Bankruptcy Injunctions and Complex Litigation: A Critical Reappraisal of Non-Debtor Releases in Chapter 11 Reorganizations

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BANKRUPTCY INJUNCTIONS AND COMPLEX LITIGATION: A CRITICAL REAPPRAISAL OF NON-DEBTOR RELEASES IN CHAPTER 11 REORGANIZATIONS

Ralph Brubaker*

Bankruptcy courts are increasingly faced with resolving complex litigation in the context of Chapter 11 business reorganizations. Meanwhile, the judicial practice of discharging creditor actions against non-debtors in these proceedings is growing. In this article, Professor Brubaker asserts that such non-debtor releases are a wholly inappropriate use of bankruptcy courts' injunctive powers.

Professor Brubaker begins with an overview of the nature and types of bankruptcy injunctions. He then carefully explores the various bankruptcy policy rationales that have been offered to justify non-debtor releases and critiques each in turn. Next, he searches for a legitimate jurisdictional foundation for non-debtor releases and finds none. Professor Brubaker concludes that the use of non-debtor releases in bankruptcy lacks theoretical merit and is outside the scope of judicial authority without express legislative approval.

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I. Introduction

The reorganization provisions of Chapter 11 of the Bankruptcy Code enable a business debtor to achieve a complex and comprehensive financial restructuring through the workings of a plan of reorganization that provides for distribution on, and discharge of, all of the debtor's prebankruptcy debts. A rather disturbing development, though, is a growing judicial acceptance of reorganization plan provisions that not only provide for discharge of the obligations of the Chapter 11 debtor, but that also release non-debtor third parties from liability to the debtor's creditors—often supplemented by injunctions that permanently restrain creditors from pursuing the released non-debtors. This practice raises some very basic questions concerning the proper reach of the bankruptcy reorganization process. Should a debtor's plan of reorganization release the debtor's officers, directors, and employees from any potential personal liability they may have to corporate creditors and shareholders for their acts and omissions on behalf of the corporate debtor (e.g., personal liability under the federal securities laws)? Should the debtor's plan release the debtor's bank group from liability for misrepresentation or fraud alleged by other creditors?

Long considered improper, such provisions nonetheless have regularly appeared in reorganization plans, because inattentive creditors who fail to object to confirmation of the plan will find themselves bound to non-debtor releases by the preclusion principles of res judicata. More recently, though, non-debtor releases have become more than a trap for the unwary; several courts have opined that, in certain circumstances, non-debtor releases are a perfectly legitimate exercise of a bankruptcy court's equitable powers. Many of these releases are approved in the context of an insurer's settlement of a coverage dispute with the debtor's estate, such as the injunctions approved by the Second Circuit in the historic reorganization of Johns-Manville Corp. (Manville), which dealt with the massive product liability resulting from Manville's manufacture of asbestos products. In these insurance coverage settlements, the non-debtor release and injunction protects the insurer from further insurance claims by the debtor's tort claimants. In many ways the insurance injunctions are sui generis, but


two other circuit opinions seized upon the Manville injunctions to pave the way for exceedingly broad non-debtor releases and injunctions.3

The Second Circuit approved non-debtor releases in the bankruptcy of former securities giant Drexel Burnham Lambert (Drexel).4 Drexel’s bankruptcy was precipitated by massive securities fraud liability, incurred through the illegal activities of Michael Milken and others in the junk bond market.5 Yet, Drexel’s plan of reorganization extinguished personal liability for such misdeeds for approximately 200 former Drexel employees, including the junk-bond kingpin him-

3. This article will not discuss such insurance injunctions. Insurance injunctions involve property of the estate issues that are not implicated by broader non-debtor releases. See infra note 51; see also Charles A. Beckham, Jr., It’s All an Unsecured Claim to Me: The Tortious Interference of Bankruptcy Law with Liability Insurance Proceeds, 22 Tex. Tech. L. Rev. 779 (1991); Barry L. Zaretzky, Insurance Proceeds in Bankruptcy, 55 Brooklyn L. Rev. 373 (1989); George Ong, Note, Directors and Officers Insurance Proceeds in Bankruptcy: The Impact on an Estate and Its Claimants, 13 Bankr. Dev. J. 235 (1996). Likewise, partners’ liability to a debtor-partner for partnership deficiencies make non-debtor partner releases and injunctions, which protect individual partners from partnership creditors, unique and beyond the scope of this article. See generally National Bankr. Conference, Reforming the Bankruptcy Code 179-80 (1994); Paul R. Glassman, Third-Party Injunctions in Partnership Bankruptcy Cases, 49 Bus. Law. 1081 (1994); Morris W. Macey & Frank R. Kennedy, Partnership Bankruptcy and Reorganization: Proposals for Reform, 50 Bus. Law. 879 (1995). Enjoining creditors from asserting successor liability claims against purchasers of a debtor’s assets also involves property concerns distinct from those addressed in this article. In addition, the non-debtor obligations addressed by successor liability injunctions are distinctive in that they do not predate the bankruptcy proceedings. Rather, they are non-debtor obligations that otherwise would be generated by a bankruptcy sale of the debtor’s assets. See generally William T. Bodoh & Michelle M. Morgan, Inequality Among Creditors: The Unconstitutional Use of Successor Liability to Create a New Class of Priority Claimants, 4 Am. Bankr. Inst. L. Rev. 325 (1996); David Gray Carlson, Successor Liability in Bankruptcy: Some Unifying Themes of Intertemporal Creditor Priorities Created by Running Covenants, Products Liability, and Toxic-Waste Cleanup, Law & Contemp. Probs., Spring 1987, at 119; Michael H. Reed, Successor Liability and Bankruptcy Sales, 51 Bus. Law. 653 (1996); J. Maxwell Tucker, The Clash of Successor Liability Principles, Reorganization Law, and the Just Demand That Relief Be Afforded Unknown and Unknowable Claimants, 12 Bankr. Dev. J. 1 (1995). Despite the different cases, many cases, nonetheless, indiscriminately and erroneously rely upon non-debtor releases in these special cases as support for the broader non-debtor releases criticized in this article. Compare In re Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 934-35 (Bankr. W.D. Mo. 1994) (citing hodgepodge of cases involving permanent, temporary, consensual, and nonconsensual non-debtor releases and injunctions in insurance, partnership, res judicata, and other contexts as authority for uniform five-factor balancing test for approval of nonconsensual, permanent non-debtor releases), with Homsy v. Floyd (In re Vitek, Inc.), 51 F.3d 530, 538 n.39 (5th Cir. 1995) (cautioning against reliance upon court’s insurance injunction opinion in other non-debtor liability contexts).


5. See Mary Zey, Banking on Fraud: Drexel, Junk Bonds, and Buyouts 3-10, 42-44 (1993); see also Drexel Burnham Lambert Group, Inc. v. Claimants Identified on Schedule 1 (In re Drexel Burnham Lambert Group, Inc.), 995 F.2d 1138, 1141-42 (2d Cir. 1993); Drexel, 960 F.2d at 287-88, aff’d 130 B.R. at 914.
self, Milken.\textsuperscript{6} Through these non-debtor releases, Milken and others shielded tremendous amounts of wealth from creditor claims.\textsuperscript{7}

In the mass tort bankruptcy of A.H. Robins Company (Robins), manufacturer of the infamous Dalkon Shield contraceptive device, the non-debtor releases affirmed by the Fourth Circuit precluded Dalkon Shield claimants from suing anyone for personal injuries caused by the Dalkon Shield.\textsuperscript{8} Beneficiaries of the non-debtor releases included Robins' insurer and alleged joint tortfeasor, Aetna, which was the subject of a class action suit by Dalkon Shield claimants.\textsuperscript{9} The personal injury claimants asserted that both Aetna and Robins affirmatively concealed from the public the dangers of the Dalkon Shield.\textsuperscript{10} Members of the Robins family were also defendants in the class action and beneficiaries of the reorganization plan's non-debtor releases,\textsuperscript{11} as were other present and former officers, directors, employees, and attorneys for Robins. These individuals were alleged to have personally participated in efforts to defraud the public in the marketing of the Dalkon Shield and to have used Robins' attorneys to perpetuate and cover up the fraud.\textsuperscript{12} The Robins plan of reorganization discharged all of these individuals from any personal liability, and the Robins non-debtor releases even went so far as to preclude injured women from suing their doctors for claims of medical malpractice.\textsuperscript{13} As in the \textit{Drexel} case, Robins insiders profited handsomely from their liability releases.\textsuperscript{14}

\textsuperscript{6} See \textit{Drexel}, 138 B.R. at 753 (confirming plan of reorganization with non-debtor releases protecting "Identified Settling Parties"); \textit{Drexel}, 995 F.2d at 1143 (affirming approval of settlement designating former employees as "Identified Settling Parties").

\textsuperscript{7} See infra note 139 and accompanying text.

\textsuperscript{8} See \textit{In re A.H. Robins Co.}, 131 B.R. 292, 294-96 (E.D. Va. 1991) (quoting plan of reorganization's non-debtor release and injunction provisions), rev'd and remanded sub nom. Dalkon Shield Claimants Trust v. Reiser (\textit{In re A.H. Robins Co.}), 972 F.2d 77 (4th Cir. 1992); \textit{In re A.H. Robins Co.}, 88 B.R. 742, 751-55 (E.D. Va. 1988) (confirming plan of reorganization), aff'd sub nom. Menard-Sanford v. Mabey (\textit{In re A.H. Robins Co.}), 880 F.2d 694, 700-02 (4th Cir. 1989). The only exception to this broad release of all non-debtor Dalkon Shield claims was for those Dalkon Shield claimants who did not timely file claims in Robins' reorganization case. Their claims against Robins were subordinated to prior satisfaction of timely filed Dalkon Shield claims, but they retained their right to sue Robins' insurer, Aetna, as a joint tortfeasor and to sue medical providers for malpractice—to recover compensatory damages only. See \textit{Robins}, 880 F.2d at 700-01 & n.5; Dalkon Shield Claimants' Comm. v. Aetna Cas. & Sur. Co. (\textit{In re A.H. Robins Co.}), 85 B.R. 373, 378 (E.D. Va. 1988), aff'd, 880 F.2d 709, 717 (4th Cir. 1989).


\textsuperscript{11} See \textit{Robins}, 85 B.R. at 375.

\textsuperscript{12} See \textit{Sobol}, supra note 10, at 220.


\textsuperscript{14} See infra note 139 and accompanying text.
Rather than provoking a backlash, the Robins and Drexel cases actually turned the tide in the direction of a much more liberal attitude toward non-debtor release provisions.\textsuperscript{15} One court’s attempt at a discretionary, multifactored balancing test bespeaks the newfound legitimacy of non-debtor releases.\textsuperscript{16} Also, in the 1994 amendments to the Bankruptcy Code, Congress specifically authorized non-debtor release and injunction provisions\textsuperscript{17} protecting, inter alia, a debtor’s management personnel and third-party financing institutions\textsuperscript{18} from

\textsuperscript{15} In the author’s experience, the practice of approving non-debtor releases is more widespread than the number of published judicial opinions would suggest. One explanation for this phenomenon is the relative scarcity of appellate review, as appellate challenges to plan of reorganization provisions are easily mooted by consummation of the plan. \textit{See, e.g.}, Bennett v. Veale, Nos. 93-3016, 93-4180, 1995 WL 385147 (6th Cir. June 25, 1995) (mem. at 60 F.3d 828) (holding that the appellate challenge to release provisions of plan of reorganization was moot); \textit{In re Specialty Equip. Cos.}, 3 F.3d 1043, 1049 (7th Cir. 1993) (same); \textit{In re AOV Indus., Inc.}, 792 F.2d 1140, 1147, 1149 (D.C. Cir.) (same), \textit{vacated in part on other grounds}, 797 F.2d 1004 (D.C. Cir. 1986).


\begin{enumerate}
  \item There is an identity of interest between the debtor and the third party, usually an indemnity relationship, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete assets of the estate.
  \item The non-debtor has contributed substantial assets to the reorganization.
  \item The injunction is essential to reorganization. Without the [sic] it, there is little likelihood of success.
  \item A substantial majority of the creditors agree to such injunction, specifically, the impacted class, or classes, has “overwhelmingly” voted to accept the proposed plan treatment.
  \item The plan provides a mechanism for the payment of all, or substantially all, of the claims of the class or classes affected by the injunction.
\end{enumerate}

\textit{Master Mortgage}, 168 B.R. at 934-35 (footnotes omitted). Each of these factors is considered \textit{infra} Part III.

\textsuperscript{17} Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 111(a), 108 Stat. 4106, 4113-17 (codified at 11 U.S.C. § 524(g) (1994)). In enacting § 524(g), Congress also expressly enacted a “rule of construction” that nothing in that section “shall be construed to modify, impair, or supersede any other authority the court has to issue injunctions in connection with an order confirming a plan of reorganization.” \textit{Id.} § 111(b), 108 Stat. at 4117; \textit{see also} 140 CONG. REC. H10,766 (daily ed. Oct. 4, 1994) (statement of Rep. Brooks, sponsor) (“[R]ule of construction [is] to make clear that the special rule being devised for the asbestos claim trust/injunction mechanism is not intended to alter any authority bankruptcy courts may already have to issue injunctions in connection with a plan or [sic] reorganization. . . . The Committee expresses no opinion as to how much authority a bankruptcy court may generally have under its traditional equitable powers to issue an enforceable injunction of this kind.”). \textit{But see Resorts Int’l v. Lowenschuss (In re Lowenschuss), 67 F.3d 1394, 1402 n.6 (9th Cir. 1995)} (citing Congress’ enactment of § 524(g) in the asbestos context as reinforcing court’s conclusion that § 524(e) prohibits non-debtor releases and injunctions in all other circumstances); Meltzer, \textit{supra} note 1, at 31-33, 42 (acknowledging rule of construction, but nonetheless, attaching interpretational significance to the enactment of § 524(g)).

\textsuperscript{18} The amendments provide:

Notwithstanding the provisions of section 524(e), such an injunction may bar any action directed against a third party . . . alleged to be directly or indirectly liable for the conduct of, claims against, or demands on the debtor to the extent such alleged liability of such third party arises by reason of—
liability to asbestos personal injury claimants in limited circumstances. This somewhat remarkable shift in the law has been met with very little critical resistance, and in fact, one commentator recently stated that a plan of reorganization "can and should be permitted to release all claims against . . . third parties . . . which are assertable against such third parties because they acted for the debtor or because of their actions or omissions in the course of their relationship with the debtor."20

This article sets forth the long-overdue challenge to non-debtor releases by questioning policy justifications and judicial authority, both of which prove illusory. The issue is a pressing one, as the bankruptcy court is quickly becoming the forum for resolution of many of the largest and most complex mass litigations.21 In addition, the recent congressional Bankruptcy Review Commission, in reexamining the Bankruptcy Code for possible reform, undertook a limited study of the proper role of non-debtor releases and injunctions in complex reorganizations.22


20. Hydee R. Feldstein, Reinterpreting Bankruptcy Code § 524(e): The Validity of Third-Party Releases in a Plan, 22 CAL. BANKR. J. 25, 46 (1994) [hereinafter Feldstein, Third-Party Releases]. Feldstein had previously presented this same conclusion at the 1994 Annual Meeting of the National Conference of Bankruptcy Judges. See Hydee R. Feldstein, Reinterpreting Bankruptcy Code Section 524(e): The Validity of Third Party Releases in a Plan, 1994 NAT'L CONF. BANKR. JUDGES 6-63, at 6-74 & n.1. Citing both Robins and Drexel, Feldstein also states that "[p]rovisions for releasing and enjoining actions against third parties have been an accepted part of large corporate reorganizations for some time." Feldstein, Third-Party Releases, supra, at 38 & n.52.


The relative dearth of critical opposition to non-debtor releases is curious and untoward. The statutory provision that courts and commentators have relied upon, almost reflexively, as supposedly prohibiting non-debtor releases, has proved to be a red herring and actually has stifled a more principled opposition. An analysis of non-debtor releases must explore a more intricate web of bankruptcy policies and jurisdictional limitations. Non-debtor releases provide a cogently illustrative case study in the contemporary theoretical debate regarding the proper role of reorganization policy in formulating bankruptcy law. This policy study counsels against any judicial discretion to approve non-debtor releases. Quite apart from these policy considerations is the question of whether bankruptcy courts presently possess any authority to approve non-debtor releases. Careful historical analysis reveals that non-debtor releases overstep the bounds of limited bankruptcy jurisdiction; bankruptcy judges have no jurisdictional authority to approve non-debtor releases, in the absence of express congressional authorization.

As background for this article’s jurisdictional, statutory, and policy analysis of non-debtor releases, part II describes the nature of bankruptcy injunctions and the differences between temporary non-debtor stays and permanent non-debtor releases. Part II also outlines the more limited statutory debate concerning non-debtor releases and its deficiencies. Part III then examines the various bankruptcy policies advanced in support of non-debtor releases. Non-debtor releases use a Chapter 11 reorganization, designed to restructure creditor claims against a bankruptcy debtor, to discharge creditor claims against others, and in the process, pervert both nonbankruptcy and bankruptcy conceptions regarding appropriate treatment of such claims. The generic desire to promote settlement tells us little about non-debtor releases, other than highlighting the fact that they permit an extraordinary nonconsensual settlement, unheard of in any other context. Unique bankruptcy policies provide no separate justification for such an exceptional “settlement.” Non-debtor releases violate fundamental creditor equality norms embodied in the Bankruptcy Code and dismantle a series of procedural and substantive protections designed to safeguard the value of creditor distributions. As a result, the released non-debtor, as well as the debtor’s other creditors and shareholders, are allowed to walk away with value rightfully belonging to creditors whose viable non-debtor rights are extinguished.

23. 11 U.S.C. § 524(e), discussed infra Part II.B. In any event, this particular statutory provision provides no theoretical counterargument to congressional action, such as the 1994 amendments authorizing release of non-debtor asbestos actions. See supra notes 17-19 and accompanying text.

Part III concludes by discussing the determinative and most potent of the bankruptcy policies—the reorganization policy. This policy ultimately fails to substantiate non-debtor releases, because they appear to serve a redistribution end more than one of reorganization. Any reorganization potential that non-debtor releases might possess falls victim to intractable screening difficulties, engendered by the fact that non-debtor releases purchase benefits at no cost to the reorganized debtor. In addition, approval of non-debtor releases in the name of reorganization vests the courts with a delicate policy-making role, inconsistent with their traditional function in reorganization cases.

Part IV moves the inquiry to the jurisdictional foundations for non-debtor releases and injunctions. This exercise of equitable powers is examined against a backdrop of the historical development of bankruptcy courts’ injunctive powers under the Bankruptcy Act of 1898 (the 1898 Act). In that jurisprudence, the Supreme Court developed a critical distinction between jurisdiction to adjudicate and jurisdiction to enjoin. Modern courts have lost sight of this distinction, as evidenced by the confused exchange between the majority and the dissent in the Supreme Court’s recent foray into bankruptcy jurisdiction and non-debtor injunctions. Failure to appreciate the difference between jurisdiction to enjoin and jurisdiction to adjudicate has led the courts to insidiously release non-debtor actions beyond their jurisdiction to adjudicate. Even more startling, though, is the fact that the jurisdictional disarray has caused the courts to completely ignore binding Supreme Court precedent prohibiting a permanent non-debtor injunction. Therefore, part IV concludes that non-debtor releases are not an appropriate use of a bankruptcy court’s injunctive powers, and bankruptcy courts are without authority to approve non-debtor releases, in the absence of express congressional authorization.

II. Bankruptcy Injunctions and the Extant Statutory Debate

Restraint of non-debtor actions by a bankruptcy court is accomplished via non-debtor injunctions of two types: temporary non-debtor stays and permanent non-debtor releases. Both of these non-debtor injunctions issue pursuant to bankruptcy courts’ general equitable powers and as supplements to statutory bankruptcy injejunc-
tions. A temporary non-debtor stay complements the Bankruptcy Code’s automatic stay provisions and is widely accepted as a legitimate exercise of a bankruptcy court’s equitable powers. A permanent non-debtor release, as an adjunct to the Bankruptcy Code’s discharge injunction, however, is much more controversial. The statutory provision courts and commentators cite as prohibiting non-debtor releases, though, simply does not speak to the issue.

A. Statutory Bankruptcy Injunctions

The Bankruptcy Code contains two injunctions imposed by statute in reorganization cases under Chapter 11: the automatic stay and the discharge injunction. Initially, commencement of the bankruptcy case, in and of itself, operates as an automatic stay of all creditor collection actions and proceedings of any nature. The dual purposes of the automatic stay are to (1) halt the creditors’ proverbial “race to the courthouse” in favor of the Bankruptcy Code’s overriding preference for creditor equality, and (2) provide the debtor a temporary “breathing spell” in which the debtor can attempt to reorganize. The vehicle by which the debtor can then emerge from bankruptcy as a reorganized entity is the Chapter 11 plan of reorganization—a very powerful means by which a troubled company can restructure its financial affairs. Through the plan of reorganization, all of the debtor’s prebankruptcy debts are discharged and all ownership interests are terminated. In the place of these old debts and ownership interests, the plan of reorganization provides the debtor an entirely new capital structure.

To take a simplified example, a Chapter 11 plan of reorganization might provide that creditors will receive all of the common stock of the reorganized company. Confirmation of this plan would simultane-

with the debtor as creditors’ non-debtor actions. A creditor’s dual claims against both the debtor and a non-debtor can be graphically represented as follows:

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Temporary restraint of creditors’ non-debtor actions will be referred to herein as a non-debtor stay. A permanent discharge of such a non-debtor claim through plan of reorganization provisions and supplementary injunctions will be referred to as a non-debtor release.

32. The process by which the plan of reorganization divides the value of the reorganized debtor amongst prebankruptcy creditors and shareholders is explored infra Part III.B.
ously extinguish all of the debtor's debts and shareholder interests and transfer ownership of the reorganized company to the former creditors. By virtue of the bankruptcy discharge, the company survives and continues to operate without the burden of its old debts, and the former creditors have now received all of the value of the company through their ownership of the reorganized entity. Creditors whose claims were automatically stayed upon commencement of the Chapter 11 proceedings, thereafter, can pursue their rights against the debtor only by way of a proof of claim against the debtor's bankruptcy estate, filed in the bankruptcy court. Creditors whose claims are allowed by the bankruptcy court will then be entitled to a pro rata distribution of postreorganization common stock, pursuant to the terms of the confirmed plan of reorganization, but nothing more. The bankruptcy discharge effected by confirmation of the plan is implemented by a statutory discharge injunction, prohibiting creditors from asserting any further rights against the reorganized debtor.

B. Supplementary Equitable Injunctions and Section 524(e)

By their terms, both the automatic stay and the discharge injunction only restrain a creditor's actions against the debtor, the debtor's property, and property of the debtor's bankruptcy estate; they do not reach any action the creditor might take against third parties who may share the debtor's liability to the creditor, such as contractual guarantors or joint tortfeasors. In fact, section 524(e) of the Bankruptcy Code expressly states that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." In addition to these statutory injunctions, though, bankruptcy courts also possess the general injunctive powers of a court of equity by virtue of section 105(a) of the Bankruptcy Code. Congress specifically contemplated that bankruptcy courts would issue section 105 injunctions "to stay actions not covered by the automatic stay," with the courts determining "on a case-by-case basis whether a particular action which may be harming the estate should be stayed." Thus, in a variety of circumstances, the courts have issued section 105 injunctions as a supplement to the auto-

34. The bankruptcy court determines the allowability of any claims to which an objection is posed. See id. § 502(a)-(b). The plan of reorganization specifies how all creditor claims and shareholder interests will be treated. See id. § 1123(a)(2)-(3).
35. See id. § 524(a).
36. See id. §§ 362(a), 524(a).
37. Id. § 524(e).
38. See id. § 105(a), discussed infra notes 281-84 and accompanying text.
matic stay where non-debtor actions threaten to frustrate the objectives of the automatic stay.\footnote{40} For example, when creditors assert liability on the part of the debtor and individual members of the debtor's management, continuing litigation against individual officers, directors, and employees may unduly divert such individuals' time and energies away from the debtor's reorganization efforts. Therefore, courts often enjoin such non-debtor litigation in order to fully effectuate the temporary "breathing spell" from creditor actions that the automatic stay seeks to afford the debtor.\footnote{41} The "breathing spell" rationale, though, expires upon confirmation of a plan of reorganization, and like the automatic stay itself,\footnote{42} such supplementary non-debtor stays do not extend beyond plan confirmation.

The propriety of such temporary non-debtor stays in certain circumstances has gained widespread acceptance in the courts and, indeed, was implicitly sanctioned by the Supreme Court recently.\footnote{43} A much more difficult question, however, is posed when the parties ask the bankruptcy court, as a supplement to the debtor's discharge injunction, to enter a permanent non-debtor injunction or approve non-debtor release provisions in the plan of reorganization. The initial and still-dominant reaction to such requests is that such a non-debtor release is prohibited by section 524(e), which expressly restricts the effects of a debtor's discharge to the debtor's personal liability only and preserves creditors' non-debtor rights.\footnote{44} According to this majority

approach, plan provisions releasing a non-debtor from liability to creditors are appropriate only with respect to those creditors who voluntarily consent to the non-debtor release. Creditor consent might be induced by an offer of additional consideration provided by the released non-debtor, such as cash distributions, for those creditors affirmatively agreeing to release claims against the non-debtor.45

Although this article contends that a bankruptcy court does, indeed, lack the authority to approve a nonconsensual release of creditors’ non-debtor claims, courts’ and commentators’ reliance upon section 524(e) as a statutory prohibition is misguided and unfortunate. Section 524(e) is necessary, as a matter of mere mechanics, to prevent the debtor’s discharge from automatically discharging co-debtors and guarantors, through the operation of common-law suretyship rules

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that release secondary obligors upon release of the primary obligor. Consistent with this limited purpose, and as several courts have noted, the literal terms of section 524(e) say only that the debtor’s discharge does not, by its own force, affect the liability of others. Nothing in section 524(e) can be read to affirmatively prohibit a bankruptcy court from using its equitable injunctive powers in furtherance of a successful reorganization by the debtor.

Preoccupation with the interpretational debate over section 524(e) has allowed the practice of approving non-debtor releases to take hold, given the absence of any full and meaningful response to the equitable powers argument. The remainder of this article takes the analysis of non-debtor releases beyond the unproductive section 524(e) debate. Part III analyzes the advisability of non-debtor releases as a policy matter and concludes that non-debtor releases are not a legitimate means to promote the policies they purportedly advance. Part IV examines jurisdictional authority to approve non-debtor releases and concludes that, in the absence of express congressional authorization, courts have no authority to approve non-debtor releases.

III. NON-DEBTOR RELEASES AND BANKRUPTCY POLICY

Attempts to rationalize non-debtor releases inevitably become an exercise in advancing general bankruptcy policies that such releases allegedly vindicate. On close scrutiny of these broad policies, however, non-debtor releases actually prove to frustrate and run counter to the carefully crafted reorganization provisions of the Bankruptcy Code, as well as the nonbankruptcy policies embedded in the non-debtor actions extinguished by the releases. The general interest in furthering settlement of complex disputes looms large in decisions approving non-debtor releases. But this general concern justifies no more than existing mechanisms for settlement of multiple non-debtor

46. See, e.g., Restatement (Third) of Suretyship and Guaranty §§ 39-44 & intro. note, at 167 (1996). Section 524(e) has predecessors in every prior bankruptcy statute, including section 16 of the 1898 Act, section 33 of the 1867 Act, section 4 of the 1841 Act, and section 34 of the 1800 Act. See 1A Collier on Bankruptcy ¶ 16.01, at 1522-23 & n.1 (James Wm. Moore & Lawrence P. King eds., 14th ed. 1978) [hereinafter Collier (14th ed. 1978)] (reproducing statutory provisions). The clear purpose of all of these provisions was to preempt efforts by co-obligors to assert the debtor’s discharge as a defense to their own personal liability. See 1A id. ¶¶ 16.02, 16.05; Hill v. Harding, 130 U.S. 699, 703-04 (1889) (construing section 33 of the 1867 Act); Feldstein, Third-Party Releases, supra note 20, at 28-34.

47. See, e.g., Specialty Equip., 3 F.3d at 1047 (“[S]ection 524(e) . . . does not purport to limit or restrain the power of the bankruptcy court to otherwise grant a release to a third party [and] a per se rule disfavoring all releases would be similarly unwarranted, if not a misreading of the statute.”); In re A.H. Robins Co., 880 F.2d 694, 702 (4th Cir. 1989) (“[W]e do not think that section [524(e)] must be literally applied in every case as a prohibition on the power of the bankruptcy courts.”); Republic Supply Co. v. Shoaf, 815 F.2d 1046, 1050 (5th Cir. 1987) (“[T]he statute does not by its specific words preclude the discharge of a guaranty when it has been accepted and confirmed as an integral part of a plan of reorganization.”).
claims, such as class action procedures. Non-debtor releases, though, permit a court to impose a mandatory class settlement of non-debtor actions in circumstances where a mandatory class is impermissible under nonbankruptcy law. Such a mandatory settlement is defensible only if the circumstances surrounding the debtor’s reorganization compel this extraordinary settlement. Bankruptcy considerations, however, do not support this mandatory settlement of non-debtor actions; instead, they condemn it.

