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Indianapolis Downs—A Flexible Approach to Consensual Releases

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Besides cold hard cash, releases are often the most sought after consideration provided in a plan of reorganization. All the significant players in a Chapter 11 case want to receive (and fight hard for) a release, waiver and discharge of any and all claims, obligations, and causes of actions from not only a Chapter 11 debtor, but also from third parties in connection with confirmation of a Chapter 11 plan. Third party releases, however, have been the subject of inquiry and scrutiny by bankruptcy courts and Offices of the United States Trustee throughout the United States to ensure that third parties do not find that they have unexpectedly waived potentially valuable claims without receiving some form of consideration in exchange for granting the release.[1] It is easy to determine that a third party release is consensual when the releasing party votes in favor of a Chapter 11 plan. In contrast, it is not so easy to determine whether a release is consensual when the releasing party abstains from voting or casts a ballot rejecting a Chapter 11 plan. In a recent ruling, *In re Indianapolis Downs, LLC*, The Honorable Brendan Linehan Shannon of the United States Bankruptcy Court for the District of Delaware added another opinion to the precedential pile that debtors, lenders and other oft-released parties use as support for confirmation of plans that bind wide and varied swaths of constituencies to third-party releases.

On January 31, 2013, Judge Shannon issued an opinion in *In re Indianapolis Downs, LLC*[2] that confirmed the debtor's Chapter 11 plan over objections filed by the Office of the United States Trustee for the District of Delaware (the "*U.S. Trustee*") and a collection of related entities holding claims against and equity interests in the debtor (collectively, the "*Oliver Parties*"). Although many that read and analyze Judge Shannon's opinion will undoubtedly focus on the analysis and holding overruling the request to designate the votes of the debtor's two main creditor constituencies based on their entry into a postpetition restructuring support agreement with the debtor (which is significant in its own right), equally as significant is the Court's ruling that third party releases can be consensual even without an affirmative act by the third party. This opinion represents a departure from the recent decision in *In re Washington Mut. Inc.*[3] and the adoption of a flexible approach to analyzing third party releases.

The Chapter 11 Case, the Restructuring Support Agreement and the Chapter 11 Plan

The debtor operates a "racino," which is a combination casino and racetrack, outside of Indianapolis, Indiana. On April 7, 2011, the debtor commenced its Chapter 11 case after unsuccessfully restructuring its debt outside of the Chapter 11 process. Other than a couple of skirmishes early on, the first year of the debtor's case was not out of the ordinary. However, on April 25, 2012, the ground work for the debtor's emergence from Chapter 11 began to take shape. Specifically, consensus was achieved among the debtor and its two main creditor constituencies on a dual-path approach to the debtor's emergence from Chapter 11. That consensus was embodied in the terms of a restructuring support agree-

[1] The inquiry and scrutiny many times begins at the hearing to consider approval of the disclosure statement as was the case in *In re Velo Holdings Inc.* (S.D.N.Y. Case No. 12-11384-mg) when The Honorable Martin Glenn specifically raised questions and concerns with respect to the deemed consent releases in the Chapter 11 plan prompting the debtor to make certain revisions to the proposed release provisions in advance of solicitation and confirmation.

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[2] Case No. 11-11046 (BLS), Chapter 11, 2013 BL 26601 (Bankr. D. Del. Jan. 31, 2013).

[3] 442 B.R. 314 (Bankr. D. Del. 2011) (hereinafter, "*Washington Mutual*").

ment, which provided, among other things, that the debtor would develop and run a marketing process to determine whether bids for its assets would be attractive enough to garner support from those creditor constituencies, but, if the marketing process failed to yield sufficient offers, then the debtor would proceed with a recapitalization according to the terms agreed to in the restructuring support agreement. To implement the dual-path approach, the Chapter 11 plan filed and solicited by the debtor provided for a toggle between a sale and a recapitalization, depending on the values received in connection with the marketing process. Importantly, the plan also provided for releases of claims and causes of action, among other things, by the debtor and third parties holding claims against the debtor.

Objections to the Chapter 11 Plan

The Oliver Parties filed an objection to confirmation of the Chapter 11 plan that included a laundry list of plan infirmities that purportedly violated numerous provisions of the Bankruptcy Code. Of particular relevance, the Oliver Parties contested confirmation of the Chapter 11 plan on the basis that the Chapter 11 plan's third party releases and exculpation provisions violated Section 524(e) of the Bankruptcy Code. The U.S. Trustee also objected to the release and exculpation provisions of the Chapter 11 plan asserting that the third party release provision was ''overbroad, overinclusive and impermissible.''[4]

The Court's Ruling and Analysis

The standard by which the propriety of third party releases in Chapter 11 plans is measured has developed through case law over recent years. Notwithstanding the United States Court of Appeals for the Third Circuit declining to establish a *per se* rule against nonconsensual third party releases in *Gillman v. Continental Airlines (In re Continental Airlines)*,[5] the distinguishing factor in many of the decisions addressing whether to approve releases is whether the third party releases are consensual or non-consensual. That is why the Oliver Parties asserted that the Chapter 11 plan impermissibly contained non-consensual third party releases in violation of Section 524(e) of the Bankruptcy Code, thus rendering the plan unconfirmable.

