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Litigating Backstop Agreements: The Limits of Appellate Jurisdiction

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Chapter 11 debtors often enter into backstop agreements to obtain committed financing to fund an emergence from bankruptcy. Under a typical backstop agreement, one or more parties commit to providing all or a portion of exit debt or equity financing in the event that other parties that are first offered the opportunity to provide such financing (usually members of a class of creditors) elect not to do so. For debtors, a backstop agreement may provide a reasonable degree of certainty that the financing necessary to consummate — and make feasible — a chapter 11 reorganization plan is or will likely become available upon the plan's effectiveness. For the backstopping parties, participation in a debt or equity financing on attractive terms for an attractive fee — often payable either in cash, additional debt or equity (sometimes at a discounted value) of the reorganized debtor — has the potential to result in economic returns.

Despite their popularity in large and complex chapter 11 cases, backstop agreements have generated controversy, particularly when certain existing creditors are the backstopping parties and exclude other parties from becoming backstopping parties.[2] A recent district court decision in the *LATAM Airlines Group* chapter 11 cases underscores certain jurisdictional limitations that could impede, and may ultimately thwart, opposition to backstop agreements.[3] In *LATAM*, the district court held that a bankruptcy court's order approving a backstop agreement was interlocutory and not final, and therefore dismissed an appeal of the bankruptcy court's order for lack of jurisdiction.

Background of the *LATAM* Cases

LATAM Airlines Group SA, an airline headquartered in Santiago, Chile, that services passenger and cargo routes within Latin America and internationally, filed for chapter 11 in May 2020 in the U.S. Bankruptcy Court for the Southern District of New York amidst the COVID-19 pandemic, during which LATAM suffered a 95 percent reduction in its passenger-service revenues.[4]

In 2021, LATAM engaged in negotiations with its key stakeholders as part of a court-ordered mediation, which culminated in the execution of a restructuring-support agreement (the RSA) among LATAM, a creditor group (the "*ad hoc* group") holding approximately 70 percent of the unsecured claims against LATAM, and certain of LATAM's shareholders. The RSA obligated parties to support a chapter 11 plan for LATAM, a key component of which was a $5 billion new money financing that was to be raised through the issuance of new convertible notes and common stock and used to satisfy certain of LATAM's debt obligations and support its ongoing operations after exiting bankruptcy.[5]

To meet the financing needs of its chapter 11 plan, LATAM entered into two backstop agreements with the parties to the RSA. Under the backstop agreement with members of the *ad hoc* group, in exchange for the backstop parties' commitment to purchase any unsubscribed new convertible notes and common stock, LATAM was obligated to pay the *ad hoc* group backstopping parties more than $700 million in cash fees for backstopping a portion of the issuance and to reimburse the reasonable expenses of the backstopping parties.[6] Following a contested evidentiary hearing, the bankruptcy court issued a memorandum decision approving LATAM's entry into the backstop agreements on March 15, 2022, and entered the accompanying order (the "backstop order") on March 22, 2022.[7]

Opponents of the backstop agreements, including the official committee of unsecured creditors and an *ad hoc* group of unsecured creditors that was excluded from becoming a party to the other *ad hoc* group's backstop agreement, among other parties, appealed the bankruptcy court's decision to the U.S. District Court for the Southern District of New York. The opponents of the backstop order argued that the bankruptcy court erred in its application of the governing law, that the backstop agreement with

1 The authors thank Hope Goimarac and Wolfgang Jordi for their contributions to this article, which represents the views of the authors; the statements made herein are not those of their firm or its clients.

2 Philip D. Anker, "The Peabody Award: Exclusive Opportunism in Bankruptcy," *Mondaq* (Oct. 25, 2022), *available at* mondaq.com/unitedstates/insolvencybankruptcy/1243884/the-peabody-award-exclusive-opportunism-in-bankruptcy; Paul Silverstein, "Does an RSA with Plum Exit Financing Constitute Vote Buying? Examining the Peabody Situation," Creditors Rights Coalition (Oct. 23, 2022), *available at* huntonak.com/images/content/8/7/v2/87667/does-an-rsa-with-plum-exit-financing-constitute-vote-buying.pdf; Ingrid Bagby, Michele Maman, Casey John Servais, Richard Solow & Eric Waxman, "The Same, Only Better: Eighth Circuit Affirms Peabody Chapter 11 Plan Backstopped Rights Offering Despite Alleged Disparate Creditor Treatment Under Peabody Plan," *JD Supra* (Sept. 11, 2019), *available at* jdsupra.com/legalnews/the-same-only-better-eighth-circuit-71113 (links last visiting Feb. 22, 2023).

