By Thomas J. Salerno

SCOTUS's *MOAC*: A Bombshell or a Sputtering Firecracker?

"The road is long, with many a winding turn. That leads us to who knows where? Who knows where?"
— The Hollys, "He Ain't Heavy, He's My Brother" (1969)

I have to confess that 40 years of law practice has been a real buzzkill when I watch movies now that involve the civil legal system. The climactic end scene is usually the underdog defeating the immoral corporate giant as the jury verdict is announced, scowling big firm attorneys vowing to appeal, tears of relief and gratitude flowing freely, fade to black, end credits. It's great cinema, and leaves the audience with the sense of closure (and justice).

However, we all know real life is just not that neat and tidy. The movie's realistic sequel would be a critically panned effort involving myriad post-trial motions, stay orders, appellate briefings, possible reversals and remands, and in some instances, the same trial court drama, part II. Possibly a bankruptcy filing, if all else fails. Not nearly as exciting, as everyone's older and less filled with moral outrage, but it is the system. As such, I always find myself wondering what becomes of a case after the movie version ends. This brings me to the U.S. Supreme Court's pronouncement in *MOAC Mall Holdings v. Transform Holdco*.[1]

Thomas J. Salerno
Stinson LLP; Phoenix

Thomas Salerno is a partner with Stinson LLP in Phoenix and a past ABI Vice President-Development.

Setting the Stage

MOAC arose from a very common situation seen daily in bankruptcy cases around the nation, from the simplest to the most complex. The § 363 sale (or in *MOAC*, a § 365 assignment of a lease, which also implicates § 363), dubbed by critics and admirers alike as the "new chapter 11." This particular transaction arose from the Sears chapter 11, which has to qualify for the most prolonged, tortuous liquidation of any retail operation in history.

Transform Holdco acquired myriad assets (leases and other things) from Sears, which held a lease from the Mall of America (or more accurately, MOAC Mall Holdings LLC). Transform sought to assign the MOAC lease to Transform's wholly owned subsidiary; MOAC objected on the basis that there was no showing of adequate assurance of future performance as required under § 365(f)(2)(B). The bankruptcy court approved the assignment.

MOAC sought a stay pending appeal because it was concerned Transform would invoke the protections of § 363(m) and, absent a stay, moot any potential appeal.[2] To defeat the stay motion, Transform represented that it would not seek to invoke the mootness arguments of § 363(m), and the stay was denied. As it turns out, simply put, Transform lied.[3]

On appeal, the district court agreed with MOAC on the merits of its § 365(f) argument. Undeterred, Transform sought a rehearing and, for the first time, invoked the mootness protections under § 363(m). Transform argued that § 363(m) was jurisdictional in nature, thereby precluding appellate review. While the district court was not amused at Transform's use of this argument after its representations that it would not do so (in fact, the district court was "appalled"),[4] it felt bound by Second Circuit precedent and dismissed the appeal under the principles of § 363(m) on the grounds that the district court no longer had jurisdiction over the appeal.[5] The Second Circuit affirmed. MOAC appealed to the Supreme Court.

Supreme Court's Ruling

A unanimous Supreme Court, resolving a split among the circuits,[6] determined once and for all that § 363(m) was not jurisdictional in nature (*i.e.*, it did not deprive appellate courts of jurisdiction to hear and adjudicate an appeal implicating § 363). Congress had not made the restrictions in § 363(m) explicit as a jurisdictional bar, and the courts should not interpret it as such. The Court then disposed of the matter as appellate courts are inclined and able to do, stating, "We vacate [the Second Circuit]

1 *MOAC Mall Holdings LLC v. Transform Holdco LLC*, 143 S. Ct. 927 (2023).

2 Section 363(m) provides that the "reversal or modification on appeal of an authorization under subsection (b) ... [permitting non-ordinary-course-of-business sales, uses or leases of estate property] ... of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal."

3 For a good overview of the case, *see* Thomas Loeb & Carrie Brosius, "Bankruptcy Sales Uncertain After Justices' Section 363 Ruling," *Law360* (April 27, 2023).

4 Litigants misrepresenting positions to gain immediate tactical advantage is a tale as old as time. The district court's outrage is reminiscent of Captain Louis Renault (Claude Rains) telling Rick Blaine (Humphrey Bogart) in *Casablanca* that he was "[s]hocked to find that gambling [was] going on in here"; because the issue was one of jurisdiction, the misrepresentation was not deemed one to which judicial estoppel or waiver would apply.

