari* should be denied for at least two reasons:

First, the Petition invites this Court to engage in appellate fact-finding and to glean from the evidentiary record that which does not exist: specific factual circumstances necessary to justify the extraordinarily broad and expansive Challenged Provisions that NHF insisted on including in its Reorganization Plan protecting the family members of its former CEO, its officers and directors. Further review of NHF's case will not change the lower courts' determination that the extraordinary factual circumstances necessary to warrant non-debtor releases in a chapter 11 plan of reorganization are not present in this case.

Second, the Petition asks this Court to entertain a perceived -- but irrelevant -- "split" in the decisional authority of the Circuit Courts. What NHF intentionally ignores in its Petition (and hopes this Court will disregard) is that its Reorganization Plan fails to satisfy ***any*** of the allegedly differing standards articulated by the Circuit Courts respecting the propriety of a non-debtor release as a component of a chapter 11 plan.

I. NHF Failed to Present Evidence to Justify the Extraordinarily Broad and Expansive Challenged Provisions

At the time of its bankruptcy filing and confirmation of its Reorganization Plan, NHF was a Georgia corporation operating as an IRC § 501(c)(3) qualified public charity[8] that allegedly administered and maintained Donor-Advised Funds (DAFs) A DAF is a fund in which a donor relinquishes the right and title in the assets which are donated but retains the right to advise in respect of the use and distribution of the assets to charity. Prior to NHF's bankruptcy filing, Respondents established a Donor-Advised Fund with NHF and transferred assets to it expressly intended for subsequent follow-on transfers for charitable purposes. However, Respondents later learned that NHF had imperiled that charitable purpose by pledging the donated assets (indeed,

[8] In November 2011, the Internal Revenue Service revoked NHF's status as a section 501(c) public charity. App. 3.

substantially all of the Donor-Advised Funds under its control) as security for a third-party financial institution loan.[9] Respondents also learned that NHF is dominated and controlled by the Houk family, whose members hold all of NHF's officer positions and all but two of NHF's board seats. These facts were undisclosed to Respondents at the time they established their Donor-Advised Fund.

On January 24, 2009, NHF filed a chapter 11 bankruptcy petition after being allegedly unable to post security to prevent execution upon a multimillion dollar state court judgment against it.[10] Respondents timely filed creditor claims in the NHF chapter 11 reorganization case asserting, *inter alia*, a right to rescind their donations.

On October 15-16, 2009, a confirmation hearing was conducted respecting NHF's proposed Reorganization Plan, the fourth iteration of which had been filed only days earlier. The Plan contained a non-debtor release provision covering NHF; the Official Committee of Unsecured Creditors (the "Committee") and its members; any designated representatives of the Committee; and any officers, directors or employee of NHF, the Committee, or their successors and assigns (collectively, the "Released

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[9] Indeed the assets were converted by NHF to pay off the bank loan in the approximate amount of $7.8 million by having the pledge liquidated.

[10] This despite the fact that NHF boasted to its donors in the same time frame that it was managing $170 million in assets and only $18 million in debt.

Parties"). The Release Provision provided that the Released Parties. . .

> shall not have or incur, and are hereby released from, any claim, obligation, cause of action, or liability to any party in interest who has filed a claim or who was given notice of the Debtor's Bankruptcy Case (the "Releasing Parties") for any act or omission before or after the Petition Date through and including the Effective Date in connection with, or relating to, or arising out of the operation of the Debtor's business, except to the extent relating to the Debtor's failure to comply with its obligations under the Plan. . . .

The Reorganization Plan also contained an Exculpation Provision which barred suits against the Released Parties for any acts or omissions in connection with the bankruptcy, and an Injunction Provision which enjoined suits in violation of either the Release or the Exculpation Provision.

A hearing respecting the confirmation of the proposed Reorganization Plan was conducted on October 15, 2009. In addressing the reorganization, and the Reorganization Plan, the Bankruptcy Court found four important facts:

1. NHF's officers and directors had made no financial contribution in exchange for the highly valuable benefits that they

were to derive from the Challenged Provisions.