The debtor, here, however, was careful in drafting the Chapter 11 plan's third party release provisions. The Chapter 11 plan's third party releases were drafted such that the third party releases only applied to holders of claims against the debtor that (i) voted to accept or reject the Chapter 11 plan and did not opt out of granting the releases, (ii) were unimpaired and deemed to accept the Chapter 11 plan, or (iii) abstained from voting on the Chapter 11 plan and did not submit a ballot opting out of the releases.[6] Importantly, if a party was deemed to have rejected the Chapter 11 plan or opted out of the releases, the third party releases did not bind that party.

The debtor also highlighted in the Chapter 11 plan and accompanying disclosure statement the existence of the third party releases. The third party release provisions in the Chapter 11 plan and disclosure statement were in bold, capitalized and, in certain areas to denote key phrases, underlined. The ballots also included clear and detailed instructions regarding how to opt out of the releases in order to protect a claimant from inadvertently consenting to the releases.

Before analyzing whether to approve the Chapter 11 plan's third party releases, Judge Shannon undertook the preliminary step of determining whether the Oliver Parties had standing to contest the third party releases. The Oliver Parties voted to reject the Chapter 11 plan and opted out of the granting the releases. Having opted out of the granting the releases, the third party releases no longer affected the Oliver Parties' direct interests, and therefore the Oliver Parties lacked standing to contest the third party releases.[7] Although Judge Shannon concluded that the Oliver Parties lacked standing, the objection from the U.S. Trustee remained to be decided.

If one were to analyze the decision in *Washington Mutual* with respect to releases, the take away would be that in order for releases by creditors to be consensual, the third party must vote to accept the plan.[8] It is therefore not surprising that both the U.S. Trustee and the Oliver Parties in their objections relied on the decision in *Washington Mutual* for the assertion that affirmative consent is required and in the absence of affirmative consent, the releases were non-consensual and did not meet the standards for non-consensual releases. But, as Judge Shannon noted, ''no such hard and fast rule applies.''[9] In fact, the *Washington Mutual* decision is at odds with the ''flexible approach'' taken by other courts in determining whether the third party releases are consensual or non-consensual. For example, the court *In re Spansion, Inc.* held that the act of returning a ballot was not necessary to demonstrate that a release was consensual if the third party was deemed to have accepted the plan.[10] Similarly, the court in *In re DBSD N. Am., Inc.*, relying on the decisions in *Calpine* and *Conseco*, determined that releases by third parties that abstained from voting and did not opt out were consensual because adequate notice of the proposed release had been given and the ballots contained a description of what would occur if the claimant failed to opt out of the release.[11]

Act or Forever Release

Judge Shannon, relying on the principles articulated in *Spansion*, *DSBD*, *Calpine* and *Conseco*, decided because no firm rule applies, it was appropriate to apply a flexible approach to determining whether third party releases are consensual or non-consensual. In applying a flexible approach, Judge Shannon ruled that the third party releases in the Chapter 11 plan were consensual even if the third party did not affirmatively act (i.e., abstained from casting a vote).[12] Reading between the lines of the decision, by forgoing to vote on the plan, a party essentially had acted, rendering the release consensual. Further, if the third party cast a vote rejecting the Chapter 11 plan, but did not take the affirmative act

[4] *In re Indianapolis Downs, LLC*, 2013 BL 26601 at *15.
[5] 203 F.3d 203, 214 (3d Cir. 2000).
[6] *In re Indianapolis Downs, LLC*, 2013 BL 26601 at *16.
[7] *Id.* at *15.
[8] *In re Washington Mut'l Inc.*, 442 B.R. at 352.
[9] *In re Indianapolis Downs, LLC*, 2013 BL 26601 at *16-17.
[10] *In re Spansion, Inc.*, 426 B.R. 114, 144 (Bankr. D. Del. 2010).
[11] *In re DBSD N. Am., Inc.*, 419 B.R. 179, 218-19 (Bankr. S.D.N.Y. 2009).
[12] *In re Indianapolis Downs, LLC*, 2013 BL 26601 at *17.

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to opt-out of the release, then the releases were rendered consensual.

Judge Shannon's ruling is significant in that it represents a departure from *Washington Mutual's* rigid interpretation and analysis of consensual versus nonconsensual releases and expands the opportunities for plan proponents to argue that a broader array of third party releases constitute consensual releases. Accordingly, a claimant, if given the opportunity, must act or take the risk of forever releasing particular parties of claims and causes of action.