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# *Flintkote and Section 524(g)'s Ongoing-Business Requirement*



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A recent decision by the United States Bankruptcy Court for the District of Delaware sheds light on what constitutes a ''viable, going concern business'' for purposes of a reorganization under Bankruptcy Code Section 524(g). In *In re Flintkote Co.*,[1] the court held that a debtor need not continue in its prepetition line of business to meet any ''ongoing business'' requirement that may be implicit in § 524(g) but instead may engage in any business that will afford just recoveries to the debtor's future claimants. The outcome in *Flintkote* thus reflects a practical understanding of the statute, one recognizing that the rights of future claimants must be central to any reorganization under § 524(g) and that a reorganizing debtor should not be forced to continue with the business that drove it into bankruptcy.

Section 524(g) serves the dual purposes of enabling a debtor drowning in asbestos liability to restructure and emerge as a viable business entity and providing suitable funding to pay equitably the claims of current and future victims of asbestos-related diseases.[2] Reorganizing under § 524(g) allows for a permanent injunction that channels the asbestos claims against the debtor to a settlement trust for resolution and payment.[3] The statute conditions issuance of this channeling injunction on multiple requirements, including certain findings about the debtor's liability and adequate protections for future claimants.[4]

In *Flintkote*, a debtor (''Flintkote''), formerly a manufacturer of asbestos-containing building materials, sought to reorganize under § 524(g) and planned to pursue five lines of business after its emergence from bankruptcy: (1) purchasing and leasing real estate for ''quick-service restaurant properties,'' including McDonald's and Burger King; (2) providing consulting and executive-management services to other companies facing asbestos-related bankruptcies; (3) providing claims-management services to trusts established under § 524(g); (4) providing administrative services to trusts established under § 524(g); and (5) pursuing litigation against Imperial Tobacco Canada Limited (''ITCAN''), Flintkote's former parent corporation.[5]

ITCAN objected to confirmation of a plan of reorganization based on these new businesses, arguing that § 524(g) implies an ''ongoing business'' requirement and that this requirement can be met only by Flintkote's continuing a viable prepetition business after confirma-

[1] *In re Flintkote Co.*, No. 04-11300 (JKF) (Bankr. D. Del. Dec. 12, 2012).

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[2] *In re Federal-Mogul Global Inc.*, 684 F.3d 355, 359 (3d Cir. 2012).

[3] 11 U.SC. § 524(g)(1)(A).

[4] *Id.*; *see also* 11 U.S.C. § 524(g)(2)(B)(ii).

[5] *Flintkote*, slip op. at 8–11. As of the confirmation hearing, the only client Flintkote was able to identify for its claims-management and trust-administration businesses was the debtor's own unconsummated § 524(g) trust, though the debtor was attempting to expand its clientele. *See id.* at 10–11.

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tion.[6] According to ITCAN, the legislative history is clear that § 524(g) requires the continuation of a prepetition business ''because § 524(g) was intended only to protect otherwise successful companies from the threat of crippling asbestos liability.''[7]

As the *Flintkote* court recognized, other courts have wrestled with whether § 524(g) should in fact be read to imply such an ''ongoing business'' requirement. The Third Circuit has reasoned in dicta that the '' 'implication of [§ 524(g)(2)(B)(i)(II)] is that the reorganized debtor must be a going concern,' ''[8] while the Bankruptcy Court for the Southern District of New York in *In re Quigley Co*. declined to impose such an ''ongoing business'' requirement.[9] The debate over the ongoing-business requirement arises in the first instance from § 524(g)(1)(A), which provides that a bankruptcy court may issue a channeling injunction ''to supplement the injunctive effect of a discharge under this section.''[10] Section 1141(d) in turn provides that ''a debtor will not receive a discharge upon confirmation if 'the debtor does not engage in business after consummation of the plan.' ''[11] Read together, §§ 524(g) and 1141(d) give rise to the implication that a debtor must engage in business after confirmation to qualify for a channeling injunction.[12] Section 524(g)(2)(B)(i)(II), which requires that a § 524(g) trust be funded by the debtor's securities and by the debtor's obligation ''to make future payments, including dividends,'' may also support the conclusion that a debtor availing itself of § 524(g) must maintain an ongoing business.[13]

In *Flintkote*, the court took a pragmatic approach to addressing the ongoing-business issue and, in doing so, may have provided a helpful template for other courts confronting the same question in the future. While the *Flintkote* court was willing to accept that § 524(g) likely implies an ongoing-business requirement, the court ultimately determined that there are many ways such a requirement, if it exists, can be met: a debtor's ''ongoing business'' need not be the same business the debtor engaged in prepetition. Nothing in § 524(g), § 1141, or Third Circuit precedent required a debtor to ''continue to engage in a pre-petition (and possibly unsuccessful) business to the exclusion of any other.''[14] The court in fact found ''nothing improper about a debtor adapting its business model while in bankruptcy'' and noted that in its experience ''most companies that successfully reorganize undertake some type of business 'reorganization.' ''[15]

