YOUNG CONAWAY

Bankruptcy Case Alert:
Judge Goldblatt Considers Consensual Releases Post-*Purdue*

In *In re Smallhold, Inc.*,[1] Judge Goldblatt of the Bankruptcy Court for the District of Delaware became the latest judge to weigh in on the issue as to whether an "opt out" mechanism in a plan constitutes a consensual third-party release. Judge Goldblatt deemed creditors who voted on the plan but did not opt out by checking a box on the ballot as consenting to the releases, focusing on the affirmative act of voting coupled with clear and conspicuous language regarding the release. With that same focus in mind, Judge Goldblatt held that creditors who did not return a ballot or "unimpaired" creditors who were not solicited did not consent to the plan's third party releases. Notably, though, Judge Goldblatt left open the possibility for a plan to "build[] in the protections of Rule 23(b)(3), under which a named representative is authorized to act on behalf of a class, subject to the rights of unnamed members to receive notice and opt out."[2]

The Court Considers Opt-Out Mechanisms.

In *Purdue Pharma*, the Supreme Court barred nonconsensual third party releases (with the exception, of course, to asbestos cases under § 524(g) of the Bankruptcy Code).[3] Following the *Purdue* ruling, bankruptcy courts are now grappling with the issue as to what constitutes consent to a proposed third party release. Some courts have held that creditors are affirmatively required to "opt in" to a plan release while other courts have concluded that, so long as the creditor was clearly and conspicuously informed, the failure to "opt out" would operate a release of third-party claims, such a release would be effective against any creditor who returned a ballot but did not check a box to "opt out" of the third-party release.

Previously, in *In re Arsenal Intermediate Holdings, LLC*, Judge Goldblatt approved the opt-out mechanism, stating that "so long as [a] disclosure is prominent and conspicuous, and . . . creditors are given the ability to opt out simply by marking their ballot or by some other comparable device, it is appropriate to infer consent from a creditor's failure to opt out."[4] In that case, Judge Goldblatt's view was that a third-party release is just like any other plan provision.[5] He reasoned that because "[c]reditors who are validly served with a plan and who take issue with . . . [a] third-party release are required to speak up," a creditor who fails to speak up may be "defaulted," which aligns with the

[1] Case No. 24-10267 (CTG)
[2] *Id.* at 7.
[3] *See Harrington v. Purdue Pharma L.P.,* 144 S. Ct. 2071 (2024).
[4] *Id.* at 23; *In re Arsenal Intermediate Holdings, LLC*, No. 23-10097 (CTG), at 1-2 (Bankr. D. Del. March 27, 2023) [D.I. 176].
[5] *See Smallhold*, No. 24-10267, at 2.

established bankruptcy practice of "defaulting" parties that do not raise objections.[6]

In *Smallhold*, Judge Goldblatt found that after the *Purdue Pharma* decision, "a third-party release is no longer an ordinary plan provision that can properly be entered by 'default' in the absence of an objection."[7] As a result, "it is no longer appropriate to require creditors to object or else be subject to (or be deemed to 'consent' to) such a third-party release."[8] Instead, Judge Goldblatt followed the reasoning of the *Ebix* court, which concluded that third-party releases "were only appropriate in circumstances in which, following a contract model, there was evidence of an agreement to grant the release."[9]

The Court Emphasizes the Limits of Purdue's Scope and Leaves Open the Possibility for "Full Pay" Plans and Future/Unknown Claimant Representatives.

Even though he rejected one form of opt-out release in *Smallhold*, Judge Goldblatt also emphasized that "the sky is not falling" for debtors and their affiliates seeking finality.[10] He noted that *Purdue* "does not affect the practice of exculpation of estate fiduciaries (which is expressly authorized by Third Circuit precedent) or prevent a debtor in appropriate circumstances from releasing estate causes of action, which under Third Circuit law would eliminate veil-piercing liability."[11] Moreover, *Purdue* "also left open the possibility that a nonconsensual third-party release might be appropriate in a 'paid-in-full plan,'" according to Judge Goldblatt, who also appreciated that "there may be a common sense to the notion that creditors who have suffered a single, indivisible injury, caused jointly by the debtor and non-debtors, and whose claims on account of that injury have been satisfied in full out of the bankruptcy estate, ought not be permitted to assert those same claims against non-debtors."[12]

Judge Goldblatt also clarified that nothing in the opinion "should be construed to foreclose reaching a different outcome" in a different context.[13] Judge Goldblatt specifically noted that there may be merit to the point that "in the mass tort context, particularly in a case in which there is a factual basis for a court to make findings akin to those that a court makes when it certifies a Rule 23(b)(3) class action, a bankruptcy court can and should treat an estate fiduciary as a class representative, giving that representative the authority to bind absent class members, subject to those members receiving individual notice and being afforded the opportunity to opt out."[14]

[6] *Id.* at 3, 22.
[7] *Id.* at 4.
[8] *Id.* at 25.
[9] *Id.* at 30 (citing *In re Ebix, Inc.*, Bankr. N.D. Tex. No. 23-80004, Aug. 2, 2024 Hr'g Tr.).
[10] *Id.* at 7.
[11] *Id.*
[12] *Id.* at 32.
[13] *Id.* at 36.
[14] *Id* at 35.