The implications of approving non-debtor releases, in the guise of fostering settlement of complex litigation, may well go beyond the bankruptcy reorganization context. Those searching for solutions to the difficulties presented by massive complex disputes often look to the procedures used in the “bankruptcy model.” To the extent that the bankruptcy model includes ill-conceived and inequitable methods for achieving settlement, such as non-debtor releases, there is potential for a pernicious effect on a much broader range of dispute resolution mechanisms. This part III begins by examining the so-called settlement effected through non-debtor releases and then analyzes each of the bankruptcy policies that allegedly warrant this mandatory settlement.

A. Facilitating Compromise and Settlement

Policy justifications for non-debtor releases often begin with the worthy and seemingly benign objective of encouraging negotiated settlement of disputes. Bankruptcy law, however, holds no monopoly on the general policy of encouraging and facilitating settlement over litigation, and the settlement analogy is incomplete and misleading.

The general policy favoring settlement does have force in the context of a bankruptcy reorganization, aimed at a comprehensive restructuring of the debtor’s affairs. This global restructuring can implicate not only determining the rights of creditors and shareholders vis-à-vis the debtor, but also the rights of creditors and shareholders inter se, yielding an intricate triangular or tripartite claims relationship. The facts underlying a creditor’s claim against a debtor’s estate not only may produce a non-debtor action, but this non-debtor action may, in turn, give rise to a contribution or indemnification claim by


the non-debtor against the estate. In addition, the estate itself also may assert claims against the non-debtor. Obviously, a vehicle for comprehensive resolution of all of these interrelated claims will promote a more efficacious administration of the debtor’s estate.

1. Mandatory Settlement Through Non-Debtor Release

A confirmed plan of reorganization, to which all of the debtor’s creditors and shareholders are parties for purposes of res judicata, is a very powerful means by which to accomplish settlement of the triangular claims implicated by non-debtor actions. In fact, the desire to foster such compromises has been the impetus for consensual non-debtor plan releases. In recognition of the force of the settlement policy in complex reorganizations, courts approving compulsory non-debtor releases clothe their decisions with the rhetoric of compromise and settlement, often emphasizing contributions the non-debtor has agreed to make to the debtor’s estate that will enhance the recoveries of all creditors, such as cash payments to or continued services for the debtor.

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50. See infra Part III.C.1 for further discussion of this tripartite claims relationship.

51. These interrelated claims can be graphically represented as follows:

A debtor’s bankruptcy estate is comprised of “all legal or equitable interests of the debtor in property as of commencement of the case.” 11 U.S.C. § 541(a)(1) (1994). This includes any causes of action the debtor might possess. See generally 5 COLLIER (15th ed.), supra note 40, ¶ 541.08. The Bankruptcy Code expressly contemplates compromise of the estate’s causes of action through a plan of reorganization. See 11 U.S.C. § 1123(b)(3)(A) (“[A] plan may provide for the settlement or adjustment of any claim or interest belonging to the debtor or to the estate.”). The non-debtor actions extinguished by objectionable non-debtor releases, however, involve creditors’ direct claims against a non-debtor that are not derivative actions belonging to the debtor’s estate. See Huddleston v. Nelson Bunker Hunt Trust Estate, 117 B.R. 231, 234 (N.D. Tex. 1990) (“[Section] 524(e) is not implicated [because] the Plan does not bar non-derivative claims.”), aff’d mem., 935 F.2d 1290 (5th Cir. 1991); In re Best Prods. Co., 168 B.R. 35, 61 (Bankr. S.D.N.Y. 1994), appeal dismissed, 177 B.R. 791 (S.D.N.Y.), and aff’d, 68 F.3d 26 (2d Cir. 1995); In re General Homes Corp., 134 B.R. 853, 861 (Bankr. S.D. Tex. 1991); In re Texaco Inc., 84 B.R. 893, 900 (Bankr. S.D.N.Y.) (“[Section] 524(e) does not apply to . . . releases . . . and discontinuances of derivative actions [that] relate to claims belonging to the debtor only.”), appeal dismissed, 92 B.R. 38 (S.D.N.Y. 1988).


53. See supra note 45 and accompanying text.

As a matter of general principles, though, the assent of the debtor, statutory committees, and the contributing non-debtor would appear to be insufficient to compromise the non-debtor claims of an objecting creditor. The general policy favoring settlement operates within the confines of the accepted notion that a settlement is a voluntary undertaking that a court cannot impose upon an unwilling litigant. "[P]arties who choose to resolve litigation through settlement may not dispose of the claims of a third party . . . without that party's agreement." Indeed, the only nonbankruptcy context in which a court can impose a settlement upon a nonconsenting claimant is through a court-approved settlement of a mandatory, non-opt-out class action,56 which provides a useful contrast with the so-called bankruptcy settlement effected by a non-debtor release.

2. Mandatory Settlement Through Class Action

Complex litigation, in general, and class actions, in particular, produce a tension between traditional notions of individual rights and judicata case, the bankruptcy court's rationale in approving non-debtor release "that an injunction was necessary to get the parties to provide consideration under the Plan . . . to prevent costly litigation, and to achieve the maximum available pay-out to creditors" and "it intended to achieve complete reprise on all matters related to the various claims and counterclaims"), aff'd on other grounds, 65 F.3d 973, 975-76, 979-80, 985 (1st Cir. 1995) (explaining and excerpting bankruptcy court's confirmation order); SEC v. Drexel Burnham Lambert, Inc. (In re Drexel Burnham Lambert Group, Inc.), 130 B.R. 910, 928 (S.D.N.Y. 1991) (stating that "[p]roviding releases to and injunctions concerning non-Debtors is permissible where a material benefit results to the Debtors' estates and advances consummation of a Plan" and "material benefits here involve [inter alia] incentive to third parties to settle, resulting in increased amounts to be received by all Class members"), aff'd, 960 F.2d 285, 293 (2d Cir. 1992) (stating that the "Settlement Agreement is unquestionably an essential element of Drexel's ultimate reorganization" and "the injunction is a key component of the Settlement Agreement [that] enables the directors and officers to settle these suits without fear that future suits will be filed" and "[w]ithout the injunction, the directors and officers would be less likely to settle"); In re A.H. Robins Co., 88 B.R. 742, 751 (E.D. Va. 1988) ("The releases and injunction . . . are an integral part of the compromises and settlements incorporated in the Plan."); aff'd sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d 694, 700-02 (4th Cir. 1989); In re Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 932-33, 935, 937-38 (Bankr. W.D. Mo. 1994); In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 735-54, 772-73 & n.12 (Bankr. S.D.N.Y. 1992) (stating that "in the absence of the Release and Injunction Provisions . . . Debtors' estates will lose the contributions of the Identified Settling Parties, a substantial source of funds that may yield hundreds of millions of dollars to be used in reorganization under the Plan"); "the Release and Injunction Provisions . . . will be instrumental in bringing an end to years of costly litigation over Drexel's activities"; "time value of money, and the emotional and personal costs of litigation, clearly evinces it is time to end it once and for all"; and "injunction and release provisions preserve our judicial and social fabric"); see also Feldstein, Third-Party Releases, supra note 20, at 26 ("[R]elease of third parties from potential liability . . . is frequently necessary as part of a compromise."). In the Robins case, the comprehensive settlement analogy was euphemistically dubbed "global peace." See In re A.H. Robins Co., 131 B.R. 292, 293, 298 (E.D. Va. 1991) (interpreting scope of non-debtor releases), rev'd and remanded on other grounds sub nom. Dalkon Shield Claimants Trust v. Reiser (In re A.H. Robins Co.), 972 F.2d 77 (4th Cir. 1992).

55. Local No. 93, Int'l Ass'n of Firefighters v. City of Cleveland, 478 U.S. 501, 529 (1986) ("A court's approval of a consent decree between some of the parties therefore cannot dispose of the valid claims of nonconsenting intervenors; if properly raised, these claims remain and may be litigated by the intervenor.").

individual choice, on the one hand, and the desire for efficient resolution of complex disputes, on the other. Class action doctrine, therefore, tempers aggregation and consolidation impulses with various devices designed to assure that class procedures protect individual claimants’ interests, including their interest in individual control of their claims. The total absence of any similar protections as a prerequisite to a bankruptcy court’s approval of non-debtor releases suggests that non-debtor releases are not a legitimate means to foster equitable settlements.

Class actions under Rule 23 of the Federal Rules of Civil Procedure authorize a representative to litigate the claims of others, but only upon a showing that the representative will “fairly and adequately protect the interests of the class.” In fact, an adequate representative is essential to protect the due process rights of individual claimants, and most of the conditions for maintaining a class action are designed to assure adequate representation. In bankruptcy, though, no such representative speaks for the interests of any properly constructed “class” of creditors whose non-debtor claims are extinguished through non-debtor releases. A Chapter 11 creditors’ committee, which represents a constituency composed of a debtor’s general unsecured creditor body as a whole (including those without viable non-debtor rights), is appointed for a very different purpose, in a very different process that contemplates no such litigation representative role for the committee.


60. Implicit in adequate representation of a class is the notion that those being represented possess similar claims constituting a cohesive “class” and the representative is a member of this class. See Hansberry v. Lee, 311 U.S. at 40-46; 3B James Wm. Moore, Moore’s Federal Practice ¶ 23.04[1], at 23-98, 23-104 to -105 (2d ed. 1996); 7A Wright et al., supra note 57, §§ 1760, at 120-23, 1761, at 137. Additional assurances of adequate representation are the requirement that there must be “questions of law or fact common to the class” and that the class representative possess claims “typical of the claims . . . of the class.” Fed. R. Civ. P. 23(a)(2)-(3); see 3B Moore, supra, ¶ 23.06-2, at 23-177 to -178; 1 Newburg, supra note 21, § 1.13, at 1-36 to -37; 7A Wright et al., supra note 57, §§ 1764, at 232-33, 1767, at 316-31, 1769, at 373-74. In addition, class action litigation is only available where necessary, because “the class is so numerous that joinder of all members is impracticable.” Fed. R. Civ. P. 23(a)(1).

61. See generally Daniel J. Bussel, Coalition-Building Through Bankruptcy Creditors’ Committees, 43 UCLA L. Rev. 1547 (1996). As Professor Bussel insightfully demonstrates, the principal purpose of a creditors’ committee is, by reflecting the many differing interests among the creditor body and through deliberation and compromise, “to facilitate the formulation and confirmation of a consensual plan of reorganization that complies with the provisions of Chapter 11.” Id. at 1551. As discussed infra Part III.B, the separate and distinct Chapter 11 classification process, by which a debtor’s plan of reorganization is confirmed, has not provided adequate representation or protection for creditors’ released non-debtor claims. A § 524(g) injunction, which can include the release of non-debtor asbestos claims, is enforceable only if “as part of the
In class actions, an adequate class representative can, indeed, compromise class members' claims through a court-approved settlement. The guiding principle for judicial approval of such a class settlement is that the amount offered in settlement must be fair and reasonable in relation to the strength of the class' claims. The judicially approved "settlement" effected by non-debtor releases in bankruptcy, by contrast, need not attempt to assure that creditors receive reasonable compensation for their released non-debtor claims. Purported settlement-like contributions by released non-debtors need not be contributions to those creditors whose non-debtor claims are released; contributions are to the debtor for the stated purpose of furthering success of the debtor's reorganization efforts. These contributions, therefore, can be for the benefit of all of the debtor's creditors and shareholders, regardless of whether they are releasing valuable non-debtor rights. Likewise, the adequacy of released non-debtors' contributions need not be judged in terms of the relative strength of the non-debtor actions being released. In fact, a non-debtor release can be approved with absolutely no principled scrutiny of the nature, extent, and potential value of the released non-debtor claims. A non-debtor's contribution evidently warrants a release of creditors' non-debtor claims if the contribution provides a "material

proceedings leading to issuance of such injunction, the court appoints a legal representative for the purpose of protecting the rights of persons that might subsequently assert demands of such kind [against the debtor or a released third party]." 11 U.S.C. § 524(g)(4)(B)(i)(IV)(bb).

62. Rule 23(e) provides that a "class action shall not be . . . compromised without the approval of the court." Fed. R. Civ. P. 23(e). Court approval of the settlement, then, binds all class members, even those affirmatively objecting to the settlement. See 7B Wright et al., supra note 57, § 1797, at 359-62.

63. See 3B Moore, supra note 60, ¶ 23.80[4], at 23-488 to -490 ("One of the most significant considerations in judging the reasonableness of a settlement is the strength of the case for the plaintiffs on the merits balanced against the amount offered in the settlement." (footnote omitted)).

64. See infra notes 226-27 and accompanying text (discussing standard for approval of non-debtor releases).

65. Cf. In re B.W. Alpha, Inc., 89 B.R. 592, 596 (Bankr. N.D. Tex.) (noting that "any funds [guarantor] contributed are to be used to pay unsecured creditors and, thus, cannot be said to provide consideration to the Bank" for nonconsensual release of guaranty), aff'd, 100 B.R. 831 (N.D. Tex. 1988). But cf. SEC v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Group, Inc.), 960 F.2d 285, 288-89, 291 (2d Cir. 1992) (court overruled objection to non-debtor release complaining that plan would not permit objector to share in contributions of released parties, yet enjoined objector from suing contributing non-debtors).

66. See, e.g., LTV Corp. v. Actea Cas. & Sur. Co. (In re Chataugay Corp.), 167 B.R. 776, 781, 780-82 (S.D.N.Y. 1994) (noting that the bankruptcy court below, in approving non-debtor release over creditors' objection, had stated that creditors' non-debtor suit "is not before me and I am not prepared to pass on the merits of it." yet court remanded for determination whether non-debtor release was nonetheless permissible because it was "essential" to the debtor's reorganization).
benefit" or is a "substantial contribution" to the debtor’s reorganization.

Most importantly, the so-called settlement effected by a non-debtor release is not a consensual endeavor; it is imposed by judicial fiat. The most egregious inequities produced by non-debtor releases could be cured merely by replicating class action standards for certification and settlement of a class action, and by segregating non-debtors’ settlement contributions for distribution only to those creditors who are members of the settled non-debtor class action. Even these measures, though, would not remove the mandatory nature of any settlement effected via non-debtor release provisions.

Even an adequate class representative generally cannot dispose of the damage claims of an individual class member who chooses to “opt out” of the class action and maintain an individual action.

67. See In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 753 (Bankr. S.D.N.Y. 1992) (noting that the district court order designating Michael Milken and other former Drexel employees as beneficiaries of non-debtor releases was premised on finding that released non-debtors will “provide a material benefit to the Debtors’ estates and Consummation of the Plan”); see also Drexel Burnham Lambert Group, Inc. v. Claimants Identified on Schedule 1 (In re Drexel Burnham Lambert Group, Inc.), 995 F.2d 1138, 1144 (2d Cir. 1993) (affirming district court order designating beneficiaries of Drexel non-debtor releases, based on district court finding that it was “in the best interests of the [Drexel] Debtors’ estates, creditors, and shareholders,” considering “the relative benefits to be received by the Debtors’ estates and their creditors”).

68. See In re Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994) (collecting cases and identifying factors relevant to approval of non-debtor release, including whether “non-debtor has contributed substantial assets to the reorganization”).

69. Section 524(g) injunctions, which can include release of non-debtor asbestos claims, can be approved only if the court finds that the injunction “is fair and equitable with respect to the persons that might subsequently assert such demands [against the debtor or a released third party], in light of the benefits provided, or to be provided, to such [reorganization] trust on behalf of such debtor or debtors or such [released] third party.” 11 U.S.C. § 524(g)(4)(B)(ii) (1994). Given past practice with respect to non-debtor releases and the lack of any requirement for subclassification between those asbestos claims against the debtor and those against released non-debtors, see id. § 524(g)(2)(B)(ii)(IV)(bb), it seems doubtful that this provision will be interpreted to assure that individual creditors will receive fair compensation for the value of their released non-debtor asbestos claims.

70. In a class action certified pursuant to Rule 23(b)(3), based on a finding that “questions of law or fact common to the members of the class predominate over any questions affecting only individual members,” each member has an absolute right to opt out of the class. Fed. R. Civ. P. 23(b)(3); see Fed. R. Civ. P. 23(c)(2)(A); 7B Wright et al., supra note 57, § 1787, at 209-11. There is no opt-out right in so-called mandatory classes under Rule 23(b)(1) and (b)(2). See 3B Moore, supra note 60, § 23.60, at 23-439 to -440. Rule 23(b)(2), however, on its face is applicable only to actions seeking “appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole.” Fed. R. Civ. P. 23(b)(2). Likewise, Rule 23(b)(1)(A) actions, necessitated by a risk that individual actions would create a risk of inconsistent results establishing incompatible standards of conduct, do not encompass actions merely seeking money damages. See 3B Moore, supra note 60, § 23.35[1], at 23-242 to -244. Rule 23(b)(1)(B) provides for a mandatorious class action where there is a risk that individual actions “would as a practical matter be dispositive of the interests of other members not parties to the adjudications or substantially impair or impede their ability to protect their interests.” Fed. R. Civ. P. 23(b)(1)(B). A mandatory Rule 23(b)(1)(B) class is also generally unavailable in an action seeking money damages, and therefore, money damages class actions ordinarily can only be maintained as a common-question action, with an opt-out right. See Ticor Title Ins. Co. v. Brown, 511 U.S. 117, 121 (1994) (noting “substantial possibility” that “in actions seeking mone-
There is authority for an extraordinary mandatory settlement of a properly maintained class action, but only in narrowly prescribed circumstances that non-debtor releases do not replicate. With respect to the kinds of money damage claims discharged via non-debtor releases, a mandatory class action is available only if the defendant is considered a “limited fund” because “the total of the class members’ individual claims may exceed a defendant’s resources.” 71 In such circumstances, the class action is mandatory in order to avoid the risk that the first plaintiffs to judgment will recover in full, to the detriment of other class members. 72 In the absence of a limited fund, though, class members retain the right to opt out of a damages class action, and indeed, such an opt-out right may be required to afford claimants constitutional due process. 73

The fact that the Chapter 11 debtor’s resources may constitute a limited fund from which to satisfy creditors’ claims does not justify limited-fund treatment of creditors’ claims against non-debtors, whose

71. AMERICAN LAW INST., supra note 48, ch. 3 intro. note, at 28-29. The courts have required clear proof of a limited fund, though, before certifying such a mandatory non-opt-out class. See id. at 29; 3B MOORE, supra note 60, ¶ 23.35[2], at 23-257; 7A WRIGHT ET AL., supra note 57, § 1774, at 443.

72. See Transrud, supra note 57, at 794-95.

73. See Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 811-12 (1985). Claimants’ interest in individual control of their actions is strongest in these common-question class actions, and indeed, this interest is explicitly enumerated as a factor for a court to consider before certifying a common-question class. See FED. R. CIV. P. 23(b)(3)(A). Because common-question classes tend to be less cohesive, the opt-out right ameliorates concerns about inadequate representation of class members. Cf. Shutts, 472 U.S. at 812-14 (approving opt-out procedure as indicating consent to jurisdiction sufficient to satisfy due process); 7A WRIGHT ET AL., supra note 57, § 1777, at 518 (“[S]pecial caution must be exercised in [common-question] class actions of this type because of the loose affiliation among the class members, which is thought to magnify the risks inherent in any representative action.”); YEAZELL, supra note 57, at 175-76 (discussing alternative theoretical justifications for representative litigation as based on either commonality of interest or consent). Whether due process requires an opt-out right in all class actions, including Rule 23(b)(1)/(B) limited fund actions, remains an open question. See TICOR TITLE INS., 511 U.S. at 124-25 (O’Connor, J., dissenting); 7B WRIGHT ET AL., supra note 57, § 1789, at 255-56 (2d ed. 1986 & Supp. 1997); 1 NEWBURG, supra note 21, §§ 1.18-1.19, 1.21-1.22; ARTHUR R. MILLER & DAVID CRUMP, JURISDICTION AND CHOICE OF LAW IN MULTISTATE CLASS ACTIONS AFTER PHILLIPS PETROLEUM CO. V. SHUTTS, 96 YALE L.J. 1, 38-57 (1986). Shutts also can be read narrowly, to require an opt-out right only with respect to class members over whom the court would not otherwise have personal jurisdiction. See 7B WRIGHT ET AL., supra note 57, § 1789, at 255.
resources may not constitute a limited fund.\textsuperscript{74} The use of non-debtor releases in bankruptcy, in effect, imposes a non-opt-out settlement of creditors’ non-debtor rights, without regard to whether such a mandatory settlement is necessitated by limited fund principles, and without any other general indicia of an appropriate settlement. Unless non-debtor releases and injunctions are to be used as an end run around such inveterate precepts,\textsuperscript{75} the practice must rest upon policy considerations unique to the bankruptcy context in which it is employed.\textsuperscript{76} The remainder of part III addresses these bankruptcy considerations.

B. Creditor Equality

One of the most enduring bankruptcy policies is that favoring equal treatment of similarly situated creditors. The Supreme Court has stated “that the object of bankruptcy laws is the equitable distri-

\textsuperscript{74} As discussed infra Part III.B.4.a, limited-fund treatment of such claims, in the absence of a limited fund, results in inequitable distributions amongst the non-debtor’s creditors.

\textsuperscript{75} In discussing federal courts’ general powers under the All Writs Act, discussed infra Part IV.A, the Supreme Court acknowledged that the “All Writs Act is a residual source of authority to issue writs that are not otherwise covered by statute,” which “empowers federal courts to fashion extraordinary remedies when the need arises.” Pennsylvania Bureau of Correction v. United States Marshals Serv., 474 U.S. 34, 43 (1985). Nonetheless, the Court emphasized that “it does not authorize them to issue ad hoc writs whenever compliance with statutory procedures appears inconvenient or less appropriate.” \textit{Id.}

\textsuperscript{76} Indeed, the \textit{Robins} court implicitly, if not expressly, acknowledged as much in approving a non-opt-out class settlement of non-debtor Dalkon Shield claims. One of the primary beneficiaries of the non-debtor releases in the \textit{Robins} case was Robins’ insurer and alleged joint tortfeasor, Aetna. \textit{See supra} notes 8-14 and accompanying text. In conjunction with the plan and its non-debtor release of Aetna, the reorganization court also certified and approved a settlement of the non-debtor class action against Aetna, and the settlement amounts contributed by Aetna were used to fund the plan of reorganization distributions to Dalkon Shield claimants whose claims against Aetna were released and enjoined. \textit{See In re A.H. Robins Co.}, 880 F.2d 709 (4th Cir. 1989), \textit{aff’d} 88 B.R. 755 (E.D. Va.), \textit{and} 85 B.R. 373 (E.D. Va. 1988). Consistent with the nonconsensual nature of the non-debtor releases, though, the Aetna class action was certified for settlement purposes as a mandatory class (with no opt-out rights) under Rule 23(b)(1)(A) of the Federal Rules of Civil Procedure. \textit{See 85 B.R.} at 380-82. A mandatory Rule 23(b)(1)(A) class is generally considered inappropriate for such money damages claims. \textit{See supra} note 70. Nonetheless, the court approved the mandatory settlement class by invoking the needs of the A.H. Robins reorganization, as did the Fourth Circuit, in affirming the mandatory class settlement. \textit{See 85 B.R.} at 381-82 (reasoning that the “effect of permitting Class A members to opt out ... coupled with the loss of Aetna’s contribution to the [Robins] Plan of Reorganization, would be entirely inconsistent with the Bankruptcy Code” and the “objectives of the [Robins] Plan ... will be frustrated if Class A members are permitted to opt out [and] to sue Aetna for compensatory damages”), \textit{aff’d}, 880 F.2d at 742, 749 (explaining that the need to resolve Aetna’s contingent contribution claims against Robins’ bankruptcy estate, inter alia, justifies a mandatory non-opt-out class, and the “[Robins] Plan of Reorganization and the [non-debtor class action] settlement are interdependent” such that “[f]ailure of approval of either the Plan of Reorganization or the ... settlement would derail hopelessly the carefully negotiated and crafted Plan and Settlement”). In doing so, the \textit{Robins} court recognized that Aetna’s aggregate damage exposure would likely be greater if Dalkon Shield claimants had a right to opt out of the class settlement. \textit{See 85 B.R.} at 382 (“Court’s conclusion as to the sums needed to satisfy the Dalkon Shield Claimants did not encompass the added expense which inevitably flows from a multi-party suit.”). The terms of that settlement are discussed infra note 124.
tribution of the debtor's assets amongst his creditors." 77 Pursuant thereto, "[t]he theme of the Bankruptcy Act is 'equality of distribution,' and if one claimant is to be preferred over others, the purpose should be clear from the statute." 78 Courts approving non-debtor releases liberally invoke a creditor equality rationale for support—characterizing the possibility of enhanced recoveries from non-debtors by some claimants as "inequitable" and "unfair." 79 However, by injecting discharge of creditors' non-debtor claims into a process constructed for treatment of creditors' claims against the debtor, non-debtor releases actually upset the Bankruptcy Code's design for creditor equality and permit creditors without valuable non-debtor rights to take value away from creditors with valuable non-debtor rights.

1. Substantial Similarity and Equal Treatment

While creditor equality prevails as a general matter, the Bankruptcy Code does not adopt absolute creditor equality. Rather, the prevailing norm is equal treatment for those similarly situated. 80 Thus, pleas for creditor equality merely beg the question: are these creditors of the same type, such that they should be treated equally, or do differences in their rights warrant different treatment?

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78. Nathanson v. NLRB, 344 U.S. 25, 29 (1952) (citing Sampsell v. Imperial Paper & Color Corp., 313 U.S. 215, 219 (1941)). In fact, the concept of creditor equality traces its origins to the equitable maxim "equality is equity," which had prominent application in mandating pro rata distribution among creditors of insolvent estates. See 1 John N. Pomeroy, A TREATISE ON EQUITY JURISPRUDENCE § 410 (John N. Pomeroy, Jr. ed., 4th ed. 1918). Creditor equality has been a staple of bankruptcy policy since the very first U.S. bankruptcy statute of broad, general applicability, enacted in 1841, ch. 9, 5 Stat. 440, "whose aim [was] to divide the assets equally, and therefore equitably." Shawhan v. Wherritt, 48 U.S. (7 How.) 627, 644 (1849).
79. E.g., Dalkon Shield Claimants Trust v. Reiser (In re A.H. Robins Co.), 972 F.2d 77, 82 (4th Cir. 1992) ("The most obvious threat [from non-debtor actions] is that [Dalkon Shield claimants] could obtain duplicate recoveries, undermining the core purpose of the [plan] to uniformly compensate all Dalkon Shield injuries."); Monarch Life Ins. Co. v. Ropes & Gray (In re Monarch Capital Corp.), 173 B.R. 31, 41 (D. Mass. 1994) (approving, in the context of contempt proceedings, bankruptcy court's confirmation of non-debtor releases and noting "the Bankruptcy Court determined that an injunction was necessary . . . to ensure equal distributions to creditors"), aff'd on other grounds, 65 F.3d 973 (1st Cir. 1995); In re A.H. Robins Co., 88 B.R. 742, 751, 753 (E.D. Va. 1988) (reasoning that "releases and injunction . . . provide equality of treatment of similarly situated creditors" and "ensure . . . [1] systematic evaluation and payment of Dalkon Shield claims in an orderly, fair manner, applying the same rules to all . . . [2] that Dalkon Shield personal injury claimants do not bypass the [plan payments] to the detriment of other Dalkon Shield personal injury claimants [and 3] equality of distribution to Dalkon Shield personal injury claimants"), aff'd sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d 694, 702 (4th Cir. 1989) ("Permitting a [non-debtor] suit by them in violation of the Plan is a . . . defeat of the other creditors."). A § 524(g) injunction, which can include provisions for release of non-debtor asbestos claims, can only be issued upon a finding by the court that "pursuit of such demands outside the procedures prescribed by such plan is likely to threaten the plan's purpose to deal equitably with claims and future demands." 11 U.S.C. § 524(g)(2)(B)(ii)(III) (1994).
80. See SBA v. McClellan, 364 U.S. 446, 452 (1960) (the "policy of equality of distribution for similar creditors expressed in the Bankruptcy Act" does not mandate equal treatment where creditors' nonbankruptcy rights differ (emphasis added)).
In Chapter 11 reorganization proceedings, the search for similarities and differences between creditors is highlighted by the primary statutory provisions codifying the creditor equality policy: sections 1122(a) and 1123(a)(4) of the Bankruptcy Code. Section 1123(a)(4) requires a plan of reorganization to "provide the same treatment for each claim or interest of a particular class"—codifying the equal treatment principle. In designating the various classes to receive equal treatment under the plan, though, section 1122(a) provides that the "plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class." Legislative history indicates that section 1122(a) codifies the 1898 Act practice regarding classification of claims "based on the nature of the claims or interests classified." The "nature" of claims and interests for purposes of classification was primarily concerned with the relative priority rights of creditors and shareholders. Thus, secured creditors with priority in specific assets were classified separately from general unsecured creditors, who had no such lien priority but whose claims ranked ahead of the residual rights of shareholders. Even within the body of unsecured creditors, there might be creditors with statutory or other priority rights that required separate classification. "Classification is simply a method of recognizing [the] difference in rights of creditors which calls for difference in treatment."