2. Respondents' claims were placed in Class III(C) of the Reorganization Plan (which had been created to render Appellees' claims "unimpaired" under the Bankruptcy Code). Thus, Respondents -- and all other members of Class III(C) -- were stripped by 11 U.S.C. § 1126(f) of *any* opportunity to vote upon the Reorganization Plan.

3. The Reorganization Plan does not contain any mechanism for payment of the claims alleged against the Houk family members barred by the release contained in the Challenged Provisions.

4. The Reorganization Plan does not provide for payment outside of the plan for the claims against the Houk family members. Indeed, the release contained in the Challenged Provisions essentially bars any opportunity for payment of the claims impacted by the release.

App. at 68-84. Respondents timely objected to the confirmation of the Reorganization Plan. Among other things, Respondents observed that the Challenged Provisions insulated the non-debtor Released Parties from suit by innocent third-parties who suffered financial losses as a result of the pre-

petition fraud, defalcation, misconduct and other wrongdoing of the Houk family members.

The only testimony offered by NHF at the October 15, 2009 confirmation hearing was that of Ms. Janet Ridgely (a member of the Houk family). In respect of the Challenged Provisions, Ms. Ridgely testified that there was "concern" that the non-debtor officers and directors (*i.e.*, principally the Houk family members) "could be sued," and that no one wanted the specter of litigation hanging over them going forward. Tellingly, however, Ms. Ridgely also testified that she was not aware of any factors or influences that were unique to the Houk family members that distinguished them from the management of any other chapter 11 debtor. She also testified that ***none*** of NHF's officers and directors -- including Ms. Ridgely -- had come forward to say that they would decline to serve in the capacity of a director or officer unless the Challenged Provisions were included in the Reorganization Plan.

Notwithstanding the paucity of evidence supporting the non-debtor release provision, the Bankruptcy Court on October 16, 2009 confirmed the Reorganization Plan over Respondents' objections. *In re National Heritage Foundation, Inc.*, 2009 Bankr. LEXIS 4928 (Bankr. E.D. Va. October 16, 2009). The District Court affirmed in a one-page Order on August 17, 2010.

On December 9, 2011, the Fourth Circuit entered its Opinion in *NHF I* reversing and vacating the confirmation of the Reorganization Plan. *NHF I*,

663 F.3d at 713.[11] The Fourth Circuit observed that the confirmation of the Challenged Provisions was only appropriate under "very limited circumstances" and, therefore, NHF should have been required to prove the existence of factual circumstances that could not apply "just as well to any number of reorganizing debtors." *Id.* at 712-13. The panel remanded to the Bankruptcy Court with instructions to review the evidentiary record of the October 15, 2009 confirmation hearing and to determine whether that record contained adequate factual and evidentiary support for the Challenged Provisions. *Id.* In connection with its instruction, the Fourth Circuit directed the Bankruptcy Court to consider the facts enumerated in *Dow Corning*:

> (1) There is an identity of interest between the debtor and the third party … ; (2) The non-debtor has contributed substantial assets to the reorganization; (3) The injunction is essential to reorganization … ; (4) The impact class, or classes, has overwhelmingly voted to accept the plan; (5) The plan provides a mechanism to pay all, or substantially all, of the class or classes affected by the injunction; [and] (6) The plan provides an opportunity for those claims who choose not to settle to recover in full.

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[11] Procedurally it should be noted that NHF sought no further review of the Fourth Circuit's Ruling in *NHF I*, and did not seek a writ of *certiorari* from the U.S. Supreme Court at that time.

280 F.3d at 658. On March 6, 2012, the Bankruptcy Court conducted a status conference at which NHF was given the opportunity to present additional evidence in support of the Reorganization Plan and the Challenged Provisions. NHF *declined the opportunity to present additional evidence* and consented to the entry by Judge Kenney of findings upon the record established at the October 15, 2009 confirmation hearing.