5 *See MOAC Mall Holdings LLC v. Sears Holding Corp. (In re Sears Holdings Corp.)*, 2021 U.S. App. LEXIS 37358 (2d Cir. Dec. 17, 2021).

6 Specifically, both the Third and Eleventh Circuits have held that § 363(m) is not jurisdictional in nature, which conflicts with the Second Circuit at issue in *MOAC*. *See In re Energy Future Holdings Corp.*, 949 F.3d 806, 820 (3d Cir. 2020); *In re Stanford*, 17 F.4th 116, 122 (11th Cir. 2021).

judgment, and remand the case for further proceedings consistent with this opinion." This is the judicial equivalent of "it ain't my problem anymore — you work it out," and illustrates the adage about excrement flowing downhill. It is the "further proceedings consistent with the opinion" that is the subject of this article.

So, Where Do Litigants Go from There?

The Second Circuit now has to address the issues that it felt it was jurisdictionally barred from addressing in disposing of the first appeal by MOAC. Similar to the aforementioned movie scenario, I cannot help but wonder what that looks like. It seems that this will graphically highlight the fundamental difference between a legal right and an effective remedy.

The Supreme Court's *MOAC* decision clearly defines that there is no jurisdictional bar precluding an appeal of an order that implicates § 363 (let's call it a "§ 363 order").[7] As there is no jurisdictional bar, the issues on appeal can move forward despite a closing of the transaction at issue (assuming that no stay pending appeal is in place). There is no doubt that the Second Circuit will push the ball down to the district court, which may (or may not, based on the discussion in the district court's previous opinion) push it to the bankruptcy court, thereby completing the great circle of life.

After eliminating the jurisdictional issues (which are now clearly defined), then what? Where does this road lead? It seems that there are still two material hurdles for the appellant of a § 363 order.

First, was there some failure to comply with a specific statutory requirement for a sale under § 363 or for assumption/assignment of an executory contract under § 365? Let's call this the "statutory defect."

Second, even assuming that there was some statutory defect, was the purchaser/assignee a "good faith" purchaser/assignee? If so, notwithstanding a statutory defect, what remedy precisely can the reviewing court provide if the reversal or modification of the sale order cannot (by statute) "affect the validity of the sale or lease?" Let's call this the "effective remedy." Put another way, even if there is some reversal, will the effective remedy materially impact the buyer? I speculate that in appeals of § 363 orders, after an appellate court rules on an alleged statutory defect, it will remand to the lower court for "further proceedings consistent with the ruling" (*i.e.*, to figure out the effective remedy).

What is the likely global impact on § 363 sales? I predict that the market will quickly adapt; deals are out there, and risks are to be evaluated in every transaction. *MOAC* will not spell certain death for § 363 sales. In addition, I also predict that there will be the following four market reactions.

"Good-Faith Purchaser" Status Is Critical!

Preliminarily, buyers/assignees in cases that will result in § 363 orders will be well-advised to pay real attention to a proper evidentiary basis for the bankruptcy court's determination that the buyer/assignee is a good-faith purchaser under § 363(m). This was always a critical component of any protection available to the buyer/assignee, but is often thrown in as an afterthought to the sale motion and order, sometimes without a lot of specific thought or evidence in support of the sales/assignments. Real evidence is needed to support the record and the bankruptcy court's finding on "good faith."[8] Overturning a § 363 order based on clear error of a factual finding of good faith will be much more difficult than the *de novo* review of any legal issues such as the statutory defects.

Equitable Mootness Will Still Be Available

The *MOAC* decision only dealt with the issue of statutory mootness because that was the sole issue upon which the Second Circuit ruled. Given the circumstances of the *MOAC* case (with the appellant relying on § 363(m) after representing that it would not do so to defeat the motion for a stay pending appeal), one has to assume that any equitable-mootness argument by Transform will face a decidedly unsympathetic audience on remand. The "appalled" district court will most assuredly not be amused having to deal with Transform yet again. In any event, equitable mootness was not fully analyzed in *MOAC* (at any appellate level in that case) because of the binding nature of the now-reversed Second Circuit precedent on statutory mootness.[9]

The foregoing notwithstanding, in other cases one has to wonder whether equitable mootness (while not nearly as direct as statutory mootness) will be relied on to effectively thwart appeals. This doctrine is much more discretionary and, therefore, much less of a sure bet. One particularly interesting case is *Clear Channel Outdoor Inc. v. Knupfer*,[10] where the Bankruptcy Appellate Panel (BAP) for the Ninth Circuit issued a decision on a debtor's ability to sell its assets "free and clear" of "out of the money" junior liens under § 363(f) of the Bankruptcy Code.