82. Id. § 1122(a) (emphasis added).
83. H.R. REP. NO. 95-595, at 406 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6362; see also S. REP. NO. 95-989, at 118 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5904. In Chapter X corporate reorganization proceedings, section 197 of the 1898 Act provided that "[f]or the purpose of the plan and its acceptance, the judge shall fix the division of creditors and stockholders into classes according to the nature of their respective claims and stock.” 1898 Act § 197, reprinted in 6, pt. 2 COLLIER (14th ed. 1978), supra note 46, at 1493. In Chapter XI arrangement proceedings, the 1898 Act also provided that "[f]or the purposes of the arrangement and its acceptance, the court may fix the division of creditors into classes.” 1898 Act § 351, reprinted in 9 COLLIER (14th ed. 1978), supra note 46, at 1. This division of claims into classes was also "according to their nature.” 9 COLLIER (14th ed. 1978), supra note 46, ¶ 8.06, at 177. Likewise, in Chapter XII real property arrangements, "[f]or the purposes of the arrangement and its acceptance, the court may fix the division of creditors into classes according to the nature of their respective claims.” 1898 Act § 452, reprinted in 9 COLLIER (14th ed. 1978), supra note 46, at 997. The congressional commission charged with study and reform recommendations that ultimately led to the 1978 Bankruptcy Reform Act, proposed designation of "classes of creditors and equity security holders which are of substantially similar character and the members of which enjoy substantially similar rights,” classification criteria they “derived from §§ 197, 357, and 452 of the [1898] Act.” COMMISSION ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, pt. II, at 241 (1973) [hereinafter COMM’N REPORT] (proposed section 7-302 & note). The role of the congressional commission in the process that culminated in enactment of the Bankruptcy Code is described in 1 COLLIER (15th ed.), supra note 40, ¶¶ 1.01[2], 1.06[1][a].
84. See generally COMM’N REPORT, supra note 83, pt. II, at 241 ("liquidation priorities are applicable [in determining] claims of a substantially similar nature"); 6, pt. 2 COLLIER (14th ed. 1978), supra note 46, ¶¶ 9.10, at 1597-1603, 9.13[1]; 9 id. ¶ 7.02, at 1005-06.
With respect to non-debtor releases, the simple response to the creditor equality argument is that creditors that have recourse against non-debtors are not similarly situated with creditors that have no such rights; therefore, permitting creditors to pursue non-debtors in no way violates the policy of equal treatment for similarly situated creditors. In fact, a plan of reorganization that classifies together, for equal treatment, creditors both with and without non-debtor recourse, while eliminating the rights of those with non-debtor recourse, actually undermines the Bankruptcy Code’s classification and treatment scheme. It is an attempt to impose equal treatment amongst creditors whose rights are not “substantially similar,” within the meaning of section 1122(a).

The courts have sidestepped the classification and equal treatment problems engendered by non-debtor releases by considering each Bankruptcy Code section in isolation and only with reference to creditors’ rights against the debtor. But section 1123(a)(4)’s require-

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86. This unequal treatment can be graphically represented as follows:

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Non-Debtor
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      /   \
     /     
    /      
Debtor
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87. Placing creditors with substantially different rights in the same class is unambiguously prohibited by § 1122(a). See 11 U.S.C. § 1122(a). A more difficult question is whether all creditors with substantially similar rights must be placed in the same class, or whether such creditors can be separated into two or more homogenous classes. Much has been written about this issue, especially with respect to separate classification of an undersecured creditor’s deficiency claim. See, e.g., John C. Anderson, Classification of Claims and Interests in Reorganization Cases Under the New Bankruptcy Code, 58 AM. BANKR. L.J. 99 (1984); David Gray Carlson, The Classification Veto in Single-Asset Cases Under Bankruptcy Code Section 1129(a)(10), 44 S.C. L. REV. 565 (1993); Jeffrey C. Krause, The Bias of the Courts Against Single-Asset Real Estate Cases Is Creating Bad Law in the Area of Classification, 22 CAL. BANKR. J. 47 (1994); Bruce A. Markell, Cleverless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification, 11 BANKR. DEV. J. 1 (1995) [hereinafter Markell, Classification]; Peter E. Meltzer, Disenfranchising the Dissenting Creditor Through Artificial Classification or Artificial Impairment, 66 AM. BANKR. L.J. 281 (1992); Louis S. Robin, Classification of Claims: An Examination of Disregarding Legislative History, 98 COM. L.J. 225 (1993); Linda J. Rusch, Gerrymandering the Classification Issue in Chapter Eleven Reorganizations, 63 U. COLO. L. REV. 163 (1992); Linda J. Rusch, Single Asset Cases and Chapter II: The Classification Quandary, 1 AM. BANKR. INST. L. REV. 43 (1993).

88. The classification and treatment issues have been addressed mostly in the context of consensual non-debtor releases. See, e.g., In re AOV Indus., Inc., 792 F.2d 1140, 1150-54 (D.C. Cir. 1986); In re Respo, Inc., 24 B.R. 412, 422, 447-48, 467-68 (Bankr. D.N.J. 1980); In re Orlando Investors, L.P., 103 B.R. 593, 596-97 (Bankr. E.D. Pa. 1989); In re Monroe Well Serv., Inc., 80 B.R. 324, 335-36 (Bankr. E.D. Pa. 1987). The AOV court was the first to recognize the problem. The D.C. Circuit, however, characterized non-debtor releases as raising a problem of unequal treatment, rather than an improper classification problem.

The other side of the coin of unequal payment, however, has to be unequal consideration tendered for equal payment. It is disparate treatment when members of a common class are required to tender more valuable consideration—be it their claim against specific property
ment of equal treatment goes hand in hand with section 1122(a)'s requirement of substantial similarity, and the two can be considered only in tandem. As Professor Markell has noted, classification issues do not exist in a vacuum; proper classification can only be determined with reference to a plan's treatment of creditor claims.89 The creditor rights that are relevant to assessing substantial similarity for purposes of classification are those rights being affected by the plan, which in-

89. See Markell, Classification, supra note 87, at 16-17, 25-26. For example, when creditors with identical priority rights vis-à-vis the debtor are parties to an intercreditor subordination agreement, a plan can place both the senior and subordinated claims in the same class only if the intercreditor subordination rights survive unaffected by the plan of reorganization. See Daniel C. Cohn, Subordinated Claims: Their Classification and Voting Under Chapter 11 of the Bankruptcy Code, 56 AM. BANKR. L.J. 293, 310 (1982); Thomas C. Given & Linda J. Philipps, Equality in the Eye of the Beholder—Classification of Claims and Interests in Chapter 11 Reorganizations, 43 OHIO ST. L.J. 735, 747 (1982); Markell, Classification, supra note 87, at 45-46.
cludes non-debtor rights when the plan extinguishes such rights through non-debtor releases. Although it is true that Congress' intended reach for both section 1122(a) and section 1123(a)(4) likely was limited to creditors' claims against the debtor,90 it is also true that Congress clearly intended that creditors' rights against non-debtors, as a norm, would remain untouched by the debtor's plan of reorganization by virtue of section 524(e).91 Assuming arguendo that section 524(e) does not prohibit the plan from altering creditors' non-debtor claims, if the plan does release non-debtor claims, this expanded treatment of claims must lead to a more expansive role for the Bankruptcy Code's treatment and classification provisions. To put it another way, if the plan departs from the debtor-only default mode with respect to section 524(e), the debtor-only default rules of sections 1122(a) and 1123(a)(4) are no longer appropriate.92

Proponents of non-debtor releases cannot have it both ways. If creditor equality notions require consideration of creditors' rights against non-debtors in an attempt to assure equal treatment, then those non-debtor rights must also be considered in assessing substantial similarity of creditors' rights for purposes of appropriate classification.93 The importance of appropriate classification becomes clearer

90. On their face, though, those sections are not so limited. Both sections deal with "claims." See 11 U.S.C. § 1122(a) (1994) (classification of "claims"); id. § 1123(a)(4) (treatment of "claims"). The Bankruptcy Code defines "creditor" as an entity with a "claim" against the debtor. Id. § 101(10)(A). "Claim" and "debt," by contrast, are merely defined in the abstract as, respectively, a "right to payment" and "liability on a claim," without any reference to the debtor. Id. § 101(5)(A), (12). Thus, those terms could encompass a creditor's rights against both the debtor and personally responsible non-debtors, an interpretation reinforced by § 524(e). See id. § 524(e) ("[D]ischarge of a debt of the debtor does not affect the liability of any other entity on ... such debt " (emphasis added)).
91. 11 U.S.C. § 524(e), discussed supra Part II.B.
93. What little 1898 Act case law on the issue exists, supports the view that non-debtor releases violate the policy of equal treatment for similarly situated creditors, as reflected in plan classification and treatment rules. In the case of In re Nine North Church Street, Inc., 82 F.2d 186 (2d Cir. 1936), the debtor's real property was encumbered by mortgage bonds issued by another company and guaranteed by a trust company. Prior to the debtor's bankruptcy filing, the bonds were in default, and the trust company proposed a restructuring of the debt that would alter its guaranty liability in the same manner—an offer accepted by many of the bondholders. Others, however, refused to consent and sued the trust company on its guaranty. The debtor then filed bankruptcy reorganization proceedings, proposing a plan that would restructure the remainder of the mortgage bond debt, including an alteration of the trust company's guaranty liability, treating all of the mortgage bond debt as one class. See id. at 187-88. The reorganization court approved the plan, but the Second Circuit reversed. In addition to holding that it was improper to alter the non-debtor trust company's liability to creditors, the Second Circuit also held that the plan's classification scheme was improper. See id. at 188-89. Some of the bondholders had already reduced their rights against the trust company, while others had not. Therefore, the creditors were not substantially similar enough to be classified together and/or the plan was providing improper disparate treatment amongst the class members: "Either there were two classes of creditors, with no consents from the second class, ... or there was a single class of creditors, with no reduction made in the rights of some of these, those certificate holders whose rights were already modified." Id. at 189; see also Hamburger v. Dyer (In re Hamburger), 117
when considering the Bankruptcy Code provisions governing voting on and distributions under the plan of reorganization.

2. **Class Voting and Impairment**

Non-debtor releases' tarnish on the initial classification and treatment of claims permeates the process by which the plan of reorganization is confirmed, because classification is the means by which the plan both allocates value amongst the creditors and binds dissenting creditors to its terms. Thus, the creditor equality problems caused by non-debtor releases infect the entire confirmation process.\(^\text{94}\)

Classification concerns initially take on importance under the Bankruptcy Code, because classification is an integral part of the procedural means by which dissenters or "holdouts" are bound to the reorganization plan's provisions. One method by which dissenters can be bound is through class voting on the plan of reorganization.\(^\text{95}\) Members of a class are entitled to vote on acceptance or rejection of the plan only if the plan's treatment of the class impairs creditors' nonbankruptcy rights.\(^\text{96}\) The court can confirm the plan, notwithstanding the dissent of holdout class members, if a majority of the class' creditors, holding at least two-thirds of the total dollar amount of class claims, vote to accept the plan.\(^\text{97}\)

Ignoring the classification and treatment implications of non-debtor releases inevitably weakens the creditor protections underlying a class voting scheme. The ability to bind dissenters through a class vote makes appropriate classification the touchstone of protecting the rights of dissenters. This is the historical function of classification.\(^\text{98}\)

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\(^{95}\) Class voting is the means by which *individual* dissenters are bound to the plan. Dissenting *classes* can be bound through "cram down," discussed *infra* Part III.B.3.a.

\(^{96}\) See 11 U.S.C. § 1124 (defining "impairment"); id. § 1126(a), (f) (only impaired classes vote).

\(^{97}\) See 11 U.S.C. § 1126(c) (acceptance by class); id. § 1129(a)(8) (plan can be confirmed if, inter alia, impaired classes accept). When a dissenter is a member of an accepting class, the dissenters' only protection from the will of the majority is that the plan must give the dissenter at least as much as a Chapter 7 liquidation would—the so-called best interests of creditors test. See id. § 1129(a)(7)(A), discussed *infra* Part III.B.3.b.

\(^{98}\) After tracing the history of classification in compositions, arrangements, equitable receiverships, and statutory reorganization proceedings, Professor Markell concludes:

If nothing else, the history of classification constitutes the history of the effort to construct classes so as to enable them to vote on debt relief. Behind the assumption that voting is meaningful lies the notion that some common interest exists among members of a class. Otherwise, it makes little sense to say that anything less than a unanimous vote could bind dissenters.

The danger of inappropriate classification, by combining creditors with substantially different rights, is that classes can be manipulated to produce class assent by diluting the voice of dissenters, placed in classes filled with agreeable creditors (perhaps agreeable because their non-debtor rights are not being trampled as much as those of the dissenters).\textsuperscript{99} We can only place confidence in the assent of a class if the class has uniform rights and treatment. By their nature, non-debtor releases only affect class members with valuable non-debtor rights. If destruction of those creditors’ non-debtor rights is ignored in constructing classes, the integrity of the class voting process is corrupted. In fact, machinations of the process can go so far as to completely disenfranchise impaired creditors.

A class is entitled to vote on the plan of reorganization only if the plan impairs class members’ rights. If the plan “leaves unaltered the legal, equitable, and contractual rights” of class members, such an unimpaired class is deemed to accept the plan and its treatment.\textsuperscript{100} Consistent with the non-debtor release approach to creditor equality and treatment, the impairment standard must be read to refer only to creditors’ “legal, equitable, and contractual rights” against the debtor.\textsuperscript{101} Under this approach, though, a plan conceivably could leave all creditors’ rights against the debtor fully intact, while completely extinguishing any creditor’s right to seek payment from a non-debtor, and the plan could be confirmed without even submitting it to a creditor vote.\textsuperscript{102} Before this hypothetical is dismissed as the unreal-

\begin{footnotesize}
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\item[99.] See 7 Collier (15th ed.), supra note 40, ¶ 1122.03[6], at 1122-21; Markell, Classification, supra note 87, at 16, 26.
\item[100.] 11 U.S.C. § 1124(1); see id. § 1126(a), (f).
\item[101.] As with §§ 1122(a) and 1123(a)(4), though, no such limitation appears on the face of the statute, which refers to impairment of abstract “claims.” See 11 U.S.C. § 1124; see also supra note 90 and accompanying text.
\item[102.] Of course, the feasibility requirement of § 1129(a)(11) would require a finding that the debtor could actually satisfy its obligations to creditors if they were left unimpaired. 11 U.S.C. § 1129(a)(11). Because there is no insolvency requisite to initiate voluntary Chapter 11 proceedings, though, for the strategic-minded, presently solvent debtor looking to lift the burden of potential personal liability from officers, directors, banks, and the like, a Chapter 11 plan with non-debtor releases is not completely outside the realm of possibility. More realistically, the strategy could be used on a limited basis, for example, by promising only particular classes unimpaired treatment in the plan, but using a non-debtor release to relieve non-debtors from any further liability to the class. The harm to the creditors is obvious when one realizes that the plan’s promise of unimpaired treatment is just that—a promise—that may or may not come to pass. See, e.g., Edith S. Hotchkiss, Postbankruptcy Performance and Management Turnover, 50 J. Fin. 3, 10, 15 (1995) (empirical study of 197 public companies emerging from Chapter 11 as operating entities, finding that over 40% continued to experience operating losses in the following three years, and 32% required further restructuring through a second bankruptcy filing, a private workout or an out-of-court liquidation); Susan Jensen-Conklin, Do Confirmed Chapter 11 Plans Consummate? The Results of a Study and Analysis of the Law, 97 COM. L.J. 297, 324-25 (1992) (empirical study of 45 confirmed Chapter 11 plans, finding only 58% completed all payments to creditors under the plan); Lynn M. LoPucki & William C. Whitford, Patterns in the Bankruptcy Reorganization of Large, Publicly Held Companies, 78 CORNELL L. REV. 597, 608 (1993) (empirical study of large Chapter 11 cases, finding that in 32% of cases where the entity survived confirmation of a plan, the emerging entity subsequently filed another Chapter 11 case). Thus, when courts rely on promises or projections of full payment to creditors in approv-
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istic ruminations of a law professor, consider the fact that this scenario roughly approximates what actually occurred in the Drexel case.

As part of the confirmation process in the Drexel case, the court certified a mandatory Rule 23 class action, with the class consisting of those Drexel creditors filing bankruptcy claims against Drexel based on securities law violations.\textsuperscript{103} In conjunction with the class action certification, the court also approved a settlement of Drexel's aggregate liability to the securities litigation claimants; these amounts, then, would be paid to the claimants pursuant to the terms of Drexel's plan of reorganization.\textsuperscript{104} Both the district court and the Second Circuit held that this mandatory compromise of the securities litigation creditors' claims established the "legal, equitable, and contractual rights" of the creditors vis-à-vis the debtor, leaving them unimpaired and unable to vote on the terms of the reorganization plan.\textsuperscript{105} Had the Drexel plan of reorganization done nothing more than provide for payment in full of this "agreed" liability, this conclusion might have been defensible.\textsuperscript{106} However, the non-opt-out settlement and reor-
organization plan also provided for a nonconsensual release of any further securities actions by creditors against certain Drexel personnel.\textsuperscript{107} Thus, securities litigation creditors were forced to relinquish whatever rights they might have to further pursue these non-debtors, under circumstances in which the nature of their settlement with Drexel implicitly recognized the fact that they were not being fully compensated.\textsuperscript{108} Even though the Drexel plan took away any "legal, equitable, and contractual" rights they might have to seek further satisfaction from released non-debtors, disregarding the plan's treatment of these non-debtor rights left them with no vote on the plan of reorganization. Consequently, they could look to none of the distribution value protections the Bankruptcy Code affords dissenters through the "cram down" and "best interests of creditors" provisions.

3. Distribution Value Protections

The ultimate injury non-debtor releases visit upon creditors is distributional. Creditors without valuable non-debtor rights can take value away from creditors whose valuable non-debtor rights are extinguished through non-debtor releases. This redistribution occurs because non-debtor releases undermine the Bankruptcy Code's distribution value protections.

Creditor equality notions embedded in the Bankruptcy Code classification and treatment provisions provide creditors with an initial assurance of procedural protection—they will be bound by the class votes of only similarly situated and treated creditors. The procedural protection of voting rights is, at the least, significantly weakened and, at times, completely eviscerated by indiscriminate non-debtor releases. The Bankruptcy Code also gives dissenting creditors an additional level of more substantive protections with respect to the value protections, discussed infra Part III.B.3. See 11 U.S.C. § 1126(f) (unimpaired class and each creditor in unimpaired class is deemed to accept the plan); id. § 1129(a)(7)(A) ("best interests" protection only applies to dissenting creditors); id. § 1129(a)(8), (b)(1) ("cram down" protections apply only to dissenting classes).

\textsuperscript{107} See Drexel, 130 B.R. at 928, aff'd, 960 F.2d at 288-89, 293 (approving class action certification and settlement); In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 745, 753-54, 756, 772-73 (Bankr. S.D.N.Y. 1992) (confirming the reorganization plan). The only non-debtor actions excepted from the scope of the Drexel non-debtor releases were the pending non-debtor suits of a particular subclass of securities litigation claimants. Even these claimants, though, were enjoined from bringing any further non-debtor actions against the released Drexel personnel. See Drexel Burnham Lambert Group, Inc. v. Claimants Identified on Schedule 1 (In re Drexel Burnham Lambert Group, Inc.), 995 F.2d 1138, 1143 (2d Cir. 1993); Drexel, 960 F.2d at 288-89, 293.

\textsuperscript{108} See supra note 106. In addition to the limited-fund finding, the court also (1) upheld the amount of the settlement liability because Drexel's assets were insufficient to withstand a greater judgment, and other parties also bore responsibility for the alleged securities violations, and (2) noted that the amount of the aggregate judgment capped Drexel's exposure and would necessitate further allocations amongst claimants—all items that tacitly recognized the great likelihood of less than full payment to the securities litigation claimants. See Drexel, 130 B.R. at 921-22, 925-26, aff'd, 960 F.2d at 291, 292-93.
of creditor distributions. One set of these distribution value protections, the so-called cram down rules, protect dissenting classes of creditors. The protection known as the "best interests of creditors" test protects individual dissenting creditors. The wrong-headed approach to creditor equality advanced by proponents of non-debtor releases distorts the application of these distribution value protections.

a. Cram Down

The class voting structure of the Bankruptcy Code is built around the philosophy that the parties should be able to negotiate and agree, by class vote, on the distribution of the value of the reorganized entity amongst the various classes of creditors and equity security holders. A class that rejects the plan's proposed value allocations, though, can enforce its priority rights through the cram down protections of section 1129(b). Then, the court can confirm the plan only if it is "fair and equitable" and "does not discriminate unfairly" with respect to the dissenting class.

In general, the "fair and equitable" requirement protects dissenting unsecured creditors' rights vis-à-vis senior and junior classes. Unless the dissenting class members are paid in full, senior classes cannot receive more than full payment and junior classes can receive nothing. Protection against "unfair discrimination" assures that the


112. 11 U.S.C. § 1129(b)(1) (1994). In addition, at least one impaired class must accept the plan. See id. § 1129(a)(10).

dissenting class will receive treatment reasonably commensurate with that of classes with an equivalent priority rank.\(^{114}\)

The cram down rules, thus, give classes baseline protection against what they regard as an improper apportionment of the debtor’s reorganization value. To the extent that non-debtor releases infect the soundness of the classification system, they dilute the voting power of those creditors with valuable non-debtor rights, and as a consequence, they also weaken those creditors’ ability, by class vote, to block distributions that depart from their baseline priority rights. And that is the nub of the nefarious nature of non-debtor releases: they permit improper redistributions of value amongst the debtors’ creditors. The extent of the redistribution becomes even clearer in light of the “best interests of creditors” test, a protection invoked by individual dissenting creditors that even class acceptance cannot preempt.

b. Best Interests of Creditors

The best interests test of section 1129(a)(7) provides that the court can confirm a plan of reorganization only if the plan will give each individual dissenting creditor at least as much as the dissenter would receive in a Chapter 7 liquidation of the debtor.\(^{115}\) This scheme recognizes that the debtor may be more valuable as a reorganized entity than if its assets were sold piecemeal through a Chapter 7 liquidation, producing a reorganization or “going concern” surplus over liquidation value.\(^{116}\) Because the cram down rules protect only dissenting classes, they permit consensual redistribution of this reorganization surplus among classes through class acceptances.

\(\text{U.S.C.C.A.N. at 6370; 7 Collier (15th ed.), supra note 40, ¶ 1129.04}[a][ii]; Klee, Cram Down II, supra note 94, at 231-32.}

\(^{114}\) Absence of unfair discrimination may well be part-and-parcel of the historical concept of fair and equitable treatment. See generally 9 Collier (14th ed. 1978), supra note 46, ¶¶ 8.06, at 177-78 & n.12, 9.18[2], at 291-92. In fact, the term “fair and equitable” was derived from the original corporate reorganization statute, which phrased the requirement as “fair and equitable and does not discriminate unfairly.” See 9 id. ¶¶ 9.18[1], at 287 n.4, 9.18[2], at 292 n.16, 9.07[4], at 1141-42 (discussing 1898 Act § 77B(f)(1)). The unfair discrimination component was set forth explicitly again in Bankruptcy Code § 1129(b)(1) “for clarity.” See 124 Cong. Rec. 32,407 (1978) (statement of Rep. Edwards, sponsor); id. at 34,006 (statement of Sen. DeConcini, sponsor). There are statements in the legislative history indicating that giving classes of equal priority anything other than “an exact aliquot distribution” constitutes unfair discrimination. H.R. Rep. No. 95-595, 1978 U.S.C.C.A.N. at 6372. However, some courts permit discrimination between equivalent classes, if they consider the discrimination to be “fair.” See generally 6 Chapter 11 Theory and Practice: A Guide to Reorganization § 31.07 (James F. Queenan, Jr. et al. eds., 1995) [hereinafter Chapter 11 Theory and Practice]; Carlson, supra note 87, at 571 n.21.


\(^{116}\) In fact, preservation of reorganization surplus is Congress’ stated purpose for enactment of reorganization provisions. See H.R. Rep. No. 95-595, at 220 (“The premise of a business reorganization is that assets that are used for production in the industry for which they were designed are more valuable than those same assets sold for scrap.”), reprinted in 1978 U.S.C.C.A.N. at 6179.
notwithstanding the dissent of minority class members. In the absence of complete creditor and shareholder unanimity, however, liquidation value for each creditor is inviolable by virtue of the best interests test.\textsuperscript{117}

In a Chapter 7 liquidation proceeding, creditors retain their rights to pursue non-debtors for full payment, because there is no reorganization to protect by providing non-debtor releases. Thus, giving at least liquidation value to each creditor requires protection of the Chapter 7 right to pursue non-debtor actions. The lopsided view of creditor equality, which sanctions confiscation of these non-debtor rights in Chapter 11 through non-debtor releases, ignores the creditors’ Chapter 7 right to seek full satisfaction from non-debtors in gauging satisfaction of the best interests test—comparing a creditor’s Chapter 11 distribution with a hypothetical Chapter 7 distribution, from the debtor only.\textsuperscript{118} Yet, the best interests equation also properly mandates consideration of creditors’ comparative recoveries on non-debtor claims, to the extent the plan is treating those non-debtor claims by release.\textsuperscript{119}

Proponents of non-debtor releases are quick to point out that released parties often make contributions to the debtor that enhance the reorganization surplus—contributions that would not be forthcoming in a Chapter 7 liquidation.\textsuperscript{120} These contributions, however, do not fully compensate for the released claims. In fact, non-debtor contributions merely serve to redistribute the value of the released non-debtor claims.

As noted above, nothing in the process by which releases are approved requires contributions by released non-debtors to approximate the value of the released claims,\textsuperscript{121} and one might surmise that the debtor (and creditors and shareholders without valuable non-debtor rights) are content to take a contribution worth less than the value of the released claims. Even if the released party were to contribute to

\textsuperscript{117} See Markell, Absolute Priority, supra note 111, at 87-89; Markell, Classification, supra note 87, at 29.

\textsuperscript{118} As with classification, treatment, and impairment, though, the statute is not restricted to “claims” against the debtor. See supra notes 90 and 101. It requires a comparison of what a holder would receive under the plan on account of an abstract “claim” with the amount the holder would receive if the debtor were liquidated under Chapter 7. See 11 U.S.C. § 1129(a)(7)(A)(ii).

\textsuperscript{119} See Feldstein, Third-Party Releases, supra note 20, at 43.


\textsuperscript{121} See supra notes 62-69 and accompanying text.
the reorganization the full value of the released claims (or more), there is still no assurance that creditors whose non-debtor claims are extinguished will receive as much as they would under a Chapter 7 liquidation scenario. This is because the non-debtor's contribution to the reorganization is not necessarily earmarked for those creditors whose non-debtor claims are released. The contribution goes into the reorganization pot, for distribution amongst all of the debtor's creditors and shareholders, regardless of whether they have valuable non-debtor claims.

The driving force behind non-debtor releases seems to be a relentless desire to steadfastly avoid articulating and valuing what and whose claims are being released. As a result, non-debtor releases

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122. The risk averse non-debtor would be willing to trade a greater certain contribution in exchange for release from a lower projected, but uncertain, liability outside bankruptcy. Of course, the non-debtor also should be willing to strike the same deal directly with the creditor.