On August 27, 2012, Judge Kenney ruled. *In re National Heritage Foundation, Inc.*, 478 B.R. at 216. Notably, Judge Kenney found that it was unlikely that the Houk family members would resign from NHF owing solely to the assertion of third party claims against them. He observed that even if NHF directors and/or officers resigned, the departing Houk family members would not eliminate liability for acts or omissions occurring prior to resignation. Moreover, Judge Kenney found that NHF had offered no evidence that NHF needed to attract new directors or officers, and it had offered no evidence respecting how the inclusion of the Challenged Provisions would impact any such need.

The Bankruptcy Court further noted that on October 16, 2009, it had entered the Confirmation Order confirming the Reorganization Plan (containing a slightly narrowed version of the Challenged Provisions, and later reversed by the Fourth Circuit in *NHF I*). However, the Court observed that even the narrower version of the Challenged Provisions continued to insulate the non-debtors (the Houk family members) from pre-petition wrongdoing and misconduct. Of significance, the

Bankruptcy Court observed that the confirmed Reorganization Plan contains a "severability" provision -- Section 12.2 -- which permitted the Bankruptcy Court to declare unenforceable and excise any provision that was unlawful or inappropriate without affecting the enforceability of the balance of the Reorganization Plan.

On appeal to the District Court, Judge Trenga determined that he would review the record from the confirmation hearing *de novo*. App. 48. After an exhaustive review of the relevant facts and controlling law, the District Court found and concluded that: (1) the Bankruptcy Court did not exceed the mandate on remand, (2) the findings of fact that formed the factual basis for the Bankruptcy Court's decision were not clearly erroneous and were, in fact, fully supported by the record, and (3) applying the applicable law *de novo* to the factual findings of the Bankruptcy Court, the Challenged Provisions were not warranted as part of the Plan.

In *NHF II* (of which *certiorari* review is now sought by NHF), the Fourth Circuit affirmed *en banc* the holding of the District Court which, in turn, had affirmed the holding of the Bankruptcy Court. All the lower Courts have held that the Challenged Provisions are unsupported by the confirmation hearing record on which NHF chose to rest. Applying each of the *Dow Corning* factors to the specific facts of this case, the Fourth Circuit concluded (as had the District Court and Bankruptcy Court before it) that the unremarkable features of this chapter 11 case do not warrant the extraordinary Challenged Provisions:

A. There is an Identity of Interest Between NHF and the Released Parties

Under the first *Dow Corning* factor, the Court must consider whether there is an identity of interest between the debtor and the third-party to be released by the provisions of the proposed chapter 11 plan. This factor is pertinent because, as the Sixth Circuit has observed, a suit against the non-debtor released party may, "in essence, [be] a suit against the debtor" that risks "deplet[ing] the assets of the estate." *Dow Corning*, 280 F.3d at 658; *see also NHF I*, 663 F.3d at 711.

Of the six *Dow Corning* factors, only this first factor weighs in favor of the Challenged Provisions. Each of the lower courts held that NHF demonstrated an identity of interests between itself and the Released Parties, therefore satisfying the first factor.

B. NHF's Officers and Directors Did Not Contribute Financially to the NHF Reorganization

The second *Dow Corning* factor required NHF to demonstrate that the Released Parties made a substantial contribution to the assets of its reorganization. *NHF I*, 663 F.3d at 711. As the Fourth Circuit observed, this factor "ensures that in order for a Released Party to achieve that status, it must have provided a cognizable and valid contribution to the debtor as part of the debtor's reorganization." App. 8.