3 *In re LATAM Airlines Grp. SA*, 2022 No. 22-CV-2556 (JMF), 2022 WL 1471125, at *6 (S.D.N.Y. May 10, 2022).

4 *Id.*

5 *Id.* at 2.

6 *Id.* at 5-9.

7 *Id.* at 9-10.

members of the *ad hoc* group provided those parties with improper preferential treatment relative to other similarly situated unsecured creditors, and that the backstop fees payable to the backstopping parties were unreasonably high.[8]

Parties' Jurisdictional Arguments on Appeal

LATAM moved to dismiss the appeal for lack of appellate jurisdiction, arguing that the backstop order was interlocutory in nature, and therefore, the appeal of the order was impermissible. Under 28 U.S.C. § 158(a)(1), a district court's jurisdiction to hear appeals from a bankruptcy court is limited to appeals from "*final* judgments, orders, and decrees" or with leave of the court.[9] LATAM compared the appeal to a similar appeal in the *Peabody Energy* bankruptcy, where the Eighth Circuit Bankruptcy Appellate Panel (BAP) dismissed as interlocutory an appeal of a bankruptcy court order approving a backstop agreement.[10]

The Eighth Circuit BAP reasoned in *Peabody* that the order approving the backstop agreement was interlocutory because it did not resolve any distinct segment of the underlying bankruptcy proceeding, nor would any delay in appellate review until after plan confirmation prevent effective relief, because the issues raised in the backstop appeal could be preserved and reviewed as part of an appeal of a confirmation order.[11] LATAM adopted this reasoning by arguing that, as the bankruptcy court's confirmation of the plan was a condition precedent to funding under the backstop agreements, any "alleged inadequacies" with respect to the backstop agreements would be "render[ed] moot" should confirmation of the plan be denied.[12]

Because LATAM maintained that the bankruptcy court's order was interlocutory in nature, it submitted that the opponents were required to seek leave to file an interlocutory appeal under 28 U.S.C. § 158(a)(3). Under governing case law, leave is only warranted if the relevant order (1) involves a controlling question of law, (2) as to which there is substantial ground for difference of opinion, and (3) an immediate appeal from the order may materially advance the ultimate termination of the litigation.[13] The appellants took the position that all three of these factors were satisfied: (1) The issue was controlling because the backstop order was fully effective and was a question of law, as a bankruptcy court could not use its general authority to grant relief that other Bankruptcy Code provisions prohibit; (2) there was substantial ground for difference of opinion because two other bankruptcy judges in separate bankruptcy cases had rejected the reasoning leading to approval of the backstop order; and (3) guidance by the district court would materially advance the chapter 11 cases by requiring the debtors to submit backstop agreements in conformity with the law.[14]

LATAM argued that the standard for granting leave is "strictly applied" by the courts, and the party seeking leave to appeal "has the burden of showing exceptional circumstances" in order to "overcome the general aversion to piecemeal litigation and justify a departure from the basic policy of postponing appellate review until after the entry of a final judgment."[15] LATAM argued that the backstop order did not involve a controlling question of law, as the bankruptcy court's entry of the backstop order was the product of an extremely fact-intensive inquiry.[16] Moreover, according to LATAM, there were not substantial grounds for differences of opinion, as no other courts had ever ruled on the set of specific factual determinations unique to the backstop agreements at issue in *LATAM*.[17] Finally, LATAM argued that a reversal of the backstop order would complicate the proceedings around the confirmation of LATAM's plan.[18] Therefore, LATAM maintained, the appeal should be dismissed for lack of appellate jurisdiction.