123. See supra notes 64-69 and accompanying text. This redistribution of the value of the released non-debtor claim can be graphically represented as follows:

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            Non-Debtor  ---- $ ----> Debtor
                               |
                             released
                             non-debtor
                             action

                           Creditor
                             $ equal
                             bankruptcy
                             claims

                             Creditor
```

124. In some respects, the Robins case is exceptional in this regard, but only partially. With respect to Dalkon Shield claimants' non-debtor tort claims against Robins' insurer, Aetna, the court actually certified and approved a class action settlement of those non-debtor claims. Dalkon Shield Claimants' Comm. v. Aetna Cas. & Sur. Co. (In re A.H. Robins Co.), 85 B.R. 373 (E.D. Va.), and 88 B.R. 755 (E.D. Va. 1988), aff'd, 880 F.2d 709 (4th Cir. 1989), discussed supra note 76. Nonetheless, there are reasons to believe that the amounts contributed by Aetna were much less than Aetna would have paid Dalkon Shield claimants in the absence of Robins' reorganization. First, and as discussed above, the court used Robins' reorganization to justify a mandatory non-opt-out class, thereby imposing a nonconsensual settlement on the Dalkon Shield claimants, fully recognizing that this would reduce Aetna's damage exposure. See supra note 76. In addition, in certifying the class action, the court noted that the class claims were for compensatory damages only, and the action would not resolve punitive damage claims against Aetna, saying that it was appropriate to have a uniform mechanism for payment of punitive damages through the plan of reorganization. See 85 B.R. at 382-83. In later confirming the plan, though, the court decided to disallow any claims for punitive damages. So Aetna's compensatory damages contribution bought it a release from both compensatory and punitive damages liability. See 880 F.2d at 722 & n.16 (affirming settlement and noting Aetna's release and disallowance of punitive damages under the plan); In re A.H. Robins Co., 89 B.R. 555 (E.D. Va. 1988) (disallowing punitive damages); In re A.H. Robins Co., 88 B.R. 742, 751, 752, 753-55 (E.D. Va. 1988) (confirming plan with non-debtor releases and disallowance of punitive damages), aff'd sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d 694, 700-02 (4th Cir. 1989).

The only provision for punitive damages was that Dalkon Shield claimants could share pro rata in any excess funds remaining in the claimants' trust after full satisfaction of all compensatory damages claims, "in lieu of" punitive damages. See 89 B.R. at 559 n.2.

Quite apart from the adequacy of Aetna's contribution, there were even more drastic abridgements of Dalkon Shield claimants' non-debtor rights that would not prevail in Chapter 7. Members of the Robins family were also defendants in the class action and beneficiaries of the plan's non-debtor releases. See supra notes 11-14 and accompanying text. Yet, noticeably absent from the judicial approvals of the class action settlement is any scrutiny of their potential liability, as opposed to that of Aetna. See 88 B.R. at 758-63, aff'd, 880 F.2d at 748-52; 880 F.2d at 700, 701 n.6. The Robins family did make a contribution to the fund for compensation of
present an opportunity for those without viable non-debtor claims to take value away from those with such claims. Contributions by released non-debtors, made in the name of the debtor's reorganization effort, simply obscure the underlying value redistributions inherent in non-debtor releases.

This classification and treatment discussion might lead one to believe that non-debtor releases should be permissible if classes are constructed and distribution value protections are applied with appropriate sensitivity to the non-debtor rights being destroyed by non-debtor releases. Although such an approach would defeat the manifest object of non-debtor release provisions to bypass these protections and likely deter efforts to obtain approval of non-debtor releases, it would not cure all of the creditor inequality ills of non-debtor releases; it would only remedy creditor inequality amongst the debtor's creditors. Because non-debtor releases interject discharge of creditors' non-debtor rights into a bankruptcy process designed to restructure only creditor claims against the debtor, non-debtor releases also undermine creditors' bankruptcy protections in their relationship with the released non-debtor and that non-debtor's other creditors.

4. The Non-Debtor's "Discharge"

Non-debtor releases systematically dismantle the Bankruptcy Code's attempt to carefully protect the relative payment rights of creditors of a Chapter 11 debtor, with nothing more than a simple proclamation of a beguiling, distorted view of the Bankruptcy Code's creditor equality policy. Furthermore, the perverse effects of non-debtor releases go beyond the relative rights of the debtor's creditors; they also do violence to the rights of the permanently enjoined creditor vis-à-vis (1) other creditors of the released non-debtor and (2) the released non-debtor. A non-debtor release is a discriminatory dis-

Dalkon Shield claimants—one that the reorganization court, in confirming the plan, found to be "valuable consideration for the releases." 88 B.R. at 751. The Fourth Circuit, though, in affirming the settlement, characterized these amounts as "minimal contributions." See 880 F.2d at 721 & n.15. The $10 million contribution was, indeed, minimal, given that the Robins family simultaneously received, under the plan of reorganization, American Home Products stock worth $385 million, as a tax-free distribution on their A.H. Robins stock. See Sobol, supra note 10, at 221-22, 286. Perhaps most significantly, the scope of the non-debtor releases went beyond those third parties making contributions toward compensation of the Dalkon Shield claimants and affirmatively restrained Dalkon Shield claimants from suing anyone for injuries caused by the Dalkon Shield. See supra notes 8-14 and accompanying text. Not surprisingly, the reorganization court avoided all of these messy issues by restricting its best interests analysis to the "liquidation value of the Debtor" only. 88 B.R. at 748; see also 89 B.R. at 560 (stating that best interests test "simply provides an assurance that funds made available in a Chapter 11 estate is at least as much as would be made available in the liquidation of a Chapter 7 estate").

125. This reinforces the notion that the debtor and its creditor and shareholder constituencies often might be willing to take a contribution worth less than the released claims. Those without valuable non-debtor rights still stand to benefit, because they give up nothing while sharing in the non-debtor's contribution to the reorganization.
charge of only certain debts of the non-debtor, in violation of basic creditor equality norms. This discharge comes without giving released creditors recourse to the non-debtor's full repayment resources—violating another basic tenet of distribution and discharge principles. Worse yet, the non-debtor’s discharge can extinguish debts that would not be dischargeable in an individual bankruptcy case.

a. Equitable Treatment of the Non-Debtor’s Creditors

One of the most frequent objections to non-debtor releases is that they give the released non-debtor the benefit of a bankruptcy discharge without having to file a bankruptcy petition. Of course, the “discharge” effected by a non-debtor release is only a partial discharge, and not nearly as broad and all-encompassing as that available through an actual bankruptcy filing. Thus, rather than focusing on the improper benefit the non-debtor obtains from a release, initially, it is even more useful to analyze the problem from the standpoint of the released non-debtor's creditors.

Addressing Congress' bankruptcy power, the Supreme Court has said:

[I]t extends to all cases where the law causes to be distributed, the property of the debtor among his creditors; this is its least limit. Its greatest, is the discharge of a debtor from his contracts. And

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126. It has been a cardinal principle of bankruptcy law from the beginning that its effects do not normally benefit those who have not themselves “come into” the bankruptcy court with their liabilities and all their assets.

To violate this principle . . . is simply to invite a wholesale restructuring of the expectations of those involved in commercial transactions without any indication from Congress that such a profound change was intended.


127. See 11 U.S.C. §§ 727(b), 1141(a), (d)(1)(A), 1228(a), (c), 1328(a), (c) (1994) (with limited exceptions, bankruptcy discharge is of all prebankruptcy debts of the debtor).

128. This approach is also consistent with the historical function of bankruptcy laws as a creditor protection device. The discharge, although a very important component of our contemporaneous bankruptcy law, arrived on the scene relatively recently. See generally Richard I. Aaron, Theory and History of Chapter 11, in 1 Chapter 11 Theory and Practice, supra note 114, ch. 1, § 1.11; Charles J. Tabb, The Historical Evolution of the Bankruptcy Discharge, 65 AM. BANKR. L.J. 325 (1991) [hereinafter Tabb, Discharge]; Charles J. Tabb, The History of the Bankruptcy Laws in the United States, 3 AM. BANKR. INST. L. REV. 5, 6-32 (1995). Even today, for corporations, who are often the immediate beneficiaries of non-debtor releases, the discharge is, in the main, a creditor-oriented protection. See infra notes 152-60 and accompanying text.
all intermediate legislation affecting substance and form but tending to further the great end of the subject—distribution and discharge—are in the competency and discretion of Congress.\textsuperscript{129} Moreover, these dual aims of bankruptcy law, distribution and discharge, are interrelated. If a creditor’s obligation is to be discharged pursuant to the bankruptcy power, the creditor must first be permitted to participate in a distribution of the debtor’s assets on an equitable basis, with Congress defining the contours of the equitable distribution scheme through duly enacted bankruptcy legislation.\textsuperscript{130} This creditor-oriented approach to the discharge power makes clear why the partial discharge effected by non-debtor releases is objectionable. The release discharges only some of the non-debtor’s obligations—without submitting all of the non-debtor’s assets to a fair, orderly, and ratable distribution amongst all of the non-debtor’s creditors.

A non-debtor release is a discriminatory discharge, discharging some, but not all of the debts of the released non-debtor. As such, it directly contravenes the Bankruptcy Code’s policy of equal treatment of similarly situated creditors. Creditors subject to the release are restricted to their diminished recovery rights under the Chapter 11 debtor’s plan of reorganization, while others with similar payment rights against the released non-debtor retain the right to seek full payment from the non-debtor. As discussed above, among the Chapter 11 debtor’s creditors, non-debtor releases improperly impose equal treatment on unequal creditors.\textsuperscript{131} Among the released non-debtor’s creditors, the converse inequality results; non-debtor releases bring unequal treatment for equal creditors.\textsuperscript{132}

This aspect of creditor inequality—amongst the non-debtor’s creditors—is easily overlooked. Yet, this inequality points out why it is particularly misguided to attach significance, as many courts do, to creditor approval percentages in voting on the Chapter 11 debtor’s

\begin{itemize}
  \item \textsuperscript{129} Hanover Nat’l Bank v. Moyses, 186 U.S. 181, 186 (1902).
  \item \textsuperscript{130} See Kuehner v. Irving Trust Co., 299 U.S. 445, 450-56 (1937). Here, as in several other respects, non-debtor releases raise serious constitutional concerns. This article will not fully address these constitutional issues, but rather suggests that an appropriate construction of the Bankruptcy Code, which denies courts the power to approve non-debtor releases, properly avoids any constitutional infirmity.
  \item \textsuperscript{131} See supra Part III.B.1.
  \item \textsuperscript{132} This unequal treatment can be graphically represented as follows:
\end{itemize}
plan of reorganization, as somehow sanctioning the worth of a non-debtor release.\footnote{133} As previously discussed, the non-debtor release itself impugns the integrity of the Chapter 11 debtor's voting classes, and, in any event, class voting cannot waive best interests protection for individual creditors.\footnote{134} Even more fundamentally, though, class voting by creditors of the Chapter 11 debtor says nothing about an appropriate distribution of the assets of the released non-debtor. The approach of Chapter 11 is that class voting will determine distribution of value amongst a debtor's creditors and owners. This voting scheme, however, assumes that voting is amongst properly constructed classes of similarly situated and treated constituencies; and moreover, the Chapter 11 process contains added distribution safeguards such as cram down and best interests protection. Mere voting approval by the Chapter 11 debtor's creditors and shareholders cannot even begin to approximate this process for a fair distribution of the value of the released non-debtor's assets.

The equitable distribution contemplated by the Bankruptcy Code also requires a debtor to submit all assets and affairs to the jurisdiction of the federal bankruptcy court.\footnote{135} The baseline rule for bankruptcy

\footnote{133} In fact, one court, after collecting cases and distilling therefrom five factors important to approval of a non-debtor release, identified as "the single most important factor" that a "substantial majority of the creditors agree to such injunction, specifically, the impacted class, or classes, has 'overwhelmingly' voted to accept the proposed plan treatment." \textit{In re} Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 938, 935 (Bankr. W.D. Mo. 1994); \textit{see also} Monarch Life Ins. Co. v. Ropes & Gray, 65 F.3d 973, 980, 985 (1st Cir. 1995) (dicta noting \textit{Master Mortgage factors and bankruptcy court's reliance on creditors' "overwhelming" approval}); Menard-Sanford v. Mabey (\textit{In re} A.H. Robins Co.), 880 F.2d 694, 702 (4th Cir. 1989) (emphasizing the fact that "the Plan was overwhelmingly approved" by Dalkon Shield claimants); \textit{cf. In re} A.H. Robins Co., 880 F.2d 709, 744, 747 (4th Cir. 1989), aff'd 88 B.R. 755, 762 (E.D. Va. 1988) (relying on Dalkon Shield claimants' approval of Robins plan of reorganization in approving non-opt-out settlement of class action against non-debtors). \textit{But cf. In re} West Coast Video Enters., Inc., 174 B.R. 906, 911 (Bankr. E.D. Pa. 1994) (citing \textit{Master Mortgage factors} with approval, but adding that each individual creditor must consent to be bound by release). The \textit{Drexel} court even went so far as to emphasize the "fact that the Plan has been accepted overwhelmingly by all classes of Impaired Creditors" as "demonstrat[ing] the determination of Creditors and Equity Interest holders that the Plan is in their best interests and maximizes distributions available to them." \textit{In re} Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 769 (Bankr. S.D.N.Y. 1992). This, in spite of the fact that securities litigation creditors, subjected to non-debtor releases, were denied any vote on the plan of reorganization. \textit{See supra} notes 103-08 and accompanying text. Section 524(g) injunctions, which can include release of non-debtor asbestos claims, also incorporate this fallacious creditor voting requirement. \textit{See} 11 U.S.C. \textsection 524(g)(2)(B)(ii)(IV)(bb) (1994) (injunction permissible only if "a separate class or classes of the claimants whose claims are to be addressed ... is established and votes, by at least 75 percent of those voting, in favor of the plan").

\footnote{134} \textit{See supra} Part III.B.1-3.

\footnote{135} \textit{See} Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (discharge is available "to the honest but unfortunate debtor who surrenders for distribution the property which he owns \textit{at the time of bankruptcy}"); Theodore Eisenberg, \textit{Bankruptcy Law in Perspective}, 28 UCLA L. Rev. 953, 977 (1981) ("[A] bankruptcy discharge should not be available merely upon request. ... In theory at least, our law has never endorsed such a lenient rule. Debtors are always asked to sacrifice something, to pay what they reasonably can."); \textit{Nimmer, supra} note 113, at 1030 (noting that discharge "policy makes various assumptions," one of the "most important" being that the debtor "lacks a substantial ability to pay debts beyond what is contemplated in the bankruptcy case itself").
distributions is that the bankruptcy estate available for satisfaction of creditors’ claims consists of “all legal or equitable interests of the debtor in property as of the commencement of the case.”136 Through non-debtor releases, however, many non-debtors are released without making any contribution whatsoever toward satisfaction of the released claims.137 Even in those cases in which released non-debtors do make contributions in exchange for the release, the contribution, as discussed above, bears no necessary relationship to the non-debtor’s liability on the released claims. In fact, the non-debtor’s contribution has nothing at all to do with satisfying the obligations of the non-debtor; the contribution is to the Chapter 11 debtor, for the benefit of the creditors and shareholders of the Chapter 11 debtor, regardless of whether they have valid claims against the released non-debtor.138 More importantly, that contribution is not judged in terms of the non-debtor’s total resources available for repayment of debt, as is required by the Bankruptcy Code. Thus, released non-debtors can receive a discharge of indebtedness, while retaining substantial wealth.139

136. 11 U.S.C. § 541(a)(1). Individual debtors can exempt some property from this all-encompassing bankruptcy estate. See id. § 522. The Bankruptcy Code actually adopts two alternative means for measuring a debtor’s ability to repay creditors. The “liquidation” measure is tied to the debtor’s assets, and the “repayment plan” measure is based on a debtor’s future income-producing ability. See Eisenberg, supra note 135, at 977-78. The court can approve a repayment plan, however, only if it will yield creditors at least as much as a liquidation of the debtor’s assets. See 11 U.S.C. §§ 1129(a)(7), 1225(a)(4), 1325(a)(4).

In filing bankruptcy, a debtor also submits extensive disclosures regarding the debtor’s financial affairs and becomes subject to even more extensive inquiries through compulsory examination procedures. See, e.g., id. § 521(1), (4) (filing of schedules and surrender of records and property to trustee); OFFICIAL BANKRUPTCY FORMS, Forms 6, 7 (schedules and statement of financial affairs); 11 U.S.C. § 343 (examination of debtor at meeting of creditors); FED. R. BANKR. P. 2004 (court-ordered examinations). The bankruptcy filing also gives the bankruptcy trustee extensive avoiding powers that can enhance the bankruptcy estate for creditor distributions, for example, by undoing prebankruptcy fraudulent and preferential transfers. See, e.g., 11 U.S.C. §§ 547-548. The debtor is under a statutory duty to cooperate with the trustee in these and all other aspects of administration of the estate. See id. § 521(3). The bankruptcy discharge is closely tied to this process of the debtor submitting all assets and affairs to the jurisdiction of the court. See infra note 143 and accompanying text. In fact, the bankruptcy discharge originated in England in 1705 as a means of inducing cooperation from the debtor in this process. See generally Tabb, Discharge, supra note 128, at 333-39.

137. This was certainly the case with respect to the broad non-debtor releases approved in the Robins case. See supra note 124; see also Abel v. Shugrue (In re Ionosphere Clubs, Inc.), 184 B.R. 648, 655 (S.D.N.Y. 1995) (approving plan which released, inter alia, Eastern Airlines’ officers and directors “in connection with their actions taken prior to the effective date of the Plan” with no mention of any contribution by released non-debtors). In the Monarch Capital case, the First Circuit explained that release of non-debtors that make no contribution to the debtor’s reorganization may be necessary to protect essential contributing non-debtors from contribution and indemnification claims by the noncontributors. Monarch Life Ins. Co. v. Ropes & Gray, 65 F.3d 973, 980 (1st Cir. 1995), aff’d 173 B.R. 31, 44-45 (D. Mass. 1994) (construing plan releases as protecting noncontributing non-debtor because noncontributor threatened indemnification and contribution claims against contributing non-debtors). The necessity of non-debtors’ contributions is explored infra Part III.C.2.c.

138. See supra notes 62-69 and accompanying text.

139. The most striking illustration of this deviation comes from the Drexel case. The releases in that case benefited approximately 200 former Drexel employees, including Michael
From the perspective of the creditors of the released non-debtor, the discharge effected by a non-debtor release is accompanied by none of the indicia of an equitable distribution that are the sine qua non for a bankruptcy discharge. The corresponding improper benefit for the released non-debtor, of course, is discharge without a sufficient contribution toward repayment of debts.

b. The Non-Debtor’s Super Fresh Start

To the extent that a non-debtor release discharges the obligations of an individual, rather than those of an artificial legal entity, the proper scope of a bankruptcy discharge implicates more than creditor distribution concerns. Historically, the bankruptcy discharge originated as a device to aid creditors in collection of their debts, with the prospect of a discharge serving to induce cooperation by the debtor. Over time, though, the discharge also took on a debtor relief orientation, evolving into an instrument for the assistance of the “honest but unfortunate debtor”\textsuperscript{140} and taking on the “fresh start” feature so readily associated with modern discharge policy.\textsuperscript{141} Non-debtor releases as a discharge device serve none of the equitable distribution goals linked to a discharge, and they also corrupt the fresh start policy embodied in the discharge by permitting discharge of obligations well beyond the purview of a legitimate fresh start.

A bankruptcy discharge is not an absolute; creditors’ repayment rights do not always yield to the desire to give an individual a financial fresh start. There are two sides to the fresh start policy. The flip side

Milken. See supra note 6 and accompanying text. Milken’s release came in exchange for a $500 million contribution to the Drexel plan, and the remaining employees contributed an aggregate of $300 million. See Drexel Burnham Lambert Group, Inc. v. Claimants Identified on Schedule 1 (In re Drexel Burnham Lambert Group, Inc.), 995 F.2d 1138, 1143 (2d Cir. 1993). Despite these substantial contributions, Milken retained personal worth of approximately $125 million, as well as control of family assets held in the names of his wife and children, reportedly worth another $350 million. See Robert J. McCartney & Susan Schmidt, FDIC Fears of Leniency for Milken Brother Delay Accord, WASH. POST, Mar. 7, 1992, at C1; Pat Widdor, Accords Reached in Drexel Saga, CHI. TRIB., Mar. 10, 1992, at B1; cf. ZEV, supra note 5, at 71-72 (describing the $500 million of remaining personal and family wealth reported in the press as “an exceedingly low estimate, perhaps one-third of what it should be”). Most of the other settling employees protected by the non-debtor releases also emerged with extraordinary amounts of wealth intact. See Jill Dutt, Shepherd of Milken Pact Wields a Powerful Staff, NEWSDAY, Mar. 11, 1992, at 43. For example, Milken’s chief deputy, Peter Ackerman, was the next largest contributor at $80 million, yet he retained the bulk of his fortune, worth anywhere from $325 to $500 million. See Anthony Bianco & Sana Siwolop, The Drexel Debacle’s “Teflon Guy”: Peter Ackerman, Milken’s Mysterious Right-Hand Man, Will Emerge with About $500 Million, Bus. Wk., June 8, 1992, at 92; Billionaires (The Forbes Four Hundred), FORBES, Oct. 18, 1993, at 112, 248.

In the Robins case, members of the Robins family contributed $10 million in exchange for their non-debtor releases. Yet, they were simultaneously receiving nearly $400 million in distributions under the plan of reorganization. See supra note 124.

140. Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).
141. See generally Tabb, Discharge, supra note 128. By the time Congress considered comprehensive reform of the 1898 Act, debtor relief had achieved a status nearly on a par with that of orderly creditor distribution, as the two primary functions of bankruptcy law. See COMM’N REPORT, supra note 83, pt. I, at 71.
of relief for the honest debtor is no relief for the dishonest or fraudulent debtor, and the bankruptcy discharge has always been conditioned, to various degrees, upon the debtor's good faith. 142 Under the Bankruptcy Code, an individual debtor's discharge can be denied altogether for various types of dishonest or fraudulent behavior affecting proper administration of the bankruptcy case. 143 In addition, particular types of debts are excepted from an individual debtor's discharge, including several in which the debtor's conduct that gave rise to the obligation was fraudulent or malicious. 144

Non-debtor releases blunt the sharp edge of fresh start policy, because they do not contain discriminating exceptions that deny discharge of the obligations of the knavish non-debtor. In fact, non-debtor releases have been used to grant many individuals discharge from debts that could not, or at least arguably could not, be discharged through an actual bankruptcy filing by the non-debtor. For example, in the Robins case, the non-debtor releases left Dalkon Shield claimants with no right to seek compensatory or punitive damages from any individual, including various officers, directors, employees, and attorneys of Robins alleged to have personally participated in a scheme to defraud the public concerning the dangers of the Dalkon Shield. 145 The non-debtor releases lifted from these individuals the prospect of staggering compensatory and punitive damages awards and the prospect that such awards might well haunt them for the rest of their lives as nondischargeable debts. 146 The same can be said of the securities fraud claims against Michael Milken and other former Drexel employees that were discharged through the Drexel non-debtor releases. 147 Thus, the objection that plan releases give non-

142. See Nimmer, supra note 113, at 1030 (noting that discharge "policy makes various assumptions about the individual's behavior... most important[ly]... that the debtor dealt fairly with creditors"). See generally Tabb, Discharge, supra note 128. In fact, the first English discharge statute not only denied "fraudulent bankrupts" a discharge, but also made conviction for same punishable by death. See id. at 336-37.


144. See, e.g., id. § 523(a)(2) (debt for benefit obtained through misrepresentation); id. § 523(a)(4) (debt for embezzlement, larceny, or fraud or defalcation while acting in a fiduciary capacity); id. § 523(a)(6) (debt for willful and malicious injury); id. § 523(a)(9) (debt for personal injury caused by driving intoxicated); id. § 523(a)(13) (debt for payment of criminal restitution order).

145. See supra notes 8-14 and accompanying text. In fact, a U.S. district judge refused to quash a subpoena issued by a grand jury impaneled in Kansas, on the ground "that there was substantial evidence that 'Robins and its employees and officers participated in the commission of crimes and fraud during the promotion, marketing and sale of the Dalkon Shield, and used its attorneys to perpetuate and cover-up [this conduct] through the commission of frauds on the court, obstruction of justice, and perjury.'" Sobol, supra note 10, at 220 (quoting from district court order affirmed by Company X v. United States (In re Grand Jury Proceedings), 857 F.2d 710 (10th Cir. 1988)).

146. For a recent discussion of the division in the courts as to the dischargeability of punitive damages awards, see Nina Lempert, Note, Punitive Damages—The Dischargeability Debate Continues, 11 Bankr. Dev. J. 707 (1995).

147. The nature and extent of the fraudulent activities of Milken and his Drexel compatriots is carefully analyzed in Zey, supra note 5. These activities resulted in Drexel pleading guilty to
debtors the benefits of a bankruptcy discharge without the burdens of a bankruptcy filing, in some respects, understates the extent of the abuse; in many cases, releases give non-debtors a discharge that they could not obtain through a bankruptcy filing.\textsuperscript{148}

When one goes beyond a simplistic incantation of the shibboleth "creditor equality," it becomes obvious that non-debtor releases do not advance accepted notions of creditor equality and, in many respects, actually disturb and distort the Bankruptcy Code's intricate design for equitable treatment of creditors. This is the case whether one approaches creditor distribution issues from the standpoint of creditors of the Chapter 11 debtor or those of the released non-debtor. Non-debtor releases permit redistributions of value that could not otherwise prevail. What non-debtor releases take from creditors holding valuable non-debtor claims, they give to (1) the released non-debtors and their other creditors, and/or (2) creditors and shareholders of the Chapter 11 debtor without valuable non-debtor rights. These redistributions must be validated on some basis other than that of creditor equality, which leaves the bankruptcy policy of equal dignity—Chapter 11 debtor rehabilitation.

\textit{C. Debtor Rehabilitation}

The debtor rehabilitation arguments for non-debtor releases are of two distinct types. One is a discharge-related argument, misleadingly characterized as protecting the debtor's "fresh start." This argument, though, completely ignores existing Bankruptcy Code provisions already designed to address the precise concerns raised by the purported solicitude for the debtor's fresh start. In reality, the fresh start argument seems to be yet another attempt to legitimize non-debtor releases' redistributional effects.

\footnotesize{\textsuperscript{148} By filing under Chapter 13 of the Bankruptcy Code, a debtor can obtain a discharge of some types of debts that would be nondischargeable in a Chapter 7 liquidation. \textit{Compare} 11 U.S.C. § 523(a), \textit{with id.} § 1328(a). Access to Chapter 13, though, is limited to individuals with regular income whose debts do not exceed modest statutory maximums. \textit{See id.} § 109(e). In addition, the Chapter 13 debtor must be willing to devote all of his/her disposable income for a three-year period to repayment of debts, \textit{see id.} § 1325(b), and give creditors at least as much as they would receive in a Chapter 7 liquidation, \textit{see id.} § 1325(a)(4).}
The more substantial debtor rehabilitation concern is the one underlying the very existence of Chapter 11—preservation of an operating business otherwise destined for piecemeal liquidation. In many cases, however, non-debtor releases do not save the debtor's business, and the reorganization policy is simply another smoke screen for non-debtor releases' redistributive consequences. Because non-debtor releases can bring the reorganized debtor various benefits at no cost, any effort to restrict the practice to the rare non-debtor release actually necessary to reorganization is doomed to failure. In any event, ad hoc authority to approve releases necessary to reorganization places courts in a difficult policy-sifting role inconsistent with their conventional province in reorganization cases.

1. Discharge and the Debtor's "Fresh Start"

The initial debtor rehabilitation argument for non-debtor releases grows out of the fact that a creditor's non-debtor action may give rise to a corresponding contribution or indemnification claim by the non-debtor against the debtor. This tripartite or triangular claims relationship—where a creditor asserts a claim against both the debtor and a non-debtor, which produces a claim by the non-debtor against the debtor—is said to undermine the debtor's "fresh start" that flows from discharge of the creditor's claim against the debtor. So, the argument goes, notwithstanding discharge of the creditor's claim against the debtor on confirmation of the debtor's plan of reorganization, the creditor's claim still comes back to haunt the debtor via the creditor's non-debtor action and the resulting contribution/indemnification claim against the debtor.\(^\text{149}\)

\[\text{149. The tripartite claims relationship can be represented graphically as follows:} \]

\[\text{Non-Debtor} \rightarrow \text{Debtor} \quad \text{Contribution/Indemnification Claim} \]

\[\text{non-debtor action} \quad \text{bankruptcy claim} \quad \text{Creditor} \]

\[\text{150. See 11 U.S.C. § 1141(d)(1).} \]