Moreover, the *Flintkote* court noted that § 524(g) includes a number of express requirements to qualify for an injunction and thus reasoned that if Congress had intended to require a debtor to continue a prepetition business, it would have said so.[16] The court embraced a practical view of § 524(g), reflecting an awareness that § 524(g) was not ''intended only to protect'' companies facing asbestos liability, as ITCAN had claimed. Instead, ''the point of engaging in business is to provide an evergreen source of funds for the trust [to] ensure that in the face of long latency periods for asbestos-related illnesses, all claimants, current and future, receive just and comparable compensation for their injuries, which is a primary purpose of § 524(g).''[17]

*Flintkote* also provides useful guidance on what factors will support a finding that a given post-confirmation activity will qualify as a ''business'' under §§ 524(g) and 1141 so as to accomplish this ''primary purpose.'' The *Flintkote* court found the transition here from manufacturing building materials to leasing out real property was acceptable because (1) every creditor agreed with the choice of business (with only ITCAN objecting);[18] (2) Flintkote had in fact previously leased real property to third parties in the 1980s (though that aspect of its business had since been discontinued);[19] (3) Flintkote had been operating the new business successfully for some time before the confirmation hearing;[20] (4) Flintkote's CEO and president had twenty years of experience in the quick-service food industry;[21] and (5) Flintkote was not merely passively investing but was actively seeking properties, evaluating tenants, inspecting properties, monitoring financial performance, and collecting and distributing rents, among other things.[22] Similarly, the court also accepted Flintkote's consulting and executive-management services as a viable post-petition business.[23] There, the court appeared to find most significant that Flintkote was successfully operating the business for some time before the confirmation hearing under an extant agreement with an outside party through which Flintkote had already received nearly a million dollars.[24]

In contrast, the *Flintkote* court affirmatively determined that the debtor's fifth proposed business—litigation against ITCAN—did not count: ''simply pursuing or managing a lawsuit . . . in pursuit of an asset'' was not a going-concern business.[25] The court expressed no opinion whether Flintkote's claims-processing and trust-services businesses, which had no clients other than Flintkote's own § 524(g) trust, qualified as ''businesses.''[26] These were precisely the sort of activities at issue in *Quigley*, where, as noted above, the Bankruptcy Court for the Southern District of New York declined to impose an ''ongoing business'' requirement in the first place.[27] Both courts' reluctance to address that particular issue suggests they were skeptical that an enterprise without any unaffiliated clients or customers could qualify as a ''business'' under § 524(g).

Effectively, *Flintkote* permits a debtor reorganizing under § 524(g) to pursue the business it chooses as long as that business can stand on its own and will allow the debtor to contribute to a trust that has enough funding

[6] *Id.* at 42–43, 45–46.
[7] *Id.* at 46.
[8] *Id.* at 44 (quoting *In re Combustion Eng'g, Inc.*, 391 F.3d 190, 248 (3d Cir. 2004)).
[9] *See id.* at 45 (citing *In re Quigley Co.*, 437 B.R. 102, 141 (Bankr. S.D.N.Y. 2010)).
[10] *Id.* at 43; *see also* 11 U.S.C. § 524(g)(1)(A).
[11] *Flintkote*, slip op. at 43–44 (quoting 11 U.S.C. § 1141(d)).
[12] *See id.*
[13] *Id.* at 44; *see also* 11 U.S.C. § 524(g)(2)(B)(i)(II).
[14] *Flintkote*, slip op. at 46.
[15] *Id.* at 50.
[16] *Id.* at 47–48.
[17] *Id.* at 50.
[18] *Id.* at 51.
[19] *Id.*
[20] *Id.*
[21] *Id.*
[22] *Id.* at 51–52.
[23] *Id.* at 52.
[24] *See id.*
[25] *Id.* at 53.
[26] *Id.*
[27] *See id.* at 64 (citing *In re Quigley Co.*, 437 B.R. 102, 121–22 (Bankr. S.D.N.Y. 2010)).

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to compensate future claimants fairly.[28] That result is entirely in keeping with the spirit of § 524(g) and reflects a practical understanding of the needs of debtors reorganizing under § 524(g) and the centrality of future claimants under the statutory scheme. Companies facing asbestos liability, as well as courts confronting the ''ongoing business'' debate, may be well advised to consider the court's deft handling of the issue in *Flintkote*.

[28] The court recognized that Flintkote needed to demonstrate that its businesses were ''profitable'' to satisfy the requirements of § 1129(a)(11) as well as to show that it could make the ''future payments, including dividends'' required under § 524(g)(2)(B)(i)(II). *See id.* at 42–43, 72–75.