In the alternative, the appellants argued that the backstop order was not interlocutory but final, as the hearing to approve the backstop agreements was a "discrete proceeding" within the larger bankruptcy case.[19] The appellants relied heavily on *Ritzen Group Inc. v. Jackson Masonry LLC*, in which the U.S. Supreme Court determined that a bankruptcy court order denying a creditor relief from the automatic stay was final.[20] The Court in *Ritzen* explained that such a discrete proceeding exists where a "motion initiates a discrete procedural sequence, including notice and a hearing, and the creditor's qualification for relief turns on [a] statutory standard," and that an order disposing of such a "proceeding" is "final" if it "disposes of a procedural unit anterior to, and separate from, [other defined] proceedings."[21]

The appellants submitted that the backstop order fulfilled these criteria because the debtors initiated a "discrete procedural sequence requesting approval of the Backstop Agreements and the authorization to use property of their estates under § 363 of the Bankruptcy Code, as well as obtaining administrative-expense authorization under § 503."[22] They also argued that the backstop order was the product of applying a statutory standard governing the relief sought and that the order was fully effective, with nothing further needed to be done to implement the order.

To support this position, the appellants pointed out that the order (1) authorized the debtors to perform their approved obligations and pay the fees granted thereunder; (2) granted relief from the automatic stay; (3) allowed the relevant obligations as administrative expenses; and

8 *Id.* at 20; *see also* 11 U.S.C. §§ 1129(a)(4), 1123(a)(4).
9 Memorandum of Law in Support of the LATAM Appellees' Motion to Dismiss for Lack of Appellate Jurisdiction (ECF No. 13), p. 8, *In re LATAM Airlines Grp. SA*, Case No. 22-CV-02556 (JMF) (S.D.N.Y. April 7, 2022).
10 *Id.* at 9 (citing *Ad Hoc Comm. of Non-Consenting Creditors v. Peabody Energy Corp.*, Case No. 16-42529 (ECF No. 2371) (B.A.P. 8th Cir. Feb. 8, 2017)).
11 *Ad Hoc Comm. of Non-Consenting Creditors v. Peabody Energy Corp.*, Case No. 16-42529 (ECF No. 2371) (B.A.P. 8th Cir. Feb. 8, 2017).
12 *Id.* at 9 (citing *In re Adelphia Commc'ns Corp.*, 333 B.R. 649, 656- 57 (S.D.N.Y. 2005)).
13 *Id.* at 14.
14 Opposition of Appellants, the Official Committee of Unsecured Creditors, the Ad Hoc Group of Unsecured Claimants, and Banco del Estado de Chile, in Its Capacity as Indenture Trustee under the Chilean Local Bonds Series A through D and Series E, to Appellee's Motion to Dismiss the Above-Captioned Appeals for Lack of Appellate Jurisdiction (ECF No. 26), pg. 12-16, *In re LATAM Airlines Grp. SA*, Case No. 22-CV-02556 (JMF) (S.D.N.Y. April 18, 2022).
15 *Id.* at 14 (citing *In re Liddle & Robinson*, 2020 WL 4194542, at *4 (S.D.N.Y. July 21, 2020)).
16 *Id.* at 15.
17 *Id.* at 16.
18 *Id.*
19 Opposition of Appellants, the Official Committee of Unsecured Creditors, the Ad Hoc Group of Unsecured Claimants, and Banco del Estado de Chile, in Its Capacity as Indenture Trustee Under the Chilean Local Bonds Series A through D and Series E, to Appellees' Motion to Dismiss the Above-Captioned Appeals for Lack of Appellate Jurisdiction (ECF No. 26), p. 8, *In re LATAM Airlines Grp. SA*, Case No. 22-CV-2556 (JMF) (S.D.N.Y. April 18, 2022).
20 *Id.* (citing *Ritzen Grp. Inc. v. Jackson Masonry LLC*, 205 L. Ed. 2d 419, 140 S. Ct. 582, 590-91 (2020)).
21 *Id.*
22 *Id.*