\[\text{151. See, e.g., Abel v. Shugrue (In re Ionosphere Clubs, Inc.), 184 B.R. 648, 655 (S.D.N.Y. 1995) (stating that non-debtor "injuries were integral to a final resolution of claims and were necessary to give finality to the Plan"); Monarch Life Ins. Co. v. Ropes & Gray (In re Monarch Capital Corp.), 173 B.R. 31, 44 n.5 (D. Mass. 1994) (res judicata case explaining bankruptcy court's rationale in approving non-debtor releases as "intended to achieve complete repose on all matters related to the various claims"); aff'd on other grounds, 65 F.3d 973 (1st Cir. 1995); SEC v. Drexel Burnham Lambert, Inc. (In re Drexel Burnham Lambert Group, Inc.), 130 B.R. 910, 928 (S.D.N.Y. 1991) ("[T]he releases [give] protection of the Debtors' estates from piecemeal dismemberment through claims over and other indemnity claims."); aff'd, 960 F.2d 285 (2d Cir. 1992); In re A.H. Robins Co., 88 B.R. 742, 751, 753 (E.D. Va. 1988) (reasoning that "the releases and injunction ... provide ... a 'fresh start' for the Debtor" and "ensure ... rehabilitation and reorganization of Robins, free from direct and indirect involvement in further Dalkon Shield litigation"); aff'd sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d \]
This fresh start argument is initially problematic because it is somewhat misleading to speak of the Chapter 11 discharge as giving a corporation a "fresh start."\(^{152}\) The Bankruptcy Code's fresh start policy for the "honest but unfortunate debtor"\(^{153}\) is embodied in the discharge provisions of Chapters 7 and 13, which extinguish the debts of an individual debtor to the extent they are not fully satisfied by bankruptcy distributions.\(^{154}\) A corporation that successfully reorganizes through Chapter 11 proceedings also receives a discharge of all debts not fully satisfied by the plan of reorganization.\(^{155}\) The existence of a corporate discharge in Chapter 11, then, is a tempting invitation to impute to Congress a desire to extend the fresh start policy to corporations. A corporation, though, is a fictional legal entity and needs no fresh start in the same sense as does an individual.\(^{156}\) Individuals

\[^{694, 701, 702}\] (4th Cir. 1989) (stating that "a suit against any of the parties [released] would affect the bankruptcy reorganization in one way or another such as by way of indemnity or contribution" and "entire reorganization hinges on the debtor being free from indirect claims such as suits against parties who would have indemnity or contribution claims against the debtor"); \[^{In re Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994) (promulgating multifactor test for approving non-debtor releases, with one factor being "an identity of interest between the debtor and the third party, usually an indemnity relationship, such that a suit against the non-debtor is, in essence, a suit against the debtor or will deplete assets of the estate"); In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 753, 754, 773 n.12 (Bankr. S.D.N.Y. 1992) (finding that without non-debtor releases, there will be "[p]iecemeal dismemberment of estate assets... from an avalanche of suits against officers, directors, employees, agents, and others related to Drexel" and "great risk of successful indemnity Claims, of liability being imputed to the Debtors from the liability established against [released non-debtors] and of Claims over and for contribution being augmented, established and liquidated against the Debtors" and "threat of disruption or dismemberment of these Chapter 11 Estates through back door litigation against parties having claims over or indemnity claims against these Debtors"); "injunction and release provisions preserve our judicial and social fabric" and "society, as a whole, benefits from the "fresh start" provisions of the Code"); cf. \[^{In re A.H. Robins Co., 131 B.R. 292, 298 (E.D. Va. 1991) (construing scope of releases and explaining that without non-debtor releases, "[o]nce may very easily assume that the propensity on the part of many to litigate would result in yet further Shield litigation brought by the [non-debtors] seeking in one form or another indemnification or contribution" and "such risk is not to be sanctioned"), rev'd on other grounds sub nom. Dalkon Shield Claimants Trust v. Reiser (In re A.H. Robins Co.), 972 F.2d 77 (4th Cir. 1992); Dalkon Shield Claimants' Comm. v. Aetna Cas. & Sur. Co. (In re A.H. Robins Co.), 85 B.R. 373, 381-82 (E.D. Va. 1988) (certifying mandatory non-opt-out class action against non-debtors based on, inter alia, fact that non-debtors would draw debtor into such litigation), aff'd, 880 F.2d 709 (4th Cir. 1989); see also Feldstein, Third-Party Releases, supra note 20, at 27, 45 ("the binding effect of a plan may be compromised if claims against the debtor can be recast as claims against the individuals who act for the debtor"); "a release may be necessary in order to effectively implement a plan of reorganization and prevent 'back door' actions which are in reality actions against the debtor").

\(^{152}\) Although individuals are eligible to reorganize their affairs and receive a discharge from indebtedness via Chapter 11, the fresh start argument for non-debtor releases has been invoked in the context of corporate Chapter 11 cases. Therefore, the textual discussion is limited to the corporate discharge in Chapter 11. Nonetheless, the same analysis reveals that non-debtor releases would not advance the fresh start function of the discharge for an individual Chapter 11 debtor.

\(^{153}\) See \[^{Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).}

\(^{154}\) See \[^{11 U.S.C. §§ 727, 1328.}

\(^{155}\) See \[^{id. § 1141(d)(1).}

\(^{156}\) See \[^{Comm'n Report, supra note 83, pt. I, at 74; Nimmer, supra note 113, at 1027-32; Tabb, Discharge, supra note 128, at 363; Warren, Policymaking, supra note 24, at 341.\]
who own a corporation as shareholders already enjoy the liability shield flowing from the concept that the fictional corporate person is the entity liable for corporate debts. A corporation can fully discharge its debts without bankruptcy, by merely dissolving the fictional corporate person.\textsuperscript{157} Thus, the Chapter 11 corporate discharge rests on grounds entirely different from those underlying an individual debtor's discharge.

The Chapter 11 corporate discharge merely gives effect to the voting and treatment provisions of Chapter 11 discussed above.\textsuperscript{158} Chapter 11's class voting and treatment structure contemplates a division of the value of the debtor's business that will give equal pro rata treatment to similarly situated claimants and bind all parties, notwithstanding the dissent of particular claimants. The Chapter 11 discharge is the means by which the plan binds dissenters to the pro rata treatment provided by the plan.\textsuperscript{159} Thus, the Chapter 11 discharge is merely a logical extension of bankruptcy's creditor equality principles.\textsuperscript{160} So, to the extent the Chapter 11 discharge is just a restatement of the Bankruptcy Code's creditor equality policy, attaching the words "fresh start" to the Chapter 11 discharge provides no independent justification for non-debtor releases and cannot support non-debtor releases any more than the creditor equality policy itself.

The specious nature of the general policy argument is, once again, doubly reinforced by looking to the specific provisions of the Bankruptcy Code. The Code is fully equipped to manage any problems presented by the tripartite claims relationship surrounding non-debtor actions. Contrary to the suggestions of the "fresh start" argument, the non-debtor's contribution/indemnification claim does not simply bypass the bankruptcy proceedings and escape the debtor's discharge. The reorganization proceedings deal with any "claim" against the debtor, broadly defined to include even contingent, unliquidated, un-
matured, and disputed payment rights.\(^{161}\) This approach to bankruptcy claims is broad enough to encompass the contingent contribution/indemnification rights of a non-debtor that would flow from a creditor's non-debtor action.\(^{162}\) Consequently, the non-debtor would be stayed from pursuing the debtor for contribution/indemnification outside the bankruptcy court.\(^{163}\) Moreover, confirmation of the debtor's plan of reorganization would discharge not only the creditor's direct "claim" against the debtor, but also the non-debtor's contingent contribution/indemnification "claim."\(^{164}\)


162. See Donald R. Korobkin, "Killing the Husband": Disallowing Contingent Claims for Contribution or Indemnity in Bankruptcy, 11 CARDOZO L. REV. 735, 748 (1990) (hereinafter Korobkin, Contribution or Indemnity). The primary authority to the contrary is the Third Circuit's much-maligned opinion in Avello & Bienes v. M. Fresnville Co. (In re M. Fresnville Co.), 744 F.2d 332 (1984), holding that a non-debtor has no contribution/indemnification "claim" within the meaning of the Bankruptcy Code until the non-debtor has a ripe cause of action that could be pursued in state court. This approach to bankruptcy "claims," though, is fundamentally at odds with the language and purposes of the Bankruptcy Code's broad definition of the "claims" that are swept into a debtor's bankruptcy proceedings. Commentators have roundly condemned the Fresnville case. E.g., Ralph R. Mabey & Annette W. Jarvis, In re Fresnville: A Critique by the National Bankruptcy Conference's Committee on Claims and Distributions, 42 BUS. LAW. 697, 697 n. (1987) (stating that the "National Bankruptcy Conference is on record as believing the Fresnville decision wrongly decided"); see also JACKSON, LOGIC AND LIMITS, supra note 157, at 172-74. Courts outside the Third Circuit have almost universally rejected Fresnville. See cases cited infra notes 163-64.


The contribution/indemnification argument is really old wine in a new bottle—advanced in one of the earliest attempts to obtain a non-debtor release and rejected by the Second Circuit on roughly the same reasoning as that set forth in the text. See In re Nine N. Church St., Inc., 82 F.2d 186, 189 (2d Cir. 1936) (noting that "relief of a guarantor [is not] essential to the debtor's reorganization [because] after [guarantor] pays the objecting [creditor,] its claim to indemnity from the debtor would be subject to reduction" in the debtor's reorganization proceedings); accord Landsing Diversified Properties-II v. First Nat'l Bank & Trust Co. (In re Western Real Estate Fund, Inc.), 922 F.2d 592, 602 (10th Cir. 1990) ("Not only does such a permanent injunction improperly insulate non-debtors... it does so without any countervailing justification of debtor protection—as... the discharge injunction provided for in section 524(a) already frees
Because they produce a bankruptcy "claim" that can be fully administered in the debtor's reorganization proceedings, the non-debtor's contribution/indemnification rights implicate creditor distribution concerns, not debtor rehabilitation. With respect to equitable creditor distribution, the non-debtor's contribution/indemnification claim introduces some complexity, because the non-debtor's contribution/indemnification claim presents the potential for double counting the creditor's direct claim against the debtor. As far as the debtor is concerned, the non-debtor's contribution/indemnification claim is duplicative of the creditor's direct claim. To allow both claims, therefore, would inflate the magnitude of the debtor's liabilities, and permitting both the creditor and the non-debtor to receive bankruptcy distributions would give this "one" claim a double distribution.\textsuperscript{165}

Non-debtor releases, though, are not necessary to solve the double-counting problem created by the triangular claims relationship, because the Bankruptcy Code already contains a solution. Furthermore, the Bankruptcy Code solution presupposes that the creditor will retain its right to seek full payment from the non-debtor. The Bankruptcy Code solution disallows the non-debtor's contingent contribution/indemnification claim.\textsuperscript{166} In the place of its disallowed con-

the debtor from potential derivative claims, such as indemnification or subrogation, that might arise from the creditor's post-confirmation attempts to recover the discharged debt from others.\textsuperscript{5} \textit{modified on other grounds sub nom.} Abel v. West, 932 F.2d 898 (10th Cir. 1991). Other commentators have noted the availability of the discharge provisions to deal with non-debtors' contingent contribution/indemnification claims. \textit{E.g.}, Starr, \textit{supra} note 44, at 495-96; Boyle, \textit{supra} note 44, at 440-41.

\textsuperscript{165} See Korobkin, \textit{Contribution or Indemnity}, \textit{supra} note 162, at 750.

\textsuperscript{166} Section 502(e)(1)(B) of the Bankruptcy Code provides that "the court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor...to the extent that...such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim." 11 U.S.C. § 502(e)(1)(B). This provision applies to contribution/indemnification rights arising from any type of co-liability, including both contract and tort. \textit{See, e.g.}, Juniper Dev. Group v. Kahn (\textit{In re} Hemingway Transp., Inc.), 993 F.2d 915, 923 (1st Cir. 1993). \textit{See generally} Korobkin, \textit{Contribution or Indemnity}, \textit{supra} note 162, at 758-59. "Reimbursement," within the meaning of § 502(e)(1)(B), encompasses the concept of indemnity. \textit{See, e.g.}, Syntex Corp. v. Charter Co. (\textit{In re} Charter Co.), 862 F.2d 1500, 1502 n.3 (11th Cir. 1989); \textit{In re} Pacor, Inc., 110 B.R. 686, 690-91 (E.D. Pa. 1990); \textit{In re} Pettibone Corp., 110 B.R. 837, 848 (Bankr. N.D. Ill. 1990); \textit{In re} Wedtech Corp., 85 B.R. 285, 289 (Bankr. S.D.N.Y. 1988); \textit{cf.} \textit{Restatement of Security} § 104 note, at 275 (1941) ("terms 'indemnity' and 'reimbursement' are frequently used as synonymous"). The non-debtor's contribution/indemnification claim is contingent until the non-debtor pays the creditor, thereby fixing the right to payment from the debtor. \textit{See 4 Collier (15th ed.), supra note 40, ¶ 502.08(d)[d], at 502-69; 124 Cong. Rec. 32,597 (1978) (statement of Rep. Edwards, sponsor); id. at 33,997 (statement of Sen. DeConcini, sponsor); cf. \textit{Restatement of Restitution} §§ 77, 82 (1937) (right to indemnity or contribution arises when the co-obligor discharges the obligation). By disallowing the non-debtor's contribution/indemnification claim to the extent the non-debtor has not yet paid the creditor, this "provision prevents competition between a creditor and [the non-debtor] for the limited proceeds in the estate." H.R. Rep. No. 95-595, at 354, \textit{reprinted in} 1978 U.S.C.C.A.N. at 6310; \textit{see also} S. Rep. No. 95-989, at 65, \textit{reprinted in} 1978 U.S.C.C.A.N. at 5851. Other commentators have noted the availability of the discharge provisions to deal with non-debtors' contingent contribution/indemnification claims. \textit{E.g.}, Mark S. Scarberry et al., \textit{Business Reorganization in Bankruptcy: Cases and Materials} 970 n.5 (1996); Starr, \textit{supra} note 44, at 495.

\textsuperscript{5} For a discussion of the "modified on other grounds sub nom." phrase, see supra note 5.
tribution/indemnification claim, the Bankruptcy Code affords the non-debtor subrogation rights.\textsuperscript{167} To the extent, then, that the non-debtor pays the creditor, the non-debtor steps into the shoes of the creditor and may assert its right of contribution/indemnification against the debtor through subrogation to the creditor’s claim against the debtor.

There may be certain elements of a non-debtor’s indemnification claim that do not duplicate the creditor’s claim against the debtor. These additional claim amounts, therefore, will fall outside the scope of the Bankruptcy Code’s disallowance/subrogation provisions and, as a result, will reduce distributions to other creditors.\textsuperscript{168} Nothing in general bankruptcy policy, however, sanctions categorical obliteration of otherwise valid claims in order to increase distributions to other creditors and shareholders. In fact, our bankruptcy law is based on a principal distributive standard “that any claim enforceable externally is enforceable in the bankruptcy process to the same extent and with the same priority status.”\textsuperscript{169}


\textsuperscript{168} See, e.g., In re Lull Corp., 162 B.R. 234, 239 (Bankr. D. Minn. 1993) (holding that a claim for non-debtor’s administrative and legal costs not disallowed because no co-liability as to these costs); In re Early & Daniel Indus., Inc., 104 B.R. 963, 968 (Bankr. S.D. Ind. 1989) (same); see also Korobkin, Contribution or Indemnity, supra note 162, at 758-68 (discussing indemnity claims that implicate no co-liability).

\textsuperscript{169} COMM’N REPORT, supra note 83, pt. I, at 77. To be sure, the Bankruptcy Code contains departures from this principle. Unlike non-debtor releases, however, these are departures expressly approved by Congress, based on countervailing policy considerations. See Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 161 (1946) (“What claims of creditors are valid and subsisting obligations against the bankrupt . . . is a question which, in the absence of overriding federal law, is to be determined by reference to state law.” (emphasis added)); Kuehner v. Irving Trust Co., 299 U.S. 445, 453-56 (1937) (upholding the validity of congressional limitation on landlords’ damages claims in reorganization, because “[i]n framing the reorganization statute Congress obviously attempted to award landlords an equitable share in the debtor’s assets as, in justice, it was bound to do since the purpose was to discharge the debtor from liability”); COMM’N REPORT, supra note 83, pt. I, at 76-79 (discussing federal policies that warrant deviation from nonbankruptcy distributional rules); Nimmer, supra note 113, at 1014-15 & n.5, 1024-26 (same); Warren, Policymaking, supra note 24, at 352-53 (same).
Courts that accept the contribution/indemnification argument for non-debtor releases also express disdain for the administrative burden and expense of resolving the validity of non-debtors’ contribution/indemnification claims—expenses that further diminish the recoveries of other creditors.\footnote{E.g., Monarch Life Ins. Co. v. Ropes & Gray (In re Monarch Capital Corp.), 173 B.R. 31, 41 (D. Mass. 1994) ("[I]njunction was necessary [inter alia] to prevent costly litigation, and to achieve the maximum available pay-out to the creditors."). aff’d on other grounds, 65 F.3d 973 (1st Cir. 1995); In re A.H. Robins Co., 131 B.R. 292, 298 (E.D. Va. 1991), rev’d on other grounds sub nom. Dalkon Shield Claimants Trust v. Reiser (In re A.H. Robins Co.), 972 F.2d 77 (4th Cir. 1992); In re A.H. Robins Co., 88 B.R. 742, 753 (E.D. Va. 1988) (stating that non-debtor releases are proper “to ensure [inter alia] efficient administration of Robins’ estate [and] minimization of expenditures and transaction costs . . . for protracted litigation of questionable value against third parties”), aff’d sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d 694 (4th Cir. 1989); In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 753 (Bankr. S.D.N.Y. 1992) ("[I]n the absence of the Release and Injunction Provisions . . . reductions in distributions of property of the estates, and increased costs to creditors will result from an avalanche of suits against officers, directors, employees, agents, and others related to Drexel.").} This concern, however, is a generic one, and one that finds expression in a general bankruptcy policy “that the process for recognizing the validity of claims and determining their amount should not be so costly, inconvenient, arcane, or slow as effectively to impair achievement of the substantive goals” of “fair and equitable treatment of creditors’ claims.”\footnote{COMM’N REPORT, supra note 85, pt. I, at 79.} That policy certainly justifies bankruptcy law’s more expeditious and efficient procedures for resolution of disputed claims.\footnote{See Jackson, Logic and Limits, supra note 157, at 44-45, 196 (noting that less costly procedures are justified if they produce no systematic bias in value of claims); LoPucki, supra note 157, at 347-52 (explaining advantageous procedural efficiencies of claims resolution in bankruptcy over nonbankruptcy litigation and the ability of the bankruptcy system to resolve disputed claims without jeopardizing the viability of the debtor’s business operations); cf. Robert M. Lawless, Realigning the Theory and Practice of Notice in Bankruptcy Cases, 29 Wake Forest L. Rev. 1215 (1994) [hereinafter Lawless, Notice in Bankruptcy] (exploring procedural due process implications of bankruptcy’s dispute resolution procedures).} Taking this general concern to the level of categorical elimination of certain types of disputed claims, though, requires an additional policy judgment that certain creditors are more worthy of payment than others—a choice that violates basic creditor equality principles and that should be reserved for Congress.\footnote{See infra Part III.C.2.d. Under the 1898 Act, contingent or unliquidated claims, such as tort claims, generally were deemed too uncertain and difficult of resolution to permit such claims to participate in any bankruptcy distribution. Because such claims had no right to receive a distribution, though, they passed through the bankruptcy proceedings unaffected by the bankruptcy discharge. See generally Korobkin, Contribution or Indemnity, supra note 162, at 744-46. Using the administrative convenience rationale to discharge claims that are not afforded equitable distribution rights, therefore, is a radical step that departs from the traditional notion that the discharge cannot reach such claims. See supra notes 129-30 and accompanying text.} For example, the concern over the administrative burden of indemnification and contribution claims could be addressed just as easily by complete elimination of non-debtors’ contribution/indemnification claims, while leaving creditors’ non-debtor rights intact. The fact that a
choice must be made between taking away creditors' rights to pursue non-debtors, on the one hand, and taking away non-debtors' rights against the debtor, on the other, punctuates the essential distributional policy judgments implicit in judges' approval of non-debtor releases.

What is cast as concern about the tripartite claims relationship interfering with the debtor's "fresh start," proves to be nothing more than dissatisfaction with the distributional consequences of creditors' non-debtor actions. The only "fresh start" relevant for a corporation is the ability of the Chapter 11 reorganization provisions to save an operating business from death through liquidation. 175

2. In Pursuit of the Elusive Reorganization Policy

The fresh start and creditor equality rationales for non-debtor releases are nothing more than shallow makeweights that cannot overcome the numerous principles and provisions of the Bankruptcy Code that compel repudiation of non-debtor releases. Ultimately, non-debtor releases must stand or fall depending upon the strength of their primary raison d'être: promoting successful reorganization of the Chapter 11 debtor. Regardless of the merits of other statutory and policy arguments, the paramount concern of courts that approve non-debtor releases is a stated policy favoring reorganization. 176

Indeed, at 758-83. Interestingly, both the district court and the bankruptcy court in the Drexel case adopted this broad interpretation of § 502(e)(1)(B). See Sorenson v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Group, Inc.), 146 B.R. 92, 94-97 (S.D.N.Y. 1992) (disallowing non-debtor's contingent claim for indemnification of defense costs); In re Drexel Burnham Lambert Group, Inc., 148 B.R. 982, 988-91 (Bankr. S.D.N.Y. 1992) (same); In re Drexel Burnham Lambert Group, Inc., 146 B.R. 98, 102-05 (Bankr. S.D.N.Y. 1992) (concluding that joint-tortfeasor contribution claim was contingent and disallowable because debtor's proportionate fault had not yet been fixed by a judicial determination, despite the joint tortfeasor's settlement with creditors). Of course, this is not at all surprising, given those courts' obvious affinity for the expedient solution. Yet, such broad-based disallowance of non-debtors' contribution/indemnification claims clearly undercuts those courts' position that non-debtor releases were necessary to protect the debtor from such claims. See supra note 151.

175. Cf. Warren, Bankruptcy Policy, supra note 157, at 785 (noting that the corporation's functional discharge outside bankruptcy only comes upon death of the corporation through dissolution).

the standard for approving a non-debtor release in any particular case, to the extent that a standard has emerged, is expressly tied to the significance of the release in furthering the debtor's reorganization.\textsuperscript{177} Overlooking the numerous statutory and theoretical deficiencies of non-debtor releases in order to assure a debtor's reorganization has a very tempting visceral appeal, but it is a dangerous practice that should not be permitted.

Initially, as a policy matter, there is substantial disagreement about whether pursuit of reorganization for the sake of reorganization is ever an appropriate independent goal of the Chapter 11 process. Even if one accepts reorganization—and the secondary benefits Congress envisioned from successful reorganization—as an acceptable policy objective, vindicating that policy through non-debtor releases presents insuperable practical and instrumental problems. Many factors contribute to a substantial risk that, in most cases, non-debtor releases do not, in fact, promote successful reorganization. The most prominent cases, \textit{Drexel and Robins}, illustrate both an inherent ambiguity in the concept of a successful reorganization and intractable screening problems that frustrate any principled method for approval of non-debtor releases. Quite apart from these practical problems is a more fundamental difficulty. Implicit in the idea that a non-debtor release is appropriate where necessary to the debtor's successful reorganization is the assumption that the reorganization policy is supreme, and in furtherance thereof, a bankruptcy judge can unilaterally override legitimate policies embodied in nonbankruptcy law that would place liability upon the released non-debtors. Such a notion is hard to square with the inherent limitations of the judicial process and Congress' primary role in making such policy determinations in the bankruptcy context.

\begin{itemize}
\item \textbf{a. Efficiency and the Reorganization Policy}

The initial issue raised by the use of reorganization policy to support non-debtor releases is a theoretical one: Does the reorganization policy alone provide a valid basis on which to premise any bankruptcy doctrine? For over a decade, academics have vigorously debated the appropriate contours of sound bankruptcy policy, with the primary focal point being the "creditors' bargain model."\textsuperscript{178} The creditors' bar-

\begin{footnotes}
\item[177] See infra notes 226-27 and accompanying text.
\item[178] The creditors' bargain model, conceptualized by Thomas Jackson, first appeared in the seminal article, Thomas H. Jackson, Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain, 91 YALE L.J. 857 (1982) [hereinafter Jackson, Creditors' Bargain]. Jackson's most comprehensive work on bankruptcy policy and the creditors' bargain is JACKSON, LOGIC AND
\end{footnotes}
gain model starts from the premise that bankruptcy is a debt collection device,\textsuperscript{179} but most importantly, a debt collection device that exists against a backdrop of individual, uncoordinated collection remedies, primarily provided by state law. Given the existence of these state collection laws, the creditors' bargain theory explains the need for a bankruptcy overlay as responding to a particular deficiency in the state collection system: a "common pool"\textsuperscript{180} or "collective action"\textsuperscript{181} problem. The common pool problem arises when the debtor's resources appear insufficient to satisfy the claims of all creditors, a typical benchmark of insolvency. In this situation, creditors as a whole may be best served by a moratorium on individual collection efforts.\textsuperscript{182}

For example, the debtor's assets may be worth more if the debtor survives as an operating business than if the debtor were dismantled through piecemeal liquidation sales conducted at the instance of various execution creditors. In such a case, the creditor body could reap a larger aggregate recovery by cooperating to forego their individual collection rights in order to preserve the debtor's going concern value and apply it toward payment on their debts.\textsuperscript{183} Yet, the existence of numerous creditors and insufficient assets to fully satisfy them all presents a classic "prisoner's dilemma" in which the interests of individual creditors clash with the collective creditor good. Notwithstanding the collective advantages of cooperation, any particular creditor of this insolvent debtor will see advantages in going forward with individual collection efforts in an attempt to obtain payment in full.\textsuperscript{184}


179. See \textit{Jackson, Logic and Limits}, supra note 157, at 3, 7; \textit{Jackson, Creditors' Bargain, supra} note 178, at 860 n.18. The congressional commission that shaped the current Bankruptcy Code described the debt collection aspects of bankruptcy law as the "primary function of the bankruptcy system." Comm'n Report, supra note 83, pt. I, at 71.

180. See \textit{Jackson, Logic and Limits, supra} note 157, at 10-11; \textit{Jackson, Creditors' Bargain, supra} note 178, at 864 n.34.

181. See \textit{Jackson & Scott, Bankruptcy Sharing, supra} note 159, at 164 n.17.

182. See \textit{Jackson, Logic and Limits, supra} note 157, at 8-11.

183. See \textit{id.} at 14; \textit{Jackson, Creditors' Bargain, supra} note 178, at 864.

184. See \textit{Jackson, Logic and Limits, supra} note 157, at 10-12; \textit{Jackson, Creditors' Bargain, supra} note 178, at 864.
Therefore, leaving creditors to their own devices in a world of individual collection remedies produces an inherently unstable situation. There is a risk of a destructive "race to the courthouse" that could destroy the debtor's going concern value, thus yielding lower aggregate creditor recoveries.\textsuperscript{185}

The creditor's bargain model posits bankruptcy law's singular, unique function as a solution to the common pool problem, with the ultimate objective of bankruptcy law being maximization of creditor recoveries. Theoretically, the creditors themselves would agree to such a solution ex ante, if an actual bargain among the creditors were feasible—the so-called creditors' bargain.\textsuperscript{186} In the context of a Chapter 11 reorganization proceeding, the automatic stay preserves the debtor's going concern value by preventing holdouts from taking precipitous actions that could dismantle the debtor,\textsuperscript{187} and the plan of reorganization provides a mechanism by which the debtor's going concern value can be distributed to the creditors.\textsuperscript{188}

One of the most firmly held implications of the creditors' bargain concerns the appropriate distribution of the debtor's reorganization value among creditors and shareholders. The creditors' bargain contemplates little independent role for bankruptcy law with respect to this distributional question. Bankruptcy law itself should not create any new, independent, substantive rights that parties do not enjoy

\textsuperscript{185} In a fuller exploration of the dynamics of the state collection process, Lynn LoPucki demonstrates that the state-law system can also produce the converse problem—continuation of a debtor whose liquidation value exceeds its going concern value. In fact, Professor LoPucki concludes that because state collection laws operate without any inquiry into the debtor's viability, they will tend to continue or terminate the debtor's operations without regard for which of these two alternatives is appropriate; and bankruptcy is superior to state law in responding to both the problem of termination of a viable entity and that of continuation of a nonviable one. See LoPucki, \textit{supra} note 157, at 325-33, 335-38, 343-48, 357-59, 361-62.

\textsuperscript{186} \textit{See} \textit{Jackson, Logic and Limits, supra} note 157, at 16-17 & n.22; Jackson, \textit{Creditors' Bargain, supra} note 178, at 860. Creditors' bargain theory contemplates larger creditor recoveries coming from many potential advantages that a compulsory, collective bankruptcy proceeding may hold over individual state collection remedies. Bankruptcy can produce a larger aggregate asset pool for repayment of creditors, not only by preserving a debtor's going concern value, but also through more effective liquidation sales. See \textit{Jackson, Logic and Limits, supra} note 157, at 14-15; Jackson, \textit{Creditors' Bargain, supra} note 178, at 864; see also LoPucki, \textit{supra} note 157, at 316-21 (identifying several advantages of bankruptcy sales procedures over those of state collection law). Bankruptcy also may reduce collection costs by eliminating the need for duplicative and wasteful individual monitoring and collection activities. See \textit{Jackson, Logic and Limits, supra} note 157, at 16; Jackson, \textit{Creditors' Bargain, supra} note 178, at 861-63, 866; see also LoPucki, \textit{supra} note 157, at 347-51. In addition, bankruptcy can give creditors a more certain recovery as compared with creditors' expected returns from the risky state-law collection race—an item holding independent value for the risk averse creditor. See \textit{Jackson, Logic and Limits, supra} note 157, at 15; Jackson, \textit{Creditors' Bargain, supra} note 178, at 861-64. In spite of these potential advantages of a collective proceeding, an actual bargain among creditors is often infeasible because of the strategic and practical complications of multiparty negotiations—thus, the need for a compulsory federal bankruptcy proceeding. See \textit{Jackson, Logic and Limits, supra} note 157, at 17-19; Jackson, \textit{Creditors' Bargain, supra} note 178, at 864-67.


\textsuperscript{188} \textit{See id.} §§ 1121-1129.