None of the Released Parties in this case made any financial contribution to the NHF reorganization. NHF nonetheless argues that its officers and directors satisfied this requirement by promising to continue serving NHF. But nowhere in the Reorganization Plan or corresponding chapter 11 disclosure statement is there any "promise" by anyone to provide post-confirmation service for any period of time. (Indeed, as the Fourth Circuit observed, the fact that John T. Houk, NHF's former CEO resigned from NHF following confirmation of the Reorganization Plan, flies in the face of NHF's representation.) App. 8, fn. 4. There is no evidence in the record to support NHF's assertion that its officers and directors actually promised to continue serving NHF, *or* that the Challenged Provisions had any impact thereupon.

Moreover, even if such a phantom promise existed (which it did not), it would be of no moment. This Supreme Court has authoritatively ruled that a promise of future services is insufficient to establish new value (which requires a *financial* contribution) for the purposes of plan confirmation. *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 203 (1988). Rather, as the Bankruptcy Court found and the Fourth Circuit agreed, NHF's "officers and directors, all of whom are insiders, performed their duties either because they were paid to do so (in the case of the officers), or because they had a fiduciary obligation to do so (in the case of the directors)." *In re National Heritage Foundation*, 478 B.R. at 229; *see also In re SL Liquidating, Inc.*, 428 B.R. 799, 804 (Bankr. S.D. Ohio 2010) (concluding that directors and officers did

not make a substantial contribution when their 'described efforts … [were] consistent with their preexisting fiduciary duties and job responsibilities"). Thus, the Fourth Circuit correctly concluded that "[u]nder these circumstances, the Released Parties did not provide meaningful consideration for their release from liability … The absence of such consideration weighs against [the Challenged Provisions]." App. 9.

C. The Challenged Provisions Were Not Essential to the Success of the Reorganization

To satisfy the third *Dow Corning* factor, a debtor must demonstrate that the non-debtor release is "essential" to its reorganization such that "the reorganization hinges on the debtor being free from indirect suits against parties who would have indemnity or contribution claims against the debtor." *Dow Corning*, 280 F.3d at 658; *NHF I*, 663 F.3d at 711-12.

As the Fourth Circuit observed, NHF's contention that the Challenged Provisions were "essential" to the reorganization was that there existed a potential deluge of litigation against NHF and, as a result, NHF would likely have to indemnify its officers and directors for their legal expenses should such suits arise. App. 9. But as all of the lower courts observed, the evidentiary record does not support this contention. Indeed, NHF provided no evidence at the confirmation hearing respecting the number of likely donor claims, the nature of such

claims, or their potential merit. Ms. Ridgely's statement at the confirmation hearing that NHF insiders were "concerned" about donors bringing suit is, as the Fourth Circuit held, "simply too vague to substantiate the risk of litigation." App. 10; *cf. In re Dow Corning Corp.*, 287 B.R. 396, 411 (E.D. Mich. 2002) (release provision was essential when more than 14,000 lawsuits had already been filed against a non-debtor).

Equally unsupported by the record is NHF's representation that the pre-bankruptcy judgment entered against it, and the follow-on litigation with Respondents, evidence a potential deluge of lawsuits. As the Fourth Circuit observed, "Based on the dearth of evidence in the record, we can only speculate as to the potential impact of any donor suits on NHF's financial bottom line." App. 10.

Were that not enough, the Fourth Circuit found additional reasons to reject NHF's contention that the Challenged Provisions are essential. For instance, the appellate court rejected any import of Ms. Ridgely's statement at the confirmation hearing that a fear of third-party suits "might render [the Released Parties] unwilling to serve." App. 11. Rather, the Fourth Circuit agreed with the Bankruptcy Court that "the risk of NHF's insiders abandoning ship is particularly low, given that most of them are members of a single family." *Id.*, *citing In re National Heritage Foundation*, 478 B.R. at 229. The Fourth Circuit also observed that "even if NHF's officers and directors do leave [in the absence of the Challenged

Provisions], NHF has not suggested that it would face difficulty recruiting new personnel." App. 11.