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(4) required the payment of various fees and a payment upon termination of the backstop agreements regardless of whether the plan was ultimately confirmed. The appellants claimed that language in *Ritzen* bolstered their position, to which the Supreme Court stated that "[i]t does not matter whether the court rested its decision on a determination potentially pertinent to other disputes in the bankruptcy case, so long as the order conclusively resolved the movant's entitlement to the requested relief."[23]

Appellate Jurisdiction Found to Be Lacking

The district court agreed with LATAM that the backstop order was interlocutory and not final, although it found the question to be "a close one." It reasoned that "without confirmation of the Plan, most of the substantive commitments laid out in the Backstop Agreements," such as the obligations of the backstop parties to fund their backstop commitments and the obligation of LATAM Airlines Group SA to pay the backstop fees, "will never become effective."[24] The district court found that the "interdependencies between the Backstop Agreements and confirmation of the Plan make plain that the Backstop Order did not resolve a discrete dispute within the overarching bankruptcy case."[25] In fact, the district court concluded that the issues raised by the appellants on appeal were "intertwined with and directly concern[ed]" the confirmation of the proposed plan, which supported the contrary position that the order did not finally resolve a discrete dispute.[26] The district court noted that in the bankruptcy court's memorandum decision approving the backstop agreements, the bankruptcy court explicitly reserved judgment on the appellant's chapter 11 arguments such that the order did not "definitively resolve" the disputes that were the subject of the appeal.[27]

In addition, the district court noted that "pragmatic considerations" weighed heavily against a finding of finality. The bankruptcy court was only one week away from its scheduled confirmation hearing for LATAM's proposed plan at the time of its decision, and the court expressed concern that "reviewing the Backstop Order on appeal concurrently with the Plan confirmation proceedings would likely cause the very 'delays and inefficiencies' that the rule of finality was designed to prevent."[28]

The district court rejected the contention by the appellants that *Ritzen* was dispositive, since the appellants failed to object solely to the portion of the backstop order that modified the automatic stay, which was the central issue in *Ritzen*.[29] Even if the appellants had objected solely to that portion of the backstop order, the court found that *Ritzen* is distinguishable, since there was no motion for or separate "distinct" proceeding regarding relief from the automatic stay, and the order merely "modified" the automatic stay to a limited extent necessary to enable performance under the backstop agreements.

The appellants argued that the backstop order "conclusively resolved" LATAM's "entitlement to the requested relief" under § 363. In addition, § 503 failed to sway the district court, which noted that the appellants focused almost exclusively on the chapter 11 issues in their appeal and failed to narrow their appeal to the §§ 363 and 503 issues exclusively. Had they done so, the court "might well have reached a different conclusion with respect to finality."[30]

Lastly, the district court rejected the appellants' argument that the court should grant them leave to appeal the backstop order as an interlocutory order under 28 U.S.C. § 158(a)(3).[31] The district court held that it was "doubtful" that the appellants satisfied any of the three requirements for leave, but that the appellants plainly failed the third prong. The court found that resolving issues raised by appellants on appeal before the bankruptcy court even had a chance to meaningfully consider them in connection with plan confirmation would not "materially advance the ultimate termination of the litigation."[32]

Takeaways

In the end, the *LATAM* decision supports the proposition that appellate jurisdiction may be lacking where parties appeal orders approving backstop agreements on various grounds related to plan confirmation before a confirmation hearing. Nevertheless, the decision's language suggests that jurisdiction may have existed had a more targeted appeal been made with respect to only certain portions of the backstop order on narrower grounds — those relating to authorization to use property of the debtors' estates under § 363 and obtaining administrative-expense authorization under § 503. abi

23 *Id.*
24 *In re LATAM Airlines Grp. SA*, No. 22-CV-2556 (JMF), 2022 WL 1471125, at *10 (S.D.N.Y. May 10, 2022).
25 *Id.* at 18.
26 *Id.* at 29 (citing *In re Energy Future Holdings Corp.*, 949 F.3d 806, 817-18 (3d Cir. 2020)).
27 *Id.* at 23.
28 *Id.* at 25.
29 *Id.* at 27.
30 *Id.* at 29-30.
31 *Id.* at 33-34.
32 *Id.*