under nonbankruptcy law.189 Furthermore, although the common pool problem mandates displacement of creditors’ state-law collection remedies, bankruptcy law should nonetheless respect the relative values of creditors’ respective state-law priorities in distributing the debtor’s reorganization value.190 An attempt at changing the parties’ relative distributional entitlements in bankruptcy simply reintroduces the same sort of strategic incentives that led to the common pool problem under state law—what creditors’ bargain theorists describe as a “forum shopping” problem.191 For example, those who fare better under the new bankruptcy distributional regime will favor a bankruptcy proceeding, not because it will maximize aggregate creditor recoveries, but simply because it gives them a distributional advantage.192 Thus, creditors’ bargain theory squares with bankruptcy law’s prevailing norm of equal treatment of similarly situated creditors, and its respect for creditors’ relative priority rights, as the proper approach to bankruptcy distributional issues.193 This theory would, therefore, condemn the redistribution of value inherent in non-debtor releases.194

190. See Jackson, Logic and Limits, supra note 157, at 27-29.
192. In a more expansive analysis of the costs of upsetting parties’ relative distributional entitlements in bankruptcy, Barry Adler describes the “forum shopping” problem as a subset of a larger problem of strategic incentives. Bankruptcy negotiation and litigation over redistributing entitlements imposes both direct costs on the firm and indirect costs via the bankruptcy process’s disruptive effect on the firm’s business. Barry E. Adler, Bankruptcy and Risk Allocation, 77 Cornell L. Rev. 439, 464-73 (1992). Similarly, James Bowers advances what he calls a “dissipative” hypothesis: the opportunity for parties to change their relative entitlements in bankruptcy creates an environment conducive to time-consuming and expensive rent-seeking activity that dissipates much of a firm’s value during a reorganization proceeding. James W. Bowers, Rehabilitation, Redistribution or Dissipation: The Evidence for Choosing Among Bankruptcy Hypotheses, 72 Wash. U. L.Q. 955, 971-72 (1994). This problem is exacerbated by the system for compensating professionals in reorganization cases, which forces one class to bear the litigation expenses of all other classes and thereby encourages these other classes to extensively negotiate and litigate distributional issues. See Cynthia A. Baker, Other People’s Money: The Problem of Professional Fees in Bankruptcy, 38 Ariz. L. Rev. 35 (1996).
194. See supra Part III.B.3-4. Professors Jackson and Scott have attempted to reconcile existing reorganization law’s tendencies to depart from creditors’ priority rights with an expanded creditors’ bargain model, but they ultimately conclude that the costs of such a redistributive scheme likely do not justify any potential benefits. See Jackson & Scott, Bankruptcy Sharing, supra note 159, at 202-04. Barry Adler has done extensive analyses of the costs imposed by redistribution in bankruptcy, and he consistently concludes that “[j]ust as, traditional creditor priority remains the likely best approach.” Barry E. Adler, Financial’s Theoretical Divide and the Proper Role of Insolvency Rules, 87 S. Cal. L. Rev. 1107, 1110 (1994); see also Adler, supra note 192; Barry E. Adler, Financial and Political Theories of American Corporate Bankruptcy, 45 Stan. L. Rev. 311, 315-18 (1993). In fact, because existing reorganization law does not uniformly respect creditors’ nonbankruptcy priority rights, many advocate abandoning Chapter 11 in favor of more efficient reorganization mechanisms. Various alternative proposals abound in the literature and are thoughtfully summarized, reviewed, and critiqued in Ayer, Finance Theory, supra note 157, at 73-79; David A. Skeel, Jr., Markets, Courts, and the Brave New World of Bankruptcy Theory, 1993 Wis. L. Rev. 465; Tabb, Chapter II, supra note 159, at 802-15.
The creditors’ bargain approach to bankruptcy distributional issues also leads to the most profound and controversial aspect of the theory: it rejects the reorganization policy as an appropriate, independent goal of reorganization law. Bankruptcy should continue a business operation only when doing so will produce more value for creditors than would a liquidation of the firm’s assets. For the bankruptcy process to continue the business when continuation is not the value-maximizing deployment of the firm’s assets is inescapably redistributional—with all of the inappropriate strategic incentives that come with such a redistributional regime.195

Criticisms of the creditors’ bargain are many and varied. Yet, its repudiation of the reorganization policy, more than any other aspect, leads many to reject the creditors’ bargain as a comprehensive, coherent explanation of the legitimate province of bankruptcy law. The creditors’ bargain, with its contractarian approach to allocative efficiency, assumes that bankruptcy law exists only to maximize firm value and creditor distributions.196 Others note that this narrow focus on creditor wealth maximization ignores the widespread effects of a business failure on those without any formal right to a distribution from the debtor’s assets, such as employees, suppliers, customers, and the larger community in which the debtor’s business operates.197 Ef

195. See Jackson, Logic and Limits, supra note 157, at 24-27, 32-33, 190-91, 209-10; Baird, Loss Distribution, supra note 178, at 828-31; Baird & Jackson, Diverse Ownership Interests, supra note 178, at 99-104, 118; Jackson & Scott, Bankruptcy Sharing, supra note 159, at 177-78.
196. See Robert K. Rasmussen & David A. Skelk, Jr., The Economic Analysis of Corporate Bankruptcy Law, 3 Am. Bankr. Inst. L. Rev. 85, 86 (1995) (“efficient bankruptcy law . . . should ensure that post bankruptcy assets are put to their highest valued use.”). Elizabeth Warren was one of the earliest advocates of a broader role for bankruptcy policy, conceptualizing bankruptcy as a system that must accommodate many different normative goals in an attempt to distribute the losses that inevitably accompany insolvency and multiple creditor defaults. See Warren, Bankruptcy Policy, supra note 157; Warren, Policymaking, supra note 24; Elizabeth Warren, Why Have a Federal Bankruptcy System?, 77 CORNELL L. REV. 1093 (1992). Raymond Nimmer contemporaneously propounded a similar “loss allocation” approach to bankruptcy policy. See Nimmer, supra note 113, at 1010 (“the primary objective of bankruptcy is loss allocation . . . based on a blend of state law and federal policy for dealing with a debtor’s insolvency”). Donald Korobkin is one of the most persistent critics of the narrow focus of the creditors’ bargain, insisting that federal bankruptcy law uniquely responds to all aspects of financial distress, in ways that cannot be addressed by nonbankruptcy law. See Donald R. Korobkin, Contractarianism and the Normative Foundations of Bankruptcy Law, 71 TEX. L. REV. 541 (1993) [hereinafter Korobkin, Contractarianism]; Donald R. Korobkin, Rehabilitating Values: A Jurisprudence of Bankruptcy, 91 COLUM. L. REV. 717 (1991) [hereinafter Korobkin, Rehabilitating Values]; Donald R. Korobkin, Value and Rationality in Bankruptcy Decisionmaking, 33 WM. & MARY L. REV. 333 (1992) [hereinafter Korobkin, Bankruptcy Decisionmaking].
forts at reorganization and accompanying redistributions that might be considered inefficient from the standpoint of maximizing firm value and creditor distributions may nonetheless be desirable for the purpose of protecting these non-creditor and community interests.\textsuperscript{198}

Putting aside the normative debate concerning the desirability of an independent reorganization policy premised on the protection of such community interests, as a positive matter, no one questions the fact that such interests have always been prominent underpinnings of corporate reorganization law.\textsuperscript{199} Congress specifically cited the relevance of such interests as one of the important, distinguishing features of a Chapter 11 business reorganization.\textsuperscript{200} Along similar lines, the Supreme Court has repeatedly looked to the policy favoring business reorganization in its decisions interpreting the Bankruptcy Code.\textsuperscript{201}

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198. To use the language of economics, the creditors' bargain ignores externalities imposed upon non-creditors. See Carlson, supra note 197, at 456-57 n.16; Rasmussen & Skeel, supra note 196, at 94; Warren, Policymaking, supra note 24, at 356.

199. The congressional commission that shaped the current Bankruptcy Code, in discussing "rehabilitation of debtors" as one of the primary functions of bankruptcy law, identified the need for a "separate, integrated system of relief for ... business entities, which as economic units may cease to exist or be radically reorganized";

In cases involving business debtors there must be flexibility in case administration as well as in relief. Unlike consumer cases, business cases vary substantially in terms of economic size, community importance, and organizational complexity [with] large, publicly owned, corporate conglomerates employing thousands of persons and providing large quantities of products or services to the public.


200. The purpose of a business reorganization case, unlike a liquidation case, is to restructure a business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders. ... It is more economically efficient to reorganize than to liquidate, because it preserves jobs and assets.


In addition, in appointing the most recent Bankruptcy Review Commission that reexamined the Bankruptcy Code for possible reform, 202 Congress stated that "the Commission should be aware that Congress is generally satisfied with the basic framework established in the current Bankruptcy Code [and] the work of the Commission should be based upon reviewing, improving, and updating the Code in ways which do not disturb the fundamental tenets and balance of current law." 203 Thus, a policy that favors reorganization of business enterprises, even at the expense of creditor returns and allocative efficiency, no doubt will remain a stable feature of Chapter 11 for the foreseeable future. 204 Whether non-debtor releases are an appropriate means by which to advance this policy is, therefore, a legitimate inquiry to pursue.

Congress' desire that Chapter 11 foster a reorganization policy does not translate directly into any particular Bankruptcy Code provision empowering bankruptcy judges to approve anything that promotes a debtor's reorganization. 205 As many have noted, the

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203. H.R. Rep. No. 103-835, at 59 (1994), reprinted in 1994 U.S.C.C.A.N. 3340, 3368. Elizabeth Warren, one of the chief academic advocates of a traditional approach to bankruptcy policy, see sources cited supra notes 196-97, served as reporter to the Bankruptcy Review Commission. The Commission aligned itself with a more traditional view of the purposes of bankruptcy reorganization: "Principally through Chapter 11, business bankruptcy creates the opportunity to restructure failing businesses, to preserve jobs, to prevent the spread of economic failure to smaller suppliers and other dependent businesses, and to permit communities to retain their tax base." National Bankr. Review Commn., supra note 22, at 303. The Commission's Chapter 11 Working Group took a similar view, believing "there was widespread (although not unanimous) agreement that the Chapter 11 system was generally functioning well and that adjustments to the system, which could have widely-felt implications throughout the economy, should be modest in scope." Id. at 310. The Working Group identified the goals of Chapter 11 as:

- Maximize enterprise value
- Preserve jobs
- Rehabilitate viable businesses
- Encourage out of court restructuring
- Promote efficiency
- Benefit other parties affected by business failure

Id. at 309.

204. Congress evidently was aware that such a policy may compromise creditors' priority rights, consistent with the approach of the "loss allocation" theorists, discussed supra note 196: "Reorganization, in its fundamental aspects, involves the thankless task of determining who should share the losses incurred by an unsuccessful business and how the values of the estate should be apportioned among creditors and stockholders." S. Rep. No. 95-989, at 10 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5796.

205. In this regard, the general provisions of Chapter 11 stand in stark contrast to the railroad reorganization provisions of Chapter 11. See generally Julie A. Veach, Note, On Considering the Public Interest in Bankruptcy: Looking to the Railroads for Answers, 72 Ind. L.J. 1211 (1997). In conjunction with several Bankruptcy Code sections, including those concerning the plan of reorganization and its confirmation, the railroad reorganization provisions provide that "the court . . . shall consider the public interest in addition to the interests of the debtor, creditors, and equity security holders." 11 U.S.C. § 1125 (1994) (emphasis added). In addition, the court can confirm a railroad reorganization plan only if "the plan is consistent with the public interest," id. § 1123(a)(4), and in considering competing plans, "the court shall confirm the plan that is most likely to maintain adequate rail service in the public interest," id. § 1123(b) (empha-
reorganization policy rests not so much on explicit provisions of Chapter 11; rather, it is advanced indirectly, through those provisions of the Bankruptcy Code enabling a debtor to continue operating its business, while attempting to restructure its affairs.\textsuperscript{206} Thus, for a bankruptcy court to use its general equitable powers in an attempt to give the reorganization policy affirmative, substantive content, independent of any express provision of the Bankruptcy Code is of dubious validity, especially given the Supreme Court’s admonition that equitable powers are confined by the provisions of the Bankruptcy Code.\textsuperscript{207} This reasoning applies with special force to non-debtor releases, which are inconsistent with numerous principles and provisions of the Code, as discussed above.\textsuperscript{208} Even if one could find a statutory hook on which to hang non-debtor releases,\textsuperscript{209} they should nonetheless be rejected as

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\item 206. A most extensive exploration of this point is contained in Frost, supra note 197, at 93, 96-99 & n.98, 101-03, 107; see also Baird, Loss Distribution, supra note 178, at 830; Braucher, supra note 197, at 512-13; Nimmer, supra note 113, at 1033-34, 1055-59; Ponoroff, Bargaining Table, supra note 197, at 481; Warren, Bankruptcy Policy, supra note 157, at 787-89; Warren, Policymaking, supra note 24, at 354-56; cf. Jackson, Logic and Limits, supra note 157, at 190-91 (to “state that an effect of bankruptcy policy is sometimes to keep firms alive . . . is very different from saying that bankruptcy law embodies a distinct substantive fresh-start policy for corporations”); Ayer, Contested Concept, supra note 197, at 872 (“the idea of preserving going-concern values, although it may be functionally important to Chapter 11, is no more than hinted at in the text of the statute”); Korobkin, Contractarianism, supra note 196, at 591 (“corporate reorganization . . . preserves the possibility that, in the proper circumstances, the corporation in financial distress may survive as a viable enterprise”). Professor Ayer perceptively notes that debtor relief and the “concern, never clearly articulated, but immanent in most popular discussions of Chapter 11, [regarding] the question of an interest in ‘the community’ . . . seems to work best as long as it is least explicit.” Ayer, Finance Theory, supra note 157, at 72.


\item 208. See supra Part III.B., III.C.1.

\item 209. The most likely candidate seems to be § 1123(b)(6), which provides that a plan of reorganization may “include any other appropriate provision not inconsistent with the applicable provisions of” the Bankruptcy Code. 11 U.S.C. § 1123(b)(6); see, e.g., Feldstein, Third-Party Releases, supra note 20, at 26 n.8, 27 & n.11, 28 & n.14, 38-39 & n.53 (arguing repeatedly that § 1123(b)(6) provides statutory authority for non-debtor releases); John E. Swallow, Note, The Power of the Shield—Permanently Enjoining Litigation Against Entities Other than the Debtor—A Look at In re A.H. Robins Co., 1990 BYU L. REV. 707, 723-24 (same). Of course, reliance on this provision erroneously assumes that non-debtor releases are not inconsistent with applicable provisions of the Bankruptcy Code. The same is true of § 1123(a)(5) of the Bankruptcy Code, which says “a plan shall provide adequate means for the plan’s implementation.” 11 U.S.C. § 1123(a)(5); see In re Drexel Burnham Lambert Group, Inc., 138 B.R. 723, 772 (Bankr. S.D.N.Y. 1992) (citing § 1123(a)(5) in support of non-debtor releases). The plan provisions to be “implemented” must still conform to the requirements of the Bankruptcy Code. See 11 U.S.C. § 1129(a)(1). In addition, supplementary implementation sections such as § 1123(b)(6) merely beg the question whether non-debtor releases are in fact “appropriate” provisions of a plan. That question inevitably requires consideration of the fact that non-debtor releases directly contravene nonbankruptcy law that would impose liability on the released non-debtors. See United States v. Energy Resources Co., 495 U.S. 545, 550 (1990) (“Even if consistent with the Code, however, a bankruptcy court order might be inappropriate if it conflicted with another law that should have been taken into consideration in the exercise of the court’s discretion.”), discussed infra notes 216, 228, 255, and accompanying text; In re Sybaris Clubs Int'l, Inc., 189 B.R. 152, 159 (Bankr. N.D. Ill. 1995) (stating that non-debtor release is not a “proper means” of implementing
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an inappropriate means by which to further a supposed reorganization policy.

b. What Is a "Reorganization"?

An additional difficulty with using non-debtor releases as a tool to aid successful reorganization is the lack of any universal vision of a successful reorganization. The conventional notion of reorganization, as contrasted with liquidation, is this: The end goal of a reorganization is preservation of the debtor firm as an operating business. Yet, nowhere does the Bankruptcy Code define a reorganization as such, and by its terms, Chapter 11 provides that a plan of reorganization can provide for liquidation of the debtor—presenting the possibility of a liquidating reorganization. In fact, the Supreme Court

plan of reorganization); cf. Boyle, supra note 44, at 438 (characterizing reliance on §§ 105(a) and 1123(b)(6) as "bootstrapping" that uses "one catch-all provision to implement another catch-all provision," which is "the equivalent of granting the court the authority to take any action it deems necessary to ensure the success of a plan of reorganization, as long as such action does not violate an express provision of the Code").


211. In fact, the Bankruptcy Code makes no attempt whatsoever to define what a reorganization is. See Ayer, Field Guide, supra note 159, at 892. In §§ 1113 and 1114, Congress has made court approval of certain actions affecting collective bargaining agreements and retiree benefits turn upon whether the changes are necessary to the debtor's reorganization. See 11 U.S.C. §§ 1113(b)(1)(A), (c)(1), 1114(f)(1)(A), (g)(3). In accordance with the conventional notion of reorganization, the courts have generally interpreted this to mean necessary to prevent liquidation and permit continuation of the debtor's business. See generally 3 Chapter 11 Theory and Practice, supra note 114, §§ 19.13, 19.20, 19.34, 19.39. Cf. 11 U.S.C. §§ 1113(e), 1114(h)(1) (authorizing interim modifications of collective bargaining agreement or retiree benefits if "essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate").

212. See 11 U.S.C. § 1123(b)(4) ("[A] plan may provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among holders of claims or interests."); cf. id. § 1141(d)(3)(A)-(B) (specifying effect of confirmation when "the plan provides for the liquidation of all or substantially all of the property of the estate" and "the debtor does not engage in business after consummation of the plan"). The historical evolution of liquidations through reorganization proceedings, culminating in enactment of the foregoing provisions, is traced in John C. Anderson & Peter G. Wright, Liquidating Plans of Reorganization, 56 Am. Bankr. L.J. 29 (1982). Liquidating plans are commonplace in modern Chapter 11 practice. See Hotchkiss, supra note 102, at 6 & n.6 (empirical study of 806 public companies filing Chapter 11, finding that 15% of confirmed plans were liquidating plans); Jensen-Conklin, supra note 102, at 322 (empirical study of 42 confirmed Chapter 11 plans, finding 26% were liquidating plans); LoPucki & Whitford, supra note 102, at 602-04 (empirical study of 43 large Chapter 11 debtors, finding 49% of confirmed plans contemplated "shattering" of debtor's core business); Ed Flynn, Administrative Office of the United States Courts, Statistical Analysis of Chapter 11, at 12-13 (Oct. 1989) (unpublished paper, on file with author) (reporting results of empirical study of 2400 confirmed Chapter 11 cases, finding approximately one-fourth of confirmed plans are liquidating plans). In fact, Professors LoPucki and Whitford find that large Chapter 11 cases nearly always produce some liquidation of the debtor's assets, and the only "meaningful distinction is among various degrees of liquidation, not between liquidation and reorganization as discrete categories." LoPucki & Whitford, supra note 102, at 605-06; cf. Jensen-Conklin, supra note 102, at 322 (finding that out of 42 confirmed Chapter 11 plans studied, in addition to 26% that were liquidating plans, an additional 17% involved a partial liquidation of the debtor's business).
has held that an operating business is not even a prerequisite to an attempt at reorganization under Chapter 11.213

The chameleon-like nature of a reorganization presents more than an academic danger of abuse in the context of non-debtor releases. If a successful reorganization includes restructuring the affairs of nonbusinesses and liquidating a business' assets through a confirmed Chapter 11 plan, then non-debtor releases can be approved even in cases where none of the secondary benefits of preserving a business operation are present. In such a case, because the reorganization is not serving the conventional purposes of the reorganization policy, such as preserving workers' jobs, the so-called reorganization policy becomes nothing more than "the general [Bankruptcy] Code policy of maximizing the value of the bankruptcy estate."214 If the reorganization policy is reduced to a simple estate-maximizing principle, then all that is required for approval of non-debtor releases is some contribution to the estate by the released non-debtor. As discussed above, though, such contributions merely mask a process by which value entitlements are reshuffled, without any of the Bankruptcy Code protections that normally accompany such redistributions.215 Thus, the unique and distinct reorganization policy, which appears to be the only slender reed by which to sustain non-debtor

213. In Toibb v. Radloff, 501 U.S. 157 (1991), the Court held that an individual debtor, not engaged in an ongoing business operation, was eligible to file a Chapter 11 petition, noting that the "[Bankruptcy] Code contains no ongoing business requirement for reorganization under Chapter 11." Id. at 161. Although noting that "the structure and legislative history of Chapter 11 indicate that this Chapter was intended primarily for the use of business debtors," the Court refused to give credence to any argument "that Congress had a single purpose in enacting Chapter 11." Id. at 166, 163. A study of Chapter 11 cases in Los Angeles found that the principal asset of a majority of Chapter 11 debtors was real estate, rather than an operating business, with the cases filed primarily to protect the property from impending foreclosure. Lisa Hill Fenning & Craig A. Hart, Measuring Chapter 11: The Real World of 500 Cases, 4 AM. BANKR. INST. L. REV. 119, 122 (1996); cf. Ayer, Contested Concept, supra note 197, at 870 ("There are no going-concern values to preserve in a one-asset case: the office building almost certainly will be retained as an office building; the only question is who will own it."). Professor Ayer has ably demonstrated the multiple purposes Chapter 11 can serve in Ayer, Field Guide, supra note 159, and Ayer, Contested Concept, supra note 197. Professor Aaron describes the schizophrenic nature of Chapter 11 as follows:

Business reorganization is a 20th century enigma wrapped up in an 18th century conundrum. The enigma is the absence of a defined, systematic theory of reorganization. The conundrum is the joiinder of English bankruptcy law with American insolvency law in the 19th century. . . . neither [of which] had anything to do with reorganization.

Aaron, supra note 128, § 1.01, at 1:7.


215. See supra Part III.B.
releases, may be wholly illusory—permitting otherwise improper value redistributions solely for the sake of redistributing value.\textsuperscript{216}

A telling illustration of the malleability of the reorganization policy is one of the primary authorities proffered as legitimizing non-debtor releases: the Drexel “reorganization.” Before its financial undoing, Drexel was the most profitable securities firm in the United States, with nearly 11,000 employees.\textsuperscript{217} The bankruptcy court’s approval of the Drexel non-debtor releases was based on the stated rationale that furthering “[t]he ability of the Debtors to reorganize [is] fundamental to the bankruptcy power,”\textsuperscript{218} and “[t]he Debtors’ ability to reorganize is dependent upon the Release and Injunction Provisions.”\textsuperscript{219} Yet, this “reorganization” did not preserve Drexel’s prebankruptcy business operations. Upon filing bankruptcy, Drexel abruptly discontinued normal operations,\textsuperscript{220} and the confirmed Drexel plan of reorganization was largely a liquidating plan, establishing a liquidating trust for the orderly liquidation and distribution of the firm’s $2.5 billion of assets to creditors.\textsuperscript{221} The entity touted as the emergent “reorganized” Drexel, renamed New Street Capital Corporation (New Street), held less than $500 million in assets and em-

\textsuperscript{216} In fact, any legal standard tied to successful reorganization of the debtor seems to inevitably degenerate into a nonstandard. For example, this same tension has begun to surface in the collective bargaining and retiree benefit cases interpreting whether modifications are necessary to the debtor’s reorganization. See supra note 211; compare In re Cedar Rapids Meats, Inc., 117 B.R. 448, 450-51 (Bankr. N.D. Iowa 1990) (holding that a nonoperating business could not modify obligations because the only effect of such modification would be to change creditors’ relative priorities), with In re Ionosphere Clubs, Inc., 134 B.R. 515, 525 (Bankr. S.D.N.Y. 1991) (“in this liquidating case, ‘necessary to permit the reorganization’ must be interpreted to mean ‘necessary to accommodate confirmation of a Chapter 11 plan’”). The same phenomenon has occurred in the wake of the Supreme Court’s decision in United States v. Energy Resources Co., 495 U.S. 545 (1990). In that case, the Supreme Court held that, in conjunction with confirmation of a debtor’s plan of reorganization, a bankruptcy court could order the IRS to apply payments made under the plan first toward satisfaction of trust fund taxes for which the debtor’s officers and employees were personally responsible, “where it concludes that this action is necessary for a reorganization’s success.” Id. at 551. Since that decision, the courts have predictably divided over whether a court can enter such a payment application order in conjunction with a liquidating Chapter 11 plan. Compare United States v. Creditors Comm. (In re Deer Park, Inc.), 10 F.3d 1478, 1481-82 (9th Cir. 1993) (yes), with United States v. Kare Kemical, Inc. (In re Kare Kemical, Inc.), 935 F.2d 243, 244-45 (11th Cir. 1991) (no). Cf. United States v. Pepperman, 976 F.2d 123, 128-31 (3d Cir. 1992) (holding that Energy Resources has no application in Chapter 7 liquidation case). See generally Bryan T. Camp, Avoiding the Ex Post Facto Slippery Slope of Deer Park, 3 AM. BANKR. INST. L. REV. 329, 342-48 (1995); Richard Orrell-Jones, Note, Blinded by the Debtor’s Headlights: Deer Park’s Liquidation of United States v. Energy Resources, 12 BANKR. DEV. J. 451 (1996); Tal Marnin, Note, Trust Fund Taxes in Chapter 11 Liquidations: A Challenge to Energy Resources, 3 AM. BANKR. INST. L. REV. 231 (1995).


\textsuperscript{219} Id. at 753.


\textsuperscript{221} See Drexel, 138 B.R. at 733-34; Drexel Emerges from Bankruptcy, ATLANTA J. & CONST., May 1, 1992, at D3.
ployed only twenty people. Furthermore, New Street was owned by the liquidating trust, and as part of its liquidation of Drexel, the trust sold New Street and distributed the proceeds to creditors.

In a liquidating case such as Drexel, the reorganization produces few, if any, of the indirect benefits Congress contemplated for a traditional reorganization. Thus, the reorganization policy often adds very little to the debate concerning non-debtor releases and, at its worst, seems to be a vacuous and pretexual cover for the redistributional effects of non-debtor releases. Such abuse, though, seems endemic to any effort to transform the reorganization policy itself into an extra-statutory power. The success of a reorganization is (like beauty) in the eyes of the beholder. The reorganization policy, therefore, simply cannot place any realistic limits on the use of non-debtor releases.

c. Screening for Releases Necessary to Reorganization

Even if non-debtor releases and the reorganization policy could be restricted to reorganization in its conventional sense of preservation of an operating business, there are still good reasons to believe that non-debtor releases, in most cases, are immaterial to the debtor's ability to reorganize. Although many courts say non-debtor releases

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223. See Drexel, 138 B.R. at 735.


225. Compare In re Forty-Eight Insulations, Inc., 133 B.R. 973, 978 (Bankr. N.D. Ill. 1991) ("Even assuming that [the] worthy result [of reorganization] is reason to find equitable powers that otherwise would not exist, in this case the Debtor is not reorganizing, but liquidating. No ongoing business will be protected by a plan."); aff'd, 149 B.R. 860 (N.D. Ill. 1992), and In re Swallen's, Inc., 210 B.R. 123, 127 (Bankr. S.D. Ohio 1997) (concluding that whether "the injunction is essential to reorganization . . . contemplates that the injunction makes it possible for the debtor to continue in operation and requested injunction did not meet this "criterion because there is no operating business, but rather the debtor is liquidating"), with Abel v. Shugure (In re Ionosphere Clubs, Inc.), 184 B.R. 648, 655 (S.D.N.Y. 1993) (approving non-debtor release of, inter alia, debtor's officers and directors in liquidating plan of reorganization for Eastern Airlines), and Bayoud v. Medical Ctr. Hosp. of Garland, Inc. (In re American Dev. Int'l Corp.), 188 B.R. 925, 936-38 (N.D. Tex. 1995) (remanding approval of settlement agreement in Chapter 7 liquidation for reconsideration of permanent injunction releasing non-debtor actions), and Polygram Distribution, Inc. v. B-A Sys., Inc. (In re Burstein-Applebee Co.), 63 B.R. 1011, 1012, 1018-20 (Bankr. W.D. Mo. 1986) (approving permanent non-debtor injunction in liquidating Chapter 11).
are to be approved only in “extraordinary” circumstances, such as when they are “essential” or “necessary” to reorganization,\textsuperscript{226} the standard announced by the Second Circuit requires only a finding that “the injunction plays an important part in the debtor’s reorganization plan.”\textsuperscript{227} The Supreme Court has held that a much less intrusive form of a bankruptcy court’s equitable powers could issue only if “necessary for a reorganization’s success,”\textsuperscript{228} and nothing short of such a showing should suffice for non-debtor releases. More importantly, though, even the most stringent requirement of necessity has not and cannot confine non-debtor releases to those cases in which the debtor’s business will fail without such relief.

Courts point to two different aspects of non-debtor actions as posing a threat to the debtor’s reorganization that requires expunging the non-debtor rights. One is the possibility of contribution/indemnification claims by the released non-debtors.\textsuperscript{229} As discussed above, however, this concern overstates the problems posed by such claims and ignores the existing Bankruptcy Code mechanisms for resolving these claims.\textsuperscript{230} In light of these mechanisms, it is not readily apparent how the existence of more claims against the debtor endangers the

\textsuperscript{226} E.g., LTV Corp. v. Aetna Cas. & Sur. Co. (\textit{In re} Chateaugay Corp.), 167 B.R. 776, 780 (S.D.N.Y. 1994) (“[B]ankruptcy courts have permanently enjoined future lawsuits against non-debtors only where such a step was essential to confirmation of the Plan.”); \textit{In re} Master Mortgage Inv. Fund, Inc., 168 B.R. 930, 935, 937 (Bankr. W.D. Mo. 1994) (listing as one of many factors to consider that “[t]he injunction is essential to reorganization” and “without the [sic] it, there is little likelihood of success” and characterizing the permanent non-debtor injunction as “a rare thing, indeed,” that can be approved “only upon a showing of exceptional circumstances”); \textit{cf.} \textit{Burstein-Applebee}, 63 B.R. at 1018 (in liquidating Chapter 11, court approved permanent non-debtor injunction because “it will be impossible to administer the within [sic] bankruptcy estate unless a permanent injunction is granted”).