The severability clause contained in the Reorganization Plan, in the words of the Fourth Circuit, "cements" the conclusion that the Release Provision is not essential to the success of the Plan. The severability clause provides that the Plan will remain in effect "[s]hould any provision in this Plan be determined to be unenforceable." App. 11-12. As the Fourth Circuit concluded, "such language suggests that the plan would remain viable absent the [Challenged] Provisions." *Id.*; *see also NHF I*, 663 F.3d at 714. Accordingly, the appellate court correctly concluded that "NHF has not met its burden of demonstrating that the [Challenged Provisions] are essential to its reorganization. This failure weighs strongly against the validity of the [Challenged Provisions]." *Id.*

D. The Impacted Class Did Not Vote in Favor of the Reorganization Plan

The fourth *Dow Corning* factor required NHF to prove that the class or classes affected by the Challenged Provisions overwhelmingly voted in favor of the Plan. *Dow Corning*, 280 F.3d at 659. NHF failed in that effort as well.

As all of the lower courts observed, the class of claimants most directly impacted by the Challenged Provisions is comprised of those who made donations to NHF's Donor-Advised Funds. (The Fourth Circuit referred to this class of claimants as "the donor class." App. 12.) Under applicable bankruptcy law, the donor

class' support for the Reorganization Plan was presumed without a formal vote because, under the terms of the Plan, donor claims were eligible for full payment with interest. *See* 11 U.S.C. § 1126(f) ("[A] class that is not impaired under a plan, and each holder of a claim or interest of such class, are conclusively presumed to have accepted the plan, and solicitation of acceptance with respect to such class … is not required").

However, as the Fourth Circuit observed, "the power to authorize non-debtor releases is rooted in a bankruptcy court's equitable authority." App. 13; *citing Menard-Sanford v. Mabey (In re A.H. Robins Co.)*, 880 F.2d 694, 701 (4th Cir. 1989), *cert. denied*, 493 U.S. 959. The Fourth Circuit determined that "the equities weigh against NHF, as the class most affected by the Release Provision was not given the opportunity to accept or reject the plan." App. 13; *cf. In re Specialty Equip. Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1993) (finding releases consensual and valid when "each creditor could choose to grant, or not to grant, the release irrespective of the vote of the class of creditors or interest holders of which he or she is a member" meaning that "a creditor who … abstains from voting may still pursue any claims against third-party nondebtors").

In its Petition to this Court, NHF makes short shrift of this dilemma, merely arguing that the Fourth Circuit "erred" in holding that this *Dow Corning* factor weighed against the Challenged Provisions. Petition at 22.

The argument is meritless for at least two reasons. First, it is at best disingenuous. During its reorganization, NHF expressly represented to the donor class that its members did not hold a claim against NHF and thereby actively dissuaded members of the class from timely filing proofs of claim in the bankruptcy case. App. 72-73; *see also* Fed.R.Bankr.P. 3003(c)(3). And of course, while NHF represents to this Court that members of the donor class are unimpaired, it omits that at Section 7.8 of its chapter 11 disclosure statement, it will (and in fact, did) object to all claims timely filed by any members of that class. App. 74.

NHF's two-handed strategy thus involved simultaneously: (i) objecting to all of the donor class' claims (which was designed to deny members of that class any right of recovery under the Reorganization Plan), and (ii) representing to the lower court that those claims were "unimpaired" notwithstanding NHF's objections. That the Fourth Circuit found the equities to weigh against NHF under these circumstances is hardly a surprise. App. 12-14.

Second, whether this factor weighs in favor or against the Challenged Provisions is, as the Fourth Circuit concluded, ultimately irrelevant — because it would not alter the conclusion "that NHF has failed to demonstrate that the circumstances warrant the [Challenged Provisions]. Creditor support does not make up for the fact that most of the other *Dow Corning* factors weigh against enforcing the [Challenged Provisions.]" App. 14.