In *Clear Channel*, the BAP considered whether the appeal was equitably moot. Equitable mootness involves a determination that the appellate relief becomes moot "when it is impossible for a court to grant any effectual relief whatever to the prevailing party."[11] In evaluating whether the appeal was equitably moot, the BAP analyzed "the consequences of the remedy and the number of third parties who have changed their position in reliance on the order that is being appealed."[12] Equitable mootness typically focuses on the difficulty of "unscrambling the egg" after a sale has been closed and the money changes hands.

The BAP in *Clear Channel* acknowledged that certain changes had taken place since the sale was closed. Those

7 This can encompass assumptions and assignments of executory contracts under § 365, as the Supreme Court clearly held (consistent with the statute involving both sales and leases) that § 363(m) applies equally in executory contract orders under § 365 and asset-sale orders under § 363.

8 *See, e.g., In re M Cap. Corp.*, 290 B.R. 743, 745 (B.A.P. 9th Cir. 2003) ("We publish this order to underscore the need for parties who desire the protection of section 363(m) to establish an evidentiary record for the bankruptcy court to make the necessary findings of fact and conclusions of law. Correlatively, the opponent of good faith does not have the burden to demonstrate the absence of good faith. Without the requisite determination, we do not assume section 363(m) good faith and must deal with the merits of these appeals without such limitation.").

9 The Supreme Court "declin[ed] to act as a court of 'first view'" with respect to equitable mootness in that case.

10 *Clear Channel Outdoor Inc. v. Knupfer (In re PW LLC)*, 391 B.R. 25 (B.A.P. 9th Cir. 2008).

11 *Chafin v. Chafin*, 568 U.S. 165, 172 (2013); *see also* Mark Salzberg, "Equitable vs. Constitutional Mootness: The Eleventh Circuit Provides a Primer," eSquire Global Crossings (April 3, 2017).

12 *Clear Channel*, 391 B.R. at 33-34.

continued on page 56

from page 13

changes were numerous and complex, which called into question whether the appeal was equitably moot. Title to the debtor's property was transferred to the buyer, and the trustee had relinquished control over the development of the debtor's property to the buyer. The buyer assumed certain executory contracts and unexpired leases, and had also executed and recorded a number of documents necessary to effectuate the sale. All of these required significant expenditures by the buyer.[13]

Nevertheless, the BAP held in *Clear Channel* that the appeal was not equitably moot. The BAP reasoned that the buyer was the only party impacted by the appeal, not any third parties, and the buyer "was aware of the risks of going forward with the sale."[14] *One has to wonder: Isn't the impact on the buyer (assuming that it is a good-faith purchaser) precisely what § 363(m) is intended to protect against?* Respectfully, the BAP's faulty analysis on the equitable mootness was only outdone by its analysis on the construction of an effective remedy.

The foregoing notwithstanding, while equitable mootness is still available as an argument for dismissal of the appeal of a § 363 order, the vagaries of courts in interpreting what is "equitable" and what an effective remedy might look like is not particularly comforting to the buyer involved in the process.

Realistically, What Is the "Effective Remedy"?

Realistically, what then are the effective remedy options for the reversed § 363 order? Again assuming a solid evidentiary record supporting a good-faith purchaser/assignee finding, we know that the sale/assignment is still valid regardless of reversal or modification of the § 363 order. Title to the property in a § 363 sale has passed or parties have acted on an assigned executory contract, and the sale/assignment cannot, by statute, be undone. So, then what? Unfortunately, any effective remedy may well be at the expense of who was to get what from the § 363 order proceeds, but not the buyer. For example, rather than proceeds going into trusts for unsecured creditors or used to pay off senior secured debt, can those proceeds be diverted for other uses?[15] While that is undoubtedly disappointing for the creditors of the estate, from the buyer's perspective that is simply not its concern.

One cannot delve into this topic without revisiting (with a shudder) the *Clear Channel* case previously discussed, where the BAP held that the debtor could not sell its property to a senior lienholder (under a "credit bid") free and clear of the liens of a junior lienholder on the property. What is of particular interest in *Clear Channel* is that the BAP, after finding neither statutory nor equitable mootness, decided that it could give effective relief by allowing the sale, but completely altering the very terms for which the property was purchased! The BAP's "effective remedy" was to say to the buyer that the BAP had good news and bad news. The good news is that the buyer still had title to the property. The bad news is that because of a statutory defect, the title was not free and clear of junior liens, but rather subject to the junior liens. The BAP's effective remedy was therefore rewriting the entire contract between the buyer and the trustee and depriving the buyer of the benefit of its bargain. The bankruptcy world reacted strongly to this commercially absurd attempt at an effective remedy, and I am aware of no cases since *Clear Channel* that have followed it.[16]

Unfortunately, the case settled after the BAP opinion, so no further clarification or opinion came down from the BAP on this decision (which is definitely an outlier). The foregoing notwithstanding, I am hard-pressed to think of anyone who would consider denying the buyer the essential benefit of its bargain (title free and clear of liens) as being an effective remedy in any commercial sense.