\textsuperscript{227} SEC v. Drexel Burnham Lambert Group, Inc. (\textit{In re} Drexel Burnham Lambert Group, Inc.), 960 F.2d 285, 293 (2d Cir. 1992). The district court opinion affirmed by the Second Circuit announced an even looser test: “Providing releases to and injunctions concerning non-Debtors is permissible where a material benefit results to the Debtors’ estates and advances consummation of a Plan.” SEC v. Drexel Burnham Lambert, Inc. (\textit{In re} Drexel Burnham Lambert Group, Inc.), 130 B.R. 910, 928 (S.D.N.Y. 1991), aff’d, 960 F.2d 285 (2d Cir. 1992). The district court characterized the non-debtor releases as producing “material benefits,” 130 B.R. at 928, and the Second Circuit described them as a “key component” of settlements that were an “essential element of Drexel’s ultimate reorganization,” 960 F.2d at 293. “Without the injunction, the directors and officers would be less likely to settle.” \textit{Id.} (emphasis added). This clearly falls short of requiring the non-debtor releases themselves to be essential or necessary to the reorganization. \textit{See also} Monarch Life Ins. Co. v. Ropes & Gray (\textit{In re} Monarch Capital Corp.), 173 B.R. 31, 42-43 (D. Mass. 1994) (juxtaposing somewhat inconsistent standards: “it is an extraordinary exercise of discretion, but bankruptcy courts may [permanently] enjoin non-debtor third party actions if such actions would [merely] adversely affect the debtor’s estate”), aff’d on other grounds, 65 F.3d 973 (1st Cir. 1995); \textit{In re} A.H. Robins Co., 88 B.R. 742, 754 (E.D. Va. 1988) (“The court may and will exercise its equitable power and authority to issue injunctive relief where there is a basis for concluding that reorganization or rehabilitation of Robins might be undermined and frustrated by the actions sought to be enjoined.” (emphasis added)), aff’d sub nom. Menard-Sanford v. Mabey (\textit{In re} A.H. Robins Co.), 880 F.2d 694 (4th Cir. 1989).

\textsuperscript{228} United States v. Energy Resources Co., 495 U.S. 545, 551 (1990), discussed infra note 255.

\textsuperscript{229} \textit{See} sources cited supra note 151.

\textsuperscript{230} \textit{See} supra Part III.C.1.
debtor's continuing viability and ability to reorganize.\textsuperscript{231} To equate the two is to link the optimal use and value of the debtor's assets with the amount and nature of the claims against those assets. Economic and finance theory, however, posit that there is no necessary relationship between the two.\textsuperscript{232} If the optimal, value-maximizing use of the debtor's assets is to continue the debtor's present business operations, that will be true whether the debtor's outstanding obligations are ten dollars or ten billion dollars. At bottom, then, the constant reminder that non-debtor actions may create additional claims against the debtor seems to be nothing more than dissatisfaction with the existence of too many claims against the debtor—a complaint that can be heard from nearly any creditor of any bankruptcy debtor. Thus, the defining theme of non-debtor releases appears once again: redistribution for the sake of redistribution.

The other threat to a debtor's reorganization cited as necessitating non-debtor releases is the potential loss of contributions the released non-debtors are making to the debtor's reorganization effort.\textsuperscript{233} Obtaining contributions necessary to the debtor's survival that would not be forthcoming in the absence of non-debtor releases would appear to advance the reorganization policy directly. To approve non-debtor releases on this basis, however, assumes an ability to determine that the proffered contribution is, in fact, necessary for the debtor's continued operations \textit{and} that this necessary contribution can be procured only through release of creditor claims against the contributing non-debtor party. In many cases, though, it seems clear that a piecemeal liquidation of the debtor's business is not the most appropriate, value-maximizing use of the debtor's assets, irrespective of contribu-

\begin{footnotesize}
\textsuperscript{231} As Professor LoPucki points out, one of the major contributions the bankruptcy system makes in the area of claims litigation and collection is "the dispute resolution process has been separated from the processes which close the debtor's business and liquidate its assets" under state law. LoPucki, \textit{supra} note 157, at 350.


\textsuperscript{233} See sources cited \textit{supra} note 120.
\end{footnotesize}
tions by released non-debtors. In such a case, non-debtor releases do not prevent liquidation and preserve the debtor's business operations; they serve only non-debtor releases' redistributational tendencies.

An illustrative case is the A.H. Robins reorganization, the watershed case paving the way for growing judicial acceptance of non-debtor releases. The primary source of funding for creditor distributions in Robins came from a sale of Robins' business as a going concern to American Home Products Corporation (AHP). Would failure to approve global non-debtor releases have prevented a going-concern sale of Robins' business, condemning A.H. Robins to death on the liquidator's auction block? That possibility seems extremely doubtful. Robins' business was attractive enough that the prospect of a sale produced vigorous bidding amongst several prospective purchasers. It was only after AHP emerged as the apparent victor, in subsequent negotiations, that "AHP took the position that the successor corporation to Robins must be as free as possible from the burdens and distractions of continuing litigation arising out of the use of the Dalkon Shield, no matter who the defendant might be." This bargaining stance was not tested by reopening the bidding, however, which may have produced less value for the business than AHP was

234. See Rasmussen & Skeel, supra note 196, at 87-88 (discussing distinction between economic distress and financial distress, and citing cases such as Johns-Manville, Federated Department Stores, and Texaco as reorganizations where "few if any thought that these firms should be closed. They were all healthy firms in that their operating revenues exceeded their operating costs. The problem was their capital structure.").

235. Professor Nimmer describes the reorganization policy and "whether the business will be continued" in terms of its indirect effect on "dependents" and the concern for "protecting the suppliers, employees, children and others who 'depend' on receiving value from the debtor." Nimmer, supra note 113, at 1055, 1027. Nimmer also notes that "[i]n many cases, the debtor and a majority of creditors agree on a particular use of an asset," and if "there is no dispute about what will be done with the business," then "[i]t eliminates concern about dependents." Id. at 1018, 1055, 1056. Nimmer then concludes that treating certain parties' distributional rights as "a surrogate for protecting dependents" risks improper redistributions of value "without benefiting the dependents." Id. at 1057, 1059. Nimmer calls this "taking assets from John and handing them to Jane, while believing we are helping Paul." Id. at 1059.

236. See supra Part I.


238. In addition to AHP, the primary contenders were the Rorer Group and Sanofi, the second largest pharmaceutical company in France. The competition amongst these companies to acquire Robins is described in Sobol, supra note 10, chs. 11, 14; see also Dalkon Shield Claimants' Comm. v. Aetna Cas. & Sur. Co. (In re A.H. Robins Co.), 88 B.R. 755, 757-59 (E.D. Va. 1988), aff'd, 880 F.2d 709 (4th Cir. 1989).

239. Robins, 88 B.R. at 758; see also Sobol, supra note 10, at 221. The Robins court, in approving the non-debtor releases, emphasized AHP's insistence. See Robins, 88 B.R. at 747. Yet, the idea of a "super discharge" of all potentially liable parties originated from within Robins' management, and well before AHP arrived on the scene. See Sobol, supra note 10, at 220, 334.
Thus, while failure to approve the non-debtor releases may well have produced lower aggregate distributions to Robins’ creditors and shareholders, that was not an issue concerning the ultimate survival of Robins’ business operations. Once again, the affinity for non-debtor releases reveals itself as a distributional concern.

One could certainly imagine an instance in which a non-debtor seeking the protection of a release could make a contribution to the debtor’s operations that could not be obtained elsewhere and that could mean the difference between continuing and discontinuing operations. For example, it is commonly recognized that many smaller, closely-held businesses are highly dependent upon the efforts and skills of the owner-manager. The ability of such a business to emerge from bankruptcy as an operating entity, then, might well hinge on the key individual’s continued management of the business. If that key manager insists on a non-debtor release as a condition to continued participation in the business, then why should the bankruptcy court be denied the authority to approve the non-debtor release in order to save the debtor’s business?

To begin with, the key manager’s demand for a non-debtor release can be usefully recharacterized as a demand for more compensation for providing future managerial services to the reorganized debtor. The key manager could just as easily demand a more straightforward means of increased compensation, directly from the debtor. The likely objection to that alternative, though, is that the cost of directly compensating the key manager for the equivalent of the non-debtor liability release would be prohibitive. Indeed, implicit in the idea that the key manager’s continued services can be assured

240. The AHP offer was clearly superior to those of Rorer and Sanofi. See Sobol, supra note 10, at 207; Robins, 88 B.R. at 747. Thus, while the Dalkon Shield claimants’ committee had consistently opposed the desire of Robins’ management for global non-debtor releases, they conceded the issue in order to retain the value of the agreement with AHP. See Sobol, supra note 10, at 220-21, 335-36. Some have even speculated that AHP was bluffing, because the Robins acquisition was much too valuable to abandon. E.g., id. at 334-35 (citing analysts’ reaction to AHP acquisition of Robins as the “steal of the century”).

241. Jackson has noted the same phenomenon in the context of a key supplier threatening to terminate the debtor’s supply line unless the supplier is given preferential treatment on a prepetition unsecured claim: “Supplier’s threat is more likely to be made when the best course of action for the creditors as a group is one of continuing the business whether or not Supplier’s demand is met. In those cases, which are likely to be far more common, the issue is not that of asset deployment but the quintessential non-bankruptcy issue of asset distribution.” Jackson, Logic and Limits, supra note 157, at 162 (footnote omitted).

242. See Lynn M. LoPucki & William C. Whitford, Bargaining over Equity’s Share in the Bankruptcy Reorganization of Large, Publicly Held Companies, 139 U. Pa. L. Rev. 125, 149-50 (1990). The analysis in the text assumes that the manager’s services are irreplaceable and the debtor’s business can continue only if the manager’s services are retained. Of course, this assumption is not universally warranted and is another item of substantial uncertainty surrounding any determination of the necessity of a non-debtor release.

243. Cf. Ayer, Contested Concept, supra note 197, at 880 n.56 (“If the old equity owner has management skills that are essential to the continuation of the business, she will certainly have the opportunity to be retained as an employee.”).
only through a non-debtor release is the notion that the potential liability release is worth far more than the debtor is willing or able to pay the manager for those services. The non-debtor release costs the continuing business nothing, while providing the key manager valuable compensation. The very existence of this alternative compensation scheme, however, assures us that requests for non-debtor releases will not be limited to instances in which they are necessary for survival of the debtor’s business. Cost-free compensation will prove attractive to any business, solvent or insolvent, viable or nonviable—allowing the business to reduce the amount of direct compensation it must pay the key manager. Thus, any reorganizing debtor and its creditor and shareholder constituencies stand to benefit directly from any non-debtor release that reduces the business’ ongoing operating expenses and correspondingly increases the value of that business. The more critical the key manager’s services to the business, the more deceptively attractive becomes the appeal that reorganization hinges on approval of the release. Yet, the mere fact that the debtor has offered a key manager compensation in the form of a non-debtor release tells us very little about whether the non-debtor release is necessary to continuation of the debtor’s business.244

In point of fact, the non-debtor release will serve the reorganization policy and save the debtor’s business from liquidation only if (1) the key manager would not accept, in lieu of the non-debtor release, monetary or another form of compensation of equivalent value, paid directly by the reorganized debtor,245 or (2) the debtor’s continuing business operations simply could not underwrite the full cost of this additional compensation for the key manager. Scenario (1) seems unlikely enough that scenario (2) appears to capture the essence of necessity. If the debtor’s business can afford to pay the key manager this additional compensation directly, the debtor’s desire for the non-debtor release is the common desire of any business for cost-free management compensation. Necessity only attaches if the prospect of fully compensating the key manager means the business is not worth continuing, and creditors and shareholders will fare better through liquidation.

When the bankruptcy court faces a request to approve a non-debtor release for the key manager, the judge must decide the knotty question of whether the request flows from the universal desire for


\[245. \text{An example of such an alternative form of equivalent compensation might be the reorganized business' commitment to fully pay or indemnify the key manager’s expenses and losses incurred in defending the non-debtor actions.} \]
cost-free compensation or is a true case of necessity. The bankruptcy judge will have little to rely on in this regard, other than the self-serving and vague statements of the debtor, statutory committees, or the key manager that the non-debtor release is "important," "necessary," or "essential."\(^{246}\) Not only do such statements seem to rely on the non sequitur that because the manager's services are necessary the non-debtor release is necessary.\(^{247}\) But true necessity—in the sense of meaning the difference between continuing economic viability and inevitable liquidation—is nearly impossible to either verify or disprove in any reliable manner.\(^{248}\) To ask a bankruptcy judge to make this determination is to ask the court to engage in unbridled speculation.\(^{249}\) Combine with this (1) the incentives of the parties to seek

\(^{246}\) In the context of the evidence proffered to support the necessity of cross-collateralization, Professor Tabb accurately describes such testimony as a "preordained" and "conclusory . . . recital of the magic words." Tabb, supra note 244, at 166, 163.

\(^{247}\) Cf. In re Classic Chem. & Supply Co., 198 B.R. 112, 116 (Bankr. E.D. Pa. 1996) (refusing to approve an Energy Resources tax payment designation order as necessary to reorganization, because testimony of debtor's principal "at best supports the conclusion that, if the Plan's designation is allowed to stand, the Plan is likely to succeed because of his efforts. It does not support the conclusion that, were the designation eliminated, the Plan would not succeed."); Zaretsky, supra note 40, at 272 (opining in temporary non-debtor stay context that "courts should treat threats to 'throw in the towel' as nothing more than empty threats").

\(^{248}\) See Rasmussen & Skeel, supra note 196, at 89 ("it is very difficult to determine the economic viability of a firm that is undergoing financial distress"). Richard Levin, one of the principal drafters of the Bankruptcy Code, has developed a model which divides the types of decisions bankruptcy courts are asked to make into "forensic" and "nonforensic" decisions. Richard B. Levin, Towards a Model of Bankruptcy Administration, 44 S.C. L. Rev. 963, 971-75 (1993). Forensic decisions are those normally associated with the judicial process and adjudicative facts, involving past events. See id. at 970-71; see also Frost, supra note 197, at 124-25. To a greater degree than in ordinary civil litigation, bankruptcy judges are also called upon to make nonforensic decisions, which "require an evaluation of risks and a balancing of competing risk/reward preferences among those involved in the case" and which "involve the exercise of considered judgment, typically business judgment, about a future course of action." Levin, supra, at 972, 973. Levin correctly concludes that bankruptcy judges are not well-suited to make nonforensic decisions:

No amount of evidence can enable the decision-maker to "find facts" about the future. In fact, because the objective facts are rarely in dispute, litigation over these matters often involves the testimony of managers and consultants concerning why a particular proposed course of action is likely to succeed or fail.

\[\ldots\] The adversary system is not a particularly satisfactory way to make \ldots nonforensic decisions. \ldots The system does not encourage the disputing parties to cooperate in developing solutions to nonforensic problems.

\[\ldots\] Courts have no particular expertise in the substance of nonforensic decisions, nor do they have the ability to become sufficiently involved in the particular estate or business to make sensible decisions. \ldots At best, the judges get an adversarial presentation of the highlights instead of the complete picture.

\[\ldots\] No legal standards exist to guide courts in making nonforensic decisions. There is \ldots no right or wrong answer to the issues presented in a nonforensic decision.

\[\ldots\] The court is relying on a formal presentation of facts and analysis by the representative of the estate, who has no particular incentive to explain why a proposed course of action might not be wise.

\ldid{Id. at 975, 982-83 (footnote omitted); see also Frost, supra note 197, at 125-29.}

\(^{249}\) Much of the economic analysis of bankruptcy reorganizations is devoted to making the point that the only reliable method of determining whether continuation of the business is economically feasible is to ensure that the continuation decision comes from those who stand to benefit directly from continuation of the business and ensure that these parties will directly bear
cost-free compensation in the form of non-debtor releases, even in cases in which they are not necessary to the business’ survival, and (2) the widely reputed and understandable tendency of bankruptcy judges to avoid “upsetting the applecart” by injecting any risk of undoing a successful reorganization. All said then, leaving approval of non-debtor releases to the equitable discretion of bankruptcy judges on a case-by-case basis sanctions wide-ranging and uncertain redistributions of value, with very little assurance that such redistributions are justified by the countervailing indirect benefits of saving a business operation in any given case.  


d. Congress, the Courts, and the Reorganization Policy

Discretionary equitable approval of non-debtor releases would be a fundamentally objectionable practice, even if it were possible to overcome the innate screening problems associated with non-debtor releases and approve only those non-debtor releases absolutely necessary to preserve a business operation otherwise destined for liquidation. Necessity, again in the context of our key manager example, indicates that the debtor’s ongoing business operations are not sufficiently profitable to shoulder the burden of directly compensating the key manager to the full extent necessary to retain the manager. A non-debtor release, thus, provides the “cost-free” compensation nec-

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250. Anyone who has ever presented an objection to confirmation of a plan of reorganization likely prefers the “steamroller” analogy to the “applecart” analogy. Judges’ reluctance to disturb the plan of reorganization is nothing new. See Korobkin, Rehabilitating Values, supra note 196, at 751-52 nn.144 & 148, 754 n.155 (quoting from contemporary commentators describing the same tendency under old equity receiverships).

251. In terms of an economist’s tabulation of costs and benefits, permitting approval of non-debtor releases in the discretion of the bankruptcy judge places another bargaining chip on the reorganization table, creating yet another opportunity for the parties to further dissipate the debtor’s reorganization value through time-consuming and expensive rent-seeking activities. See sources cited supra note 192. In addition, both the difficulties of screening for necessary releases and the inherent unpredictability of a discretionary approval introduce costs of their own, which also offset any indirect benefits produced by releases that do permit an otherwise infeasible reorganization. See Adler, supra note 192, at 443, 464, 472-73 (discussing costs of uncertain redistributions); Jackson & Scott, Bankruptcy Sharing, supra note 159, at 199-202 (discussing uncertainty and screening costs introduced by redistributive rules); cf. Skeel, supra note 113, at 244-47 (same in context of new value plans).
necessary to save the business, producing all of the indirect community benefits the reorganization policy promotes.

A non-debtor release, though, is cost-free only from the standpoint of the reorganized debtor’s business operations; the cost of this additional compensation is extracted involuntarily from those creditors with valuable non-debtor claims against the key manager. Nonbankruptcy law would place liability upon the key manager, presumably, based on legitimate policies that contemplate various benefits from this liability scheme.252 In many cases, of course, non-debtor liability law and policy assumes its greatest significance in precisely the context in which non-debtor releases are approved; nonbankruptcy law gives the creditor another source of recovery in the event the debtor is unable to fully pay the creditor because of financial difficulties. Thus, the propriety of a necessary non-debtor release directly pits the reorganization policy against these legitimate nonbankruptcy policies underlying non-debtor liability.

Given these conflicting policies, then, approval of a non-debtor release is a unilateral determination by a bankruptcy judge that the reorganization policy alone, without any further statutory directive from Congress, is sufficient to override both fundamental distributional policies and provisions of the Bankruptcy Code253 and the nonbankruptcy law and policy of non-debtor liability. Yet, the Supreme Court’s most recent pronouncements on the scope of a bankruptcy court’s equitable powers emphasized that they may not be used to reorder distributional priorities in a manner that arrogates to the courts the policy-making functions that Congress exercises in enacting specific provisions of the Bankruptcy Code.254 Moreover, the

252. For example, in the context of securities fraud, liability rules embody complex public policy judgments regarding, inter alia, compensation for innocent victims, deterrence of fraud, internalizing the costs of fraudulent conduct, and placing liability upon the least-cost-avoiders of fraud. See Louis Loss & Joel Seligman, Fundamentals of Securities Regulation 1108 (3d ed. 1995); see also Zaretsky, supra note 40, at 227-32, 238-44, 248, 250, 269-74, 279-80 (discussing impact of non-debtor stays upon policies underlying various types of non-debtor liability, including guaranty liability and trust fund tax liability); Boyle, supra note 44, at 421 & n.2, 444 (citing SEC’s position that non-debtor release of individual tort and securities fraud liability “tends to undermine the policy considerations underlying joint and several liability”).

253. See supra Part III.B.

Court has never gone so far as to sanction a use of general equity powers that would so directly contravene nonbankruptcy law and policy. Indeed, Callaway v. Benton, striking down a permanent non-debtor injunction under the 1898 Act, was premised on legislative supremacy in making such cardinal policy choices: "We do not believe that Congress intended to leave to individual judges the question of whether state laws should be accepted or disregarded, or to make the criterion to be applied the effect of the law upon the [reorganized debtor's operations]."

The case for withholding such policy-making judgments from the bankruptcy courts is compelling in the context of non-debtor releases. Non-debtor releases compromise the law and policy of non-debtor liability, presumably in an effort to produce indirect community benefits from a successful reorganization. Yet, even the staunchest advocates of a broad community-based approach to bankruptcy policy readily admit that the full extent of such benefits are difficult, if not impossible, to predict or measure. Indeed, there may be negative indirect

prompt a court to order equitable subordination must not occur at the level of policy choice at which Congress itself operated in drafting the Bankruptcy Code." Noland, 116 S. Ct. at 1528.

255. In fact, in affirming a bankruptcy court order affecting non-debtor liability, issued pursuant to the court's general equitable powers under Bankruptcy Code § 105(a), the Supreme Court said that "[e]ven if consistent with the [Bankruptcy] Code, . . . a bankruptcy court order might be inappropriate if it conflicted with another law that should have been taken into consideration in the exercise of the court's discretion." United States v. Energy Resources Co., 495 U.S. 545, 550 (1990). The order at issue in Energy Resources was entered in conjunction with confirmation of a Chapter 11 plan of reorganization, requiring the IRS to apply tax payments made by the debtor under the plan first toward satisfaction of trust fund taxes for which the debtor's officers and employees were personally responsible, because "the Bankruptcy Court concluded that this designation was necessary to ensure the success of the reorganization." Id. at 548. The debtor, of course, was interested in eliminating these individuals' personal liability as quickly as possible, by first paying the trust fund taxes. However, the IRS obviously was concerned about a potential default by the debtor and wanted these individuals' guaranties to remain in place to the fullest extent possible, by applying the debtor's payments first toward satisfaction of non-trust-fund taxes for which there was no such guaranty. Pursuant to internal policy, the IRS considered reorganization plan payments to be "involuntary" ones for which the debtor could not designate application. Nothing in the Internal Revenue Code, however, prevented prior application of reorganization plan payments toward trust fund taxes. Therefore, the bankruptcy court's equitable order did not present a direct conflict between the reorganization policy and the non-debtors' liability under the Internal Revenue Code. In fact, the order, by assuring earlier payment of trust fund taxes, actually promoted the congressional policy of enhancing collectability of these taxes. See id. at 546-51.


257. Id. at 141 (citation omitted). This passage is quoted in full, infra text accompanying note 459.

258. E.g., Gross, supra note 197, at 1045-46; Korobkin, Contractarianism, supra note 196, at 581 n.179 ("I do not mean to suggest that diverse aims may be reduced to a single value of measurement. On the contrary, I am committed to the position that the aims of persons in financial distress are fundamentally incommensurable."); Warren, Bankruptcy Policy, supra note 157, at 788 ("the broader effects of business failure can be elusive to measure"). In an expanded analysis of the indirect costs and benefits of effecting redistributions by promoting reorganization, Professor Frost demonstrates that it is not only difficult to predict or measure the indirect benefits of reorganization, but determining who actually bears the ultimate cost of bankruptcy redistributions is also very slippery, because of the ability of many creditors to anticipate and recoup such costs ex ante. Frost, supra note 197, at 102-03, 112-22; see also Ayer, Contested
effects from preserving the debtor's business for the debtor's business rivals and those business' employees and communities. By what means, then, is a bankruptcy judge to determine that the indirect “benefits” of reorganization are more important than the indirect benefits produced by non-debtor liability, and outweigh the direct costs imposed on creditors whose valuable non-debtor rights are extinguished?\footnote{260}

Professor Frost is correct. The adjudicative process through which bankruptcy reorganizations are effected is ill-suited for engaging in an appropriate case-by-case analysis of such far-reaching consequences.\footnote{261} The various communities of affected indirect interests have no representatives to speak on their behalf;\footnote{262} their interests are

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Concept, supra note 197, at 879 n.52; Baird & Jackson, Diverse Ownership Interests, supra note 178, at 102; Bowers, supra note 192, at 964-68; Braucher, supra note 197, at 517-19; Nimmer, supra note 113, at 1034; Rasmussen & Skeel, supra note 196, at 86-87; Warren, Unmentionable Case, supra note 197, at 468 (“[t]racing redistributive consequences is extraordinarily difficult”).

\footnote{259} See Jackson, Logic and Limits, supra note 157, at 25 n.8; Baird & Jackson, Diverse Ownership Interests, supra note 178, at 102; Frost, supra note 197, at 120-21; Korobkin, Contractarianism, supra note 196, at 554 n.63; Warren, Policymaking, supra note 24, at 344 n.17. For a recent empirical study finding negative effects of bankruptcy proceedings on competitors' stock prices, see Robert M. Lawless et al., Industry-Wide Effects of Corporate Bankruptcy Announcements, 12 Bankr. Dev. J. 293 (1996).

\footnote{260} Professor Gross responds to the problem of inability to measure the indirect effects of reorganization by placing “confidence in the ability to measure seemingly amorphous concepts (which could be termed externality in economic parlance) if we set about trying to do so rather than assuming it cannot be done.” Gross, supra note 197, at 1045-46. An important instrumental question, though, is whether this is a task we should leave to the courts. See Hon. Barry S. Schermer, Response to Professor Gross: Taking the Interests of the Community into Account in Bankruptcy—A Modern-Day Tale of Selling the Cat, 72 Wash. U. L.Q. 1049 (1994). Professor Warren, in the vanguard of those advocating bankruptcy policy's responsibility to the larger community, argues that “judges who believe they can discern and protect the public interest... risk upset the balance of interests established by the legislature.” Warren, Policymaking, supra note 24, at 356 n.47. Professor Korobkin also apparently believes that Congress should be the one to strike the delicate balance among the diverse interests affected by bankruptcy laws. See Korobkin, Contractarianism, supra note 196, at 627-31. Yet, he also believes that “the rule of equity has an essential role in bankruptcy decisionmaking.” Korobkin, Bankruptcy Decisionmaking, supra note 196, at 364. Korobkin recognizes that such “[e]quitable decisionmaking... introduce[s] certain identifiable risks” and would give to Congress the role of placing specific constraints on courts' equitable decision-making powers, while at the same time arguing that “[a]t least as a starting point, it must allow the bankruptcy court sufficient flexibility to reach a decision that responds to the characteristics of the individual bankruptcy case.” Id. at 361, 358. Non-debtor releases, however, present such stark policy conflicts that giving flexibility to the courts inevitably undermines Congress' role as the found of fundamental bankruptcy policy. But cf. Ponoroff & Knippenberg, Good Faith Filing, supra note 197, at 961, 963, 966, 968-70 (arguing that the courts, not Congress, should control the evolution of bankruptcy policy).

\footnote{261} Frost, supra note 197, at 122-35; see also Baird, Loss Distribution, supra note 178, at 831-32.

\footnote{262} See Warren, Policymaking, supra note 24, at 355. The farthest current law goes in this direction is to give a “labor union or employees' association, representative of employees of the debtor,... the right to be heard on the economic soundness of a plan affecting the interests of the employees.” Fed. R. Bankr. P. 2018(d). The employee representative, however, “shall not be entitled to appeal any judgment, order, or decree relating to the plan, unless otherwise permitted by law.” Id. Given the far-flung consequences of a bankruptcy reorganization and the difficulty of tracing those consequences, any attempt to formulate appropriate standing rules for indirectly affected interests would be haphazard, at best. See Frost, supra note 197, at 129-32; Schermer, supra note 260, at 1050-51; cf. Lawless, Notice in Bankruptcy, supra note 172, at 1228.