E. The Reorganization Plan Does Not Provide a Mechanism to Pay the Affected Class

The fifth *Dow Corning* factor requires the court to "consider whether the debtor's reorganization plan provides a mechanism to consider and pay all or substantially all of the class or classes affected by the non-debtor release." *NHF I*, 663 F.3d at 712. As the District Court noted, "[t]his consideration has typically been used to justify release provisions where the reorganization plan includes a mechanism such as a dedicated settlement fund to pay the claims … of those affected by an injunction." App. 64; *see also In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005) ("Courts have approved nondebtor releases when … the enjoined claims were 'channeled' to a settlement fund rather than extinguished …"); *A.H. Robins Co.*, 880 F.2d at 700-02. Although the Fourth Circuit held that there is no *per se* requirement that claims be "channeled" to a settlement fund or similar device, "the absence of such a mechanism can weigh against the validity of a non-debtor release, especially when the result is that the impact class's claims are extinguished entirely." App. 15.

Here, not only is there no "channeling" mechanism, there is no mechanism ***at all*** to satisfy the claims of the donor class. Rather, as the Fourth Circuit observed, "Any donor claims not filed or allowed during the bankruptcy proceedings have simply been extinguished." App. 15. (Indeed, the Fourth Circuit observed that during the

reorganization process, NHF expressly advised members of the donor class that "Donors are not creditors of the Debtor and will have no rights to vote or receive Distributions under the Plan"). *Id.* The appellate court was not impressed by the disingenuous approach taken by NHF in this case, noting that its representations to members of the donor class "hardly strikes us as a *bona fide* effort to ensure the consideration of nearly all of the donor class's claims." *Id.* The Fourth Circuit therefore correctly concluded, and agreed with both the District Court and Bankruptcy Court before it, that this factor also weighs against the Challenged Provisions. *Id.*

F. The Reorganization Plan Does Not Provide an Opportunity for Those Who Choose Not to Settle to Recover in Full

The final *Dow Corning* factor is "whether the plan provides an opportunity for those who choose not to settle to recover in full." *NHF I*, 663 F.3d at 712.

The significant of this factor is demonstrated in *A.H. Robins*, where claimants who opted out of a settlement funded by the debtor's insurers were barred from pursuing claims against the debtor's officers and directors. However, in *A.H. Robins*, the creditors who opted out of the settlement retained their rights to recover outside the reorganization plan by pursuing suit against the insurer. In contrast, NHF's Reorganization Plan was not funded by any insurer or other third-party source, and the

Reorganization Plan provided no mechanism for the satisfaction of creditor claims outside of its own terms. App. 16.

Thus, the Fourth Circuit correctly observed that this final factor also weighs against the Challenged Provisions because NHF simply "fail[ed] to provide any mechanism to pay donor claims outside of the bankruptcy proceedings." *Id.* Indeed, as the Bankruptcy Court found and the Fourth Circuit agreed, "the very purpose of the [Challenged Provisions] is to … preclud[e] any recovery from third party sources outside of the Plan." *Id.*, *citing In re National Heritage Foundation*, 478 B.R. at 232.

Having affirmed that all but one of the *Dow Corning* factors weighed against the Challenged Provisions, the Fourth Circuit concluded that "NHF has failed to demonstrate that it faces exceptional circumstances justifying the enforcement of the [Challenged Provisions] in its Reorganization Plan." App. 17. The Fourth Circuit emphasized that its "decision is ultimately rooted in NHF's failure of proof rather than circumstances alone … a debtor must provide adequate factual support to show that the circumstances warrant such exception relief, and NHF has failed to do so here." *Id.*

II. Any Perceived "Difference" in the Decisional Authority of the Circuit Courts is Irrelevant

NHF emphasizes in its Petition what it asserts to be a "difference" among the Circuit Courts

respecting the propriety of confirming a chapter 11 plan containing a non-debtor release.[12]