MOAC Will Undoubtedly Tilt the Playing Field to the Detriment of Debtors

The bigger issue is that an already difficult dynamic will be further challenged, and buyers will be very wary of *MOAC*'s implications. Beyond the prospect of "chilling bidding,"[17] prudent buyers would be well advised to negotiate as part of any sale transaction a material reserve to pay the buyer/assignee's legal fees and expenses if they get dragged into an appellate process that is not quickly dismissed on equitable-mootness grounds.[18] This will have an adverse economic impact on the creditors awaiting payments, but at the end of the day, what choice is there really if the sale is indeed an economic necessity to start with?

Moreover, objectors will rattle their proverbial sabers over their now-sacrosanct and Supreme Court-protected statutory appellate rights under *MOAC*. While this is to be expected, equitable mootness is still available, and the protections for the buyer under § 363(m) still exist. Attempts to obtain stays pending appeals are suspected to be taken on

13 *Id.* at 33-34.

14 *Id.* at 34.

15 *See* Loeb & Brosius, *supra* n.3, discussing *In re Energy Future Holdings Corp.*, 949 F.3d 806 (3d Cir. 2020), and the high standards to overturn a sale in light of § 363(m) protections; *In re ICL Holding Co. Inc.*, 802 F.3d 547 (3d Cir. 2015) (again discussing altering who got paid what from the sales proceeds, not invalidating sale itself). Unlike the Second Circuit in *MOAC*, the Third Circuit did not view § 363(m) as jurisdictional, so these issues percolated through the appellate system.

16 *See* Thomas J. Salerno, *Acquisitions from Financially Distressed Companies: An Overview* (ABI 2020), at 24-25 and n.26 (listing numerous cases that have declined to follow *Clear Channel*); Geoffrey S. Goodman, "*Clear Channel* Affects Debtor's Ability to Sell Assets Under § 363," *Legal New Alert* (Nov. 18, 2008). *Clear Channel* has often been referred to as the "twist cap" of its day. *See In re Twist Cap Inc.*, 1 B.R. 284 (Bankr. M.D. Fla. 1979) (shock waves were sent through commercial markets when bankruptcy court held that automatic stay prevented call on letter of credit by nondebtor beneficiary). This case was also widely criticized and ignored after it was rendered. *Editor's Note:* Purchase a copy of *Acquisitions from Financially Distressed Companies: An Overview* at store.abi.org.

17 "Chilling bidding," as in discouraging stalking-horse bidders, is used to justify all sorts of interesting tactics in the sale process, including approval of large break-up fees and other bidder protections (without which, it is argued, no one will agree to be a stalking-horse bidder). The real impact of failing to approve break-up fees is often overstated, and most bidders (perhaps grudgingly) still proceed. For example, in 2009, despite disapproval of a $15 million break-up fee sought by the stalking-horse bidder in the *Phoenix Coyotes* sale, the stalking-horse bidder remained in the process.

18 Frankly, this issue already had existed in those jurisdictions, such as the Third and Ninth Circuits, which pre-*MOAC* did not view § 363(m) as jurisdictional in nature.

renewed urgency, with demands for substantial bonds to the extent any stay is issued. No doubt there will be threatened hold-up value by objectors, but just how material that is in the course of actual practice remains to be seen.

Conclusion

Will the new risks wrought by *MOAC* sound a death knell for § 363 sales? I tend to doubt it. While it will tilt the playing field a bit, as a practical matter, other than some delay (and decisions such as *Clear Channel* that are outliers), the effective remedy to be imposed in any appeal will likely not be against the buyer, and will not destroy the distressed asset sale marketplace. Deals will still be available, and buyers' self-interest will win out. To paraphrase Albert Einstein, "in adversity there is opportunity!"[19] Is *MOAC* the cosmic explosion that kills § 363 sales as we know them, or more of a sputtering firecracker? I suspect it is the latter. abi

19 The actual quote was, "in the middle of every difficulty lies opportunity."