Any such difference is irrelevant in this case because NHF's proposed Reorganization Plan fails to satisfy *any* of the standards articulated by the Circuit Courts. *Deutsche Bank AG v. Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005) ("No case has tolerated nondebtor releases absent the finding of circumstances that may be characterized as unique"); *Dow Corning*, 280 F.3d at 658 (injunction barring suit against non-debtor "is a dramatic measure to be used cautiously"); *Gillman v. Continental Airlines*, 203 F.3d 203, 212-13 (3d Cir. 2000) (non-debtor releases have been approved only in "extraordinary cases"); *In re A.H. Robins Co.*, 788 F.2d 994, 999 (4th Cir. 1986), *cert. denied*, 479 U.S. 876 (1986) (non-debtor releases permissible only in "unusual circumstances"); *Resorts International, Inc. v. Lowenschuss*, 67 F.3d 1394, 1402 (9th Cir. 1995) (declining to recognize exception to general rule disfavoring non-debtor releases); *In re Western Real Estate Fund, Inc.*, 922 F.2d 592, 599-600 (10th Cir. 1990) (finding non-debtor release inappropriate for case-specific reasons). Any "difference" between the decisional authority of the Circuit Courts is clearly irrelevant where, as here, the outcome is the same regardless which authority is applied.

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[12] Patently, an attempt by NHF to persuade the Pool review that there is a split in the law that commands Certiorari by the Supreme Court.

Moreover, NHF seeks that which Congress has expressly rejected: uniformity in the outcome of bankruptcy proceedings irrespective of the location of the case. To the contrary, the Bankruptcy Code expressly provides for differing outcomes in bankruptcy cases depending upon the venue of the proceeding. For instance, 11 U.S.C. § 522(b)(3)(A) permits each of the states to adopt exemptions which differ from the federal exemptions and which can dramatically alter the outcome and result of a bankruptcy case depending upon its venue. And in *Butner v. U.S.*, 440 U.S. 48, 54-56 (1979), this Court expressly recognized the authority of the bankruptcy and district courts to rely upon state law and local decisional authority to determine the contours of "property" in the context of bankruptcy proceedings.

This Court has long recognized that where Congress has elected *not* to exercise its constitutional authority to establish a uniform rule of bankruptcy law, the district and bankruptcy courts are permitted to fashion non-uniform standards to be applied in the context of bankruptcy proceedings:

> The constitutional authority of Congress to establish 'uniform Laws on the subject of Bankruptcies throughout the United States' [U.S. Const., Art. I, § 8, cl. 4] would clearly encompass a federal statute defining the mortgagee's interest in the rents and profits earned by property in a in a bankruptcy estate. But Congress has not chosen to exercise its power to fashion any such rule …

> Congress has generally left the determination of property rights in the assets of a bankrupt's estate to state law.

Id. at 54; *see also Stellwagen v. Clum*, 245 U.S. 605, 613 (1918) (emphasis supplied):

> Notwithstanding this requirement as to uniformity the bankruptcy acts of Congress may recognize the laws of the State in certain particulars, although such recognition may lead to *different results in different States*. For example, the Bankruptcy Act recognizes and enforces the laws of the States affecting dower, exemptions, the validity of mortgages, priorities of payments and the like. Such recognition in the application of state laws does not affect the constitutionality of the Bankruptcy Act, although in these particulars the operation of the act is not alike in all the States.

Here, as in *Butner*, Congress has elected not to establish a uniform rule of bankruptcy law. And here, as in *Butner*, Congress's silence authorizes the creation of differing local standards respecting the contours of the Bankruptcy Code. NHF's Petition founded upon "different" standards among the Circuit Courts misconstrues the Bankruptcy Code and this Court's decisional precedent expressly permitting "different" results in different bankruptcy venues. This is *especially* true where, as here, the outcome

and result of the bankruptcy proceeding would not change regardless of where NHF filed its bankruptcy petition.

CONCLUSION

For all of the foregoing reasons, and in the light of all the authorities cited above, Respondents respectfully submit that NHF's Petition for Writ of *Certiorari* should be denied.

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Respectfully submitted,

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