raised only by those parties with a direct financial stake, seeking to enhance their returns by invoking the undefined "public interest" in reorganization.\footnote{263} Little wonder, then, that non-debtor releases seldom promote this public interest and are primarily a mechanism for realigning parties' distributonal rights.\footnote{264} Furthermore, a discretionary case-by-case assessment of the ultimate public interest in reorganization, versus the public interest in non-debtor liability, is simply beyond the ken of the adjudicative process. Such public interest determinations implicate not only the relative institutional competency of the judiciary as compared with the legislature, but also the legitimacy of judicial encroachment into the arena of social policymaking.\footnote{265} Any attempt to give the judiciary such a function with respect to non-debtor releases will be fraught with inconsistency and arbitrariness\footnote{266} that can do nothing but weaken the effectiveness of non-debtor liability law and policy,\footnote{267} and as discussed above, without any clear progress toward a more effective reorganization policy.

Ultimately, then, not even the reorganization policy will support the practice of approving non-debtor releases. Strictly in terms of policy considerations, the courts should flatly prohibit non-debtor releases, and Congress should seriously consider repeal of those portions of the 1994 Bankruptcy Code amendments that give bankruptcy judges discretion to approve the release of non-debtor asbestos claims against a debtor's management and financiers.\footnote{268} Many courts, after considering the relevant policies, have nonetheless approved

\footnote{263} See Baird, Loss Distribution, supra note 178, at 830; Frost, supra note 197, at 102; Nimmer, supra note 113, at 1057-59.

\footnote{264} See supra Part III.C.2.b-c.

\footnote{265} See Frost, supra note 197, at 123; Schermer, supra note 260, at 1052. For more on the comparative institutional advantages and disadvantages of the courts, see Neil K. KOMESAR, IMPERFECT ALTERNATIVES: CHOOSING INSTITUTIONS IN LAW, ECONOMICS, AND PUBLIC POLICY ch. 5 (1994).

\footnote{266} There is no consensus-reaching mechanism for reconciling the disparate policy views of bankruptcy judges as to the importance of reorganization versus non-debtor liability, and stare decisis can play little role in providing consistency for the equitable, case-by-case, discretionary approval of non-debtor releases. Thus, a coherent, coordinated policy-driven approach to non-debtor releases seems unlikely to emerge. See Frost, supra note 197, at 132-35; Schermer, supra note 260, at 1052. But cf. Ponoroff & Knippenberg, Good Faith Filing, supra note 197, at 970-71 (arguing that dialectic prompted by courts' reported opinions "minimizes the potential for random or inconsistent decision making").

\footnote{267} Economic analyses advocating respect for parties' relative nonbankruptcy entitlements voice the concern that bankruptcy redistributions risk diluting or undermining the force of nonbankruptcy law and policy. See, e.g., Adler, supra note 192, at 477-79; Bowers, supra note 192, at 967-68 n.55, 977; Jackson, Creditors' Bargain, supra note 178, at 869-71 & n.61; Jackson & Scott, Bankruptcy Sharing, supra note 159, at 162-63 & nn.13, 15; Rasmussen & Skeel, supra note 196, at 87. This same concern underlies bankruptcy's traditional presumptive respect for nonbankruptcy rights. See COMM'N REPORT, supra note 83, pt. I, at 67-68, 71, 74-75, 77-78; Eisenberg, supra note 135, at 956-59; Nimmer, supra note 113, at 1015, 1024-25, 1058; Warren, Policymaking, supra note 24, at 359.

\footnote{268} See supra notes 17-19 and accompanying text.
non-debtor releases. This part III has argued that those courts’ policy analyses are superficial and misguided. For those courts, though, perhaps the more important analysis is one that demonstrates they lack authority to approve non-debtor releases. Part IV of this article sets forth that analysis by examining the jurisdictional bases for bankruptcy courts to enjoin non-debtor actions.

IV. Bankruptcy Jurisdiction to Enjoin Non-Debtor Actions

Perhaps the most complicated and confusing aspect of the controversy surrounding non-debtor releases and injunctions is the preliminary inquiry for any exercise of judicial power—jurisdiction. Without regard to the advisability of a non-debtor release in any particular case, is there bankruptcy jurisdiction to release non-debtors from liability to creditors and permanently enjoin creditors’ actions against them? Most of the cases approving or disapproving non-debtor releases contain little, if any, discussion of the jurisdictional issue, and what little discussion appears is woefully cryptic and conclusory. Courts that have approved non-debtor releases have done so pursuant to the equitable injunctive powers of bankruptcy courts under section 105 of the Bankruptcy Code. Section 105, however, is not an independent source of jurisdiction, a notion that section 105(c) now makes explicit. Therefore, a more searching inquiry into the jurisdictional foundations for such an extraordinary injunction is warranted.

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269. This jurisdictional discussion focuses on the subject matter jurisdiction of federal courts under federal bankruptcy law, enacted pursuant to Article I, Section 8, Clause 4 of the U.S. Constitution. Personal jurisdiction in bankruptcy proceedings is rarely problematic, as Bankruptcy Rule 7004(d) authorizes nationwide service of process, unrestricted by any requirement of “minimum contacts” with the forum state. The relevant forum for “minimum contacts” in the bankruptcy setting is the United States as a whole. See generally 1 NORTON, supra note 21, § 4.41. But see Jeffrey T. Ferrell, The Perils of Nationwide Service of Process in a Bankruptcy Context, 48 WASH. & LEE L. REV. 1199 (1991) (arguing that the courts’ failure to consider whether nationwide service of process is fundamentally fair in a given case raises due process concerns); E. Scott Fruhwald, The Related To Subject Matter Jurisdiction of Bankruptcy Courts, 44 DRAKE L. REV. 1, 33-37 (1995) (same).

270. See infra notes 422-24 and accompanying text.

271. Section 105(c) provides as follows:

   The ability of any district judge or other officer or employee of a district court to exercise any of the authority or responsibilities conferred upon the court under this title shall be determined by reference to the [jurisdictional] provisions relating to such judge, officer, or employee set forth in [the Judicial Code]. This subsection shall not be interpreted to exclude bankruptcy judges . . . from its operation.


272. Another analysis of bankruptcy jurisdiction to enjoin non-debtor actions can be found in Howard C. Buschman III & Sean P. Madden, The Power and Propriety of Bankruptcy Court Intervention in Actions Between Nondebtors, 47 BUS. LAW. 913 (1992).
The traditional powers of a federal court to enjoin collateral litigation that would interfere with the court’s jurisdiction, frequently relied upon as support for permanent non-debtor releases and injunctions, cannot sustain this exceptional exercise of injunctive powers.\textsuperscript{273} It can only be defended based upon the unique character of jurisdiction over bankruptcy reorganization proceedings. The Supreme Court recently spoke to the jurisdictional issue in the context of a temporary non-debtor stay in the case of \textit{Celotex Corp. v. Edwards}.\textsuperscript{274} Unfortunately, the \textit{Celotex} opinion did not clarify the most important jurisdictional questions, especially those surrounding permanent non-debtor releases.

A complete understanding of any bankruptcy jurisdictional issue requires some background in the rich history of bankruptcy jurisdiction, and this is especially true with respect to bankruptcy injunctions. History reveals that wide-ranging status quo injunctions have always been integral to the administration of bankruptcy estates, especially in bankruptcy reorganization proceedings.\textsuperscript{275} Temporary non-debtor stays narrowly tailored to promote a Chapter 11 debtor’s attempts to successfully reorganize are fully consistent with these historical injunctive powers. Permanent non-debtor releases and injunctions, however, go well beyond the traditional status quo injunction; in the name of promoting the debtor’s successful reorganization, they extinguish obligations of non-debtors that historically have been completely beyond the reach of bankruptcy jurisdiction.\textsuperscript{276}

Expansion of federal bankruptcy jurisdiction, with the advent of the Bankruptcy Reform Act of 1978,\textsuperscript{277} removed courts’ unwarranted misgivings about the propriety of temporary non-debtor stays.\textsuperscript{278} To the extent courts perceive this expanded bankruptcy jurisdiction as somehow sanctioning permanent non-debtor releases, however, the reversal in judicial attitude has gone too far. Loose usage of jurisdictional terminology has blurred critical jurisdictional distinctions to a point where bankruptcy courts use permanent non-debtor releases and injunctions to expunge non-debtor rights that they could not directly adjudicate.\textsuperscript{279} Moreover, confusion concerning jurisdiction to enjoin non-debtor actions has led the courts to overlook Supreme Court precedent under the 1898 Act striking down a permanent non-debtor injunction.\textsuperscript{280} A proper understanding of the reach of bankruptcy courts’ jurisdiction and accompanying injunctive powers leads to the conclusion that non-debtor releases are not an appropriate ex-

\textsuperscript{273} See infra Part IV.A.
\textsuperscript{274} 514 U.S. 300 (1995), discussed infra Part IV.D, IV.F.
\textsuperscript{275} See infra Part IV.B.
\textsuperscript{276} See infra Part IV.C.
\textsuperscript{277} Pub. L. No. 95-598, 92 Stat. 2549.
\textsuperscript{278} See infra Part IV.D, IV.F.
\textsuperscript{279} See infra Part IV.E, IV.G.1.
tension of the historical injunctive powers of federal bankruptcy courts. The courts have no jurisdictional authority to approve non-consensual non-debtor releases in the absence of express congressional authorization.

A. Injunctions in Aid of Jurisdiction

Courts rely upon section 105(a) of the Bankruptcy Code for authority to approve non-debtor releases. That section provides that "[t]he court may issue any order, process or judgment that is necessary or appropriate to carry out the provisions of" the Bankruptcy Code. This provision, like its predecessor under the 1898 Act, gives to federal bankruptcy courts the powers of courts of equity granted to all federal courts in the All Writs Act. The All Writs Act provides that "all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdictions," which includes writs of injunction. 284

282.
284. See 9 Moore, supra note 60, ¶ 110.29, at 359. With respect to enjoining state court proceedings, federal courts operate under the strictures of the Anti-Injunction Act, which provides that "[a] court of the United States may not grant an injunction to stay proceedings in a State court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments." 28 U.S.C. § 2283 (emphasis added). Bankruptcy Code § 105 is an "expressly authorized" exception to the Anti-Injunction Act, permitting federal bankruptcy courts to enjoin state court proceedings. H.R. REP. NO. 95-595, at 317 ("This section [105] is also an authorization, as required under 28 U.S.C. § 2283, for a court of the United States to stay the action of a State court."). reprinted in 1978 U.S.C.C.A.N. at 6274; see also S. REP. NO. 95-989, at 29 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5815. Bankruptcy injunctions were the first explicit exception to the Anti-Injunction Act, added in 1874 to except "cases where such injunction may be authorized by any law relating to proceedings in bankruptcy." 17 CHARLES A. WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 4221, at 497 & n.6 (2d ed. 1988) (quoting section 720 of former Revised Statutes); see also Toucey v. New York Life Ins. Co., 314 U.S. 118, 132-33 (1941). Before the 1874 bankruptcy exception to the Anti-Injunction Act, there were inconsistent pronouncements from the Supreme Court regarding the ability of a federal bankruptcy court to enjoin state court proceedings. Compare Ex parte Christy, 44 U.S. (3 How.) 292, 318 (1845) (Story, J.) ("We entertain no doubt that, under the provisions of the [Bankruptcy Act of 1841], the District Court does possess full jurisdiction to suspend or control such proceedings in the state courts."), with Peck v. Jenness, 48 U.S. (7 How.) 612, 626, 625 (1849) (holding, without citing Ex parte Christy, that the Bankruptcy Act of 1841 "confers no authority on the District Court to restrain proceedings [in state court] by injunction or any other process," citing the Anti-Injunction Act). When the Anti-Injunction Act was amended after the Toucey decision, the specific bankruptcy exception was removed and replaced with a general exception for any injunction expressly authorized by another federal statute. See 28 U.S.C. § 2283 note (historical and revision notes).

Even though Bankruptcy Code § 105 is an "expressly authorized" exception to the Anti-Injunction Act, courts give similar constructions to the parallel "in aid of jurisdiction" language
One of the most enigmatic arguments advanced to justify non-debtor releases is an "in aid of jurisdiction" argument dubbed the "channeling" rationale.\textsuperscript{285} Both the \textit{Robins} and \textit{Drexel} courts characterized the non-debtor releases they approved as appropriate "channeling" injunctions,\textsuperscript{286} obviously alluding to a discussion in the \textit{Manville} confirmation opinion that coined the phrase "equitable channeling injunctions."\textsuperscript{287} The so-called channeling in the \textit{Robins} and \textit{Drexel} cases was related to the fact that many released parties made contributions of various types to the debtor's reorganization, creating a bigger reorganization pot for creditors.\textsuperscript{288} Through the non-debtor releases, then, creditor claims were supposedly "channeled" away from the released parties and into the now-bigger reorganization pot. The superficial appeal of the channeling rationale is such that it has become common to rationalize non-debtor releases as equitable channeling injunctions\textsuperscript{289}—without a genuine understanding of what an equitable channeling injunction is, and why non-debtor releases are \textit{not} a proper exercise of equitable channeling powers.

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\textsuperscript{285} \textit{See}, e.g., \textit{In re Forty-Eight Insulations, Inc.}, 133 B.R. 973, 976 (Bankr. N.D. Ill. 1991) ("[Debtor] suggests that [creditor's] rights will be protected because [creditor's non-debtor] claims . . . will be channeled to [Debtor's] estate. What exactly that means, however, is not clear."). aff'd, 149 B.R. 860 (N.D. Ill. 1992).

\textsuperscript{286} \textit{In re A.H. Robins Co.}, 88 B.R. 742, 753, 754 (E.D. Va. 1988) (characterizing non-debtor releases and injunctions as "channeling provisions" and stating that "[t]he Court has the equitable and inherent power and authority to channel claims to a specific res"), aff'd \textit{sub nom.} Menard-Sanford v. Mabe (\textit{In re A.H. Robins Co.}), 880 F.2d 694 (4th Cir. 1989); \textit{In re Drexel Burnham Lambert Group, Inc.}, 138 B.R. 723, 754, 772-73 (Bankr. S.D.N.Y. 1992) ("Release and Injunction Provisions effectively channel the Debtor's recoveries . . . into a fund or pool from which claims arising from Drexel's activities and business can be satisfied," "while preserving, increasing, andrationally providing for claimants through the [Release and Injunction] provisions of the Plan that channel recoveries into identifiable funds.").


\textsuperscript{288} \textit{See supra} notes 76, 120, 124, 139, and accompanying text.

\textsuperscript{289} For instance, the Fifth Circuit, in discussing non-debtor releases in prior cases, stated: "In those cases, however, the courts upheld permanent injunctions of third-party claims because while the injunction permanently enjoined the lawsuits, it also channeled those claims to allow recovery from separate assets and thereby avoided discharging the non-debtor." \textit{Feld v. Zale Corp.} (\textit{In re Zale Corp.}), 62 F.3d 746, 760 (5th Cir. 1995). The recent Bankruptcy Review Commission's proposals risk perpetuating the mischief associated with so-called channeling injunctions by recommending that "[s]ection 524 should authorize courts to issue channeling injunctions." \textbf{National Bankr. Review Comm'n, supra} note 22, at 345.
The *Manville* discussion of equitable channeling injunctions centered around the power of a court to effectuate the sale of an asset free and clear of liens on the asset.\(^{290}\) Such a free-and-clear sale effectively enjoins lien claimants from further pursuit of that asset and channels lien claims to the proceeds of the sale for satisfaction from those proceeds.\(^{291}\) The Supreme Court has explained this injunctive power as one rooted in notions of in rem jurisdiction:

This is but an application of the well recognized rule that when a court of competent jurisdiction takes possession of property through its officers, this withdraws the property from the jurisdiction of all other courts which, though of concurrent jurisdiction, may not disturb that possession; and that the court originally acquiring jurisdiction is competent to hear and determine all questions respecting title, possession and control of that property.\(^{292}\)

This concept of exclusive jurisdiction applies to an in rem or quasi in rem action to the extent that possession or control of property is necessary for effective relief.\(^{293}\) When a court exercises such exclusive in rem jurisdiction, "[t]o protect its jurisdiction, that court may issue an injunction."\(^{294}\)

The general power to prevent interference with exclusive in rem jurisdiction over property by enjoining collateral proceedings is limited to enjoining other in rem actions against that same property.\(^{295}\) In this way, any such claim against the property can be channeled to the court with exclusive in rem jurisdiction over the property. Equitable channeling of all in rem claims to the court with exclusive jurisdiction over the property in no way prejudices the channeled claims; it simply assures orderly resolution of all conflicting claims to the property. A collateral in personam suit, though, does not interfere with a court’s exclusive in rem control of property. An in personam suit will not establish a plaintiff’s claim to any specific property interest, but

\(^{290}\) See *Johns-Manville*, 68 B.R. at 625.

\(^{291}\) The power of a bankruptcy court to effectuate sale of a debtor's property free and clear of liens, with the liens attaching to the proceeds of the sale, is now codified. See 11 U.S.C. § 363(e)-(f) (1994).


\(^{293}\) See *Penn Gen. Cas. Co. v. Pennsylvania ex rel. Schnader*, 294 U.S. 189, 195 (1935). This jurisdiction would include proceedings to "enforce liens against specific property, to marshall assets, administer trusts, or liquidate insolvent estates," *Kline v. Burke Constr. Co.*, 260 U.S. 226, 231 (1922), and the common-law precursor to modern bankruptcy reorganization proceedings, "suits in equity for the control by receivership of the assets of an insolvent corporation." *Penn Gen. Cas.*, 294 U.S. at 195. On equitable receivership proceedings, see generally 6 *COLLIERS* (14th ed. 1978), *supra* note 46, ¶ 0.04. The transition from common-law equitable receivership proceedings to statutory bankruptcy reorganization proceedings is traced in 6 id. ¶ 0.05; *Aaron, supra* note 128, § 1.15; *Korobkin, Rehabilitating Values, supra* note 196, at 744-55; *Markell, Absolute Priority, supra* note 111, at 74-87.

\(^{294}\) *Ex parte Baldwin*, 291 U.S. 610, 615 (1934). This in rem injunctive power is so firmly established that it was considered an implicit exception to the Anti-Injunction Act, even before the explicit addition of the "in aid of jurisdiction" exception. See *Toucey v. New York Life Ins. Co.*, 314 U.S. 118, 134-36 (1941).

\(^{295}\) See *Penn Gen. Cas.*, 294 U.S. at 195.
will merely determine the defendant's personal obligations to the plaintiff, irrespective of what assets might be available to satisfy those obligations.\textsuperscript{296} Exclusive in rem jurisdiction, therefore, is not a basis on which to enjoin collateral in personam actions.\textsuperscript{297}

Federal bankruptcy courts possess the in rem "exclusive jurisdiction of all of the property, wherever located, of the debtor as of the commencement of" the bankruptcy case.\textsuperscript{298} Nonetheless, the essence of a non-debtor release is that it forever bars any action against a non-debtor based on the non-debtor's personal liability to creditors—in personam actions that in no way encroach upon the bankruptcy court's exclusive in rem jurisdiction over the debtor's property. Extinguishing these in personam actions, therefore, cannot be justified by "the equitable and inherent power to channel claims to a specific res,"\textsuperscript{299} not even by analogy. Applying the channeling rationale to non-debtor releases takes a mechanism designed to preserve, consolidate, and resolve all in rem claims and transforms it into a mechanism that forcibly converts creditors' in personam claims against a non-debtor into in rem claims against the debtor's property. In the process, those in personam rights against the non-debtor are extinguished, without any assurance that the substituted in rem rights against the debtor's property are the equivalent of the extinguished in personam rights.\textsuperscript{300} This drastic alteration of in personam claims against a non-debtor, in the guise of merely protecting the bankruptcy court's exclusive in rem jurisdiction over the debtor's property, is not a proper exercise of traditional in rem channeling powers.\textsuperscript{301}

\textsuperscript{296} See Kline v. Burke Constr. Co., 260 U.S. at 230 (stating that "a controversy is not a thing, and a controversy over a mere question of personal liability does not involve the possession or control of a thing"). Indeed, in the equitable receivership context, mere liquidation of a claim against the debtor by reduction to judgment (as opposed to collection of the claim) in collateral proceedings was not considered an action that impaired the exclusive in rem jurisdiction of the federal receivership court. See Riehle v. Margolies, 279 U.S. 218, 223-25 (1929).

\textsuperscript{297} See, e.g., United States v. Ford Motor Co., 522 F.2d 962, 965 (6th Cir. 1975); Signal Properties, Inc. v. Farha, 482 F.2d 1136, 1136-37 (5th Cir. 1973); Hyde Constr. Co. v. Koehring Co., 388 F.2d 501, 508-09 (10th Cir. 1968); Hemmerick v. Chrysler Corp., 769 F. Supp. 525, 531-32 (S.D.N.Y.), aff'd mem., 952 F.2d 393 (2d Cir. 1991); cf. State Farm Fire & Cas. Co. v. Tashire, 386 U.S. 523, 533-37 (1967) (holding that federal statutory interpleader proceedings initiated by insurer to resolve all claims to insurance "fund" could not support enjoining collateral in personam suits by injured parties against insured and co-defendants).


\textsuperscript{301} The Fourth Circuit, in affirming the Robins non-debtor releases, floated another inapposite analogy—the "ancient but very much alive" equitable doctrine of marshaling of assets. Robins, 880 F.2d at 701. The marshaling analogy, however, fails on roughly the same grounds as the channeling analogy. "The equitable doctrine of marshaling rests upon the principle that a creditor having two funds to satisfy his debt, may not by his application of them to his demand, defeat another creditor, who may resort to only one of the funds." Sowell v. Federal Reserve Bank, 268 U.S. 449, 456-57 (1925). By the doctrine of marshaling, the equity court can, by way
Moreover, non-debtor releases cannot be considered an appropriate corollary to a federal bankruptcy court's in personam jurisdiction under conventional standards for "in aid of jurisdiction" injunctions. An elemental and unique attribute of a non-debtor release is that it precludes collateral litigation of in personam non-debtor claims that the bankruptcy court has not and will not attempt to adjudicate or resolve in any manner whatsoever. The so-called channeling of a non-debtor claim to the debtor's estate does not mean that the creditor now has two claims against the debtor's estate—one for its rights against the debtor and one for its channeled rights against the non-debtor. Through the channeling sleight of hand, the court completely extinguishes the claim against the non-debtor and leaves the creditor with only its claim against the debtor's estate, without even purporting to address the merits of the released non-debtor claim. This sort of channeling is unknown to general "in aid of jurisdiction" jurisprudence.

In those cases in which federal courts have addressed enjoining collateral in personam litigation in order to protect their own in per-

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302. See, e.g., LTV Corp. v. Aetna Cas. & Sur. Co. (In re Chateaugay Corp.), 167 B.R. 776, 781, 780-82 (S.D.N.Y. 1994) (noting that the bankruptcy court below, in approving a non-debtor release over creditors' objection, had stated that the creditors' non-debtor suit "is not before me and I am not prepared to pass on the merits of it," yet remanding for determination of whether the non-debtor release was nonetheless permissible as "essential" to the debtor's reorganization).
sonam jurisdiction, they have made it clear that, as the Supreme Court put it, "nonexistent jurisdiction . . . cannot be aided." The only proper use of this power is by an "injunction in aid of any jurisdiction which has been invoked and is being exercised." Thus, federal courts will not enjoin collateral proceedings with respect to claims and issues that are not before the federal court for resolution, and this is especially true when the collateral proceedings involve persons

303. Although injunctions in aid of in rem jurisdiction are firmly established in the federal courts, the courts have been much more hesitant to enjoin collateral proceedings in aid of their in personam jurisdiction, with the general rule being: "Where the judgment sought is strictly in personam, . . . both a state court and a federal court having concurrent jurisdiction may proceed with the litigation . . . ." Penn Gen. Cas. Co. v. Pennsylvania ex rel. Schnader, 294 U.S. 189, 195 (1935). Only recently have the federal courts begun chipping away at this rule, enjoining collateral proceedings that would interfere with their in personam jurisdiction over school desegregation cases, Voting Rights Act cases, and complex class actions. See generally 1A, pt.2 MOORE, supra note 60, ¶ 0.209[2], at 2339-40 (2d ed. 1996 & Supp. 1996-97); 17 WRIGHT ET AL., supra note 284, § 4225, at 531-33 (2d ed. 1988 & Supp. 1997).


305. Jos. L. Muscarelle, Inc. v. Central Iron Mfg. Co., 328 F.2d 791, 794 (3d Cir. 1964); see also 1A, pt.2 MOORE, supra note 60, ¶ 0.209[2], at 2337 ("The Richman case in no way impairs the power of a federal court to enjoin state proceedings where necessary in aid of jurisdiction which it properly has and is exercising."). Commentators have advocated abandonment of the in rem/in personam gloss the Court has placed on the "in aid of jurisdiction" provisions of the injunction statutes, with a correspondingly larger role for injunctions in aid of a federal court's in personam jurisdiction. E.g., William T. Mayton, Ersatz Federalism Under the Anti-Injunction Statute, 78 COLUM. L. REV. 330, 354-70 (1978); Edward F. Sherman, Class Actions and Duplicative Litigation, 62 IND. L.J. 507, 531-32, 548-49 (1987). This approach, however, does not go so far as to lose the "in aid of" injunction from the jurisdictional anchor of an existing federal action. See, e.g., MARTIN H. REDISH, FEDERAL JURISDICTION: TENSIONS IN THE ALLOCATION OF JUDICIAL POWER 335 (2d ed. 1990) (advocating revised interpretation of "in aid of jurisdiction" injunctions, but noting that such injunctions cannot be used if the sole claim in the federal court is the prayer for a suit injunction, for in those circumstances the federal court has no preexisting jurisdiction to aid"). The American Law Institute has proposed a novel system for massive consolidation of complex litigation that would include a broad federal injunctive power with respect to collateral litigation. See AMERICAN LAW INST., supra note 48, § 5.04. Still, this proposal makes clear that such "[a]n injunction should be used against those cases that are truly duplicative, and not those only tangentially related," and "the mere existence of a consolidated proceeding cannot justify intrusions on . . . parties' rights that go beyond what is necessary to promote the efficient handling of the cases being litigated in the magnet forum." Id. § 5.04, reporter's note 11 to cmt. d, at 274.

306. See, e.g., Atlantic Coast Line R.R. Co. v. Brotherhood of Locomotive Eng'rs, 398 U.S. 281, 294-96 (1970) (holding that restraint of a collateral suit on state-law claims was not in aid of jurisdiction of federal suit addressing only federal claims, because "it is not enough that the requested injunction is related to that jurisdiction"); United States v. International Bhd. of Teamsters, 907 F.2d 277, 279-80 (2d Cir. 1990) (upholding injunction that merely channeled all litigation concerning consent decree into federal court with jurisdiction over implementation of consent decree); In re Baldwin-United Corp., 770 F.2d 328, 334, 336-37, 339 (2d Cir. 1985) (upholding an injunction in aid of class action that would not extend to any action that does not affect the rights of members of plaintiff class in pending class action); Alton Box Bd. Co. v. Espirit De Corp., 682 F.2d 1267, 1271 & n.7 (9th Cir. 1982) (holding that an injunction in aid of class action could not enjoin parties from pursuing claims not part of federal class action). Foreshadowing arguments in support of non-debtor stays and releases in bankruptcy, the Seventh Circuit held that a risk that the distinct collateral litigation will destroy a plaintiff's financial ability to continue its federal suit is not an appropriate basis on which to stay the collateral suit in aid of the federal court's jurisdiction. See Kurek v. Pleasure Driveway & Park Dist., 574 F.2d 892, 896 (7th Cir.), vacated and remanded on other grounds, 435 U.S. 992 (1978).
not parties to the federal court adjudication. 307 Thus, whatever jurisdiction a bankruptcy court might exercise in resolving creditors' claims against the debtor provides no basis for an “in aid of jurisdiction” injunction that extinguishes collateral claims against a non-debtor that the bankruptcy court will not address. 308 As with the in rem channeling argument, this perverts the function of the “in aid of jurisdiction” injunction as a device to channel identical or duplicitious claims into one forum for efficient resolution. 309 Non-debtor releases

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307. See, e.g., Carlough v. Amchem Prods., Inc., 10 F.3d 189, 203-04 (3d Cir. 1993) (holding that an injunction in aid of jurisdiction over a class action would not apply to opt-out plaintiffs); White Mountain Apache Tribe v. Smith Plumbing Co., 856 F.2d 1301, 1306 (9th Cir. 1988) (holding that a collateral suit against contractor's surety could not be enjoined in aid of jurisdiction of the federal court entertaining an underlying contract dispute); St. Paul Fire & Marine Ins. Co. v. Lack, 443 F.2d 404, 405-07 (4th Cir. 1971) (holding that a collateral suit by the injured party against the insured could not be enjoined in aid of jurisdiction of a federal insurance coverage suit between the insurer and the insured); Pacific Indem. Co. v. Acel Delivery Serv., Inc., 432 F.2d 952, 954-56 (5th Cir. 1970) (same); Jos. L. Muscarelle, Inc. v. Central Iron Mfg. Co., 328 F.2d 791, 793-94 (3d Cir. 1964) (holding that subcontractors' lien suits against owner could not be enjoined in aid of jurisdiction of a federal suit between a general contractor and subcontractors); Safeco Ins. Co. of Am. v. Norris & Hirshberg, Inc., 640 F. Supp. 712, 715-16 (N.D. Ga. 1986) (holding that a collateral suit by the injured party against the insured could not be enjoined in aid of jurisdiction of a federal insurance coverage suit between the insurer and the insured).

308. This conclusion is bolstered by consideration of the third exception to the Anti-Injunction Act, for a federal court injunction “to protect or effectuate its judgments.” 28 U.S.C. § 2283 (1994). The Supreme Court has said that the “necessary in aid of jurisdiction” phrase “implies something similar to the concept of injunctions to ‘protect or effectuate’ judgments.” Atlantic Coast Line, 398 U.S. at 295. The “protect or effectuate judgments” exception is commonly known as the relitigation exception, and “an essential prerequisite for applying the relitigation exception is that the claims or issues which the federal injunction insulates from litigation in state proceedings actually have been decided by the federal court.” Chick Kam Choo v. Exxon Corp., 486 U.S. 140, 148 (1988). Thus, in the prejudgment phase of litigation, “in aid of jurisdiction” can be thought of as restricted to claims or issues that actually have been placed before the federal court for resolution. Learned Hand applied these principles to a non-debtor injunction in reorganization proceedings under the 1898 Act, saying that “since this stay is permanent, and not merely to give the debtor or the trustee a chance so to intervene, it can be defended only in case the [non-debtor action] may eventually fall within the jurisdiction in invitum of the bankruptcy court, and also in case the state suit will interfere with that power.” Radin v. Chemical Bank & Trust Co. (In re Prudence Bonds Corp.), 75 F.2d 262, 263 (2d Cir. 1935). In the context of a bankruptcy sale under the 1898 Act, where the court approved a sale of the debtor's property subject to the interests of claimants to that property (without adjudicating those interests), the Ninth Circuit held that the bankruptcy court could not permanently enjoin a subsequent state court suit by the claimants to determine their interests in the property. See McQuaid v. Owners of NW 20 Real Estate (In re Federal Shopping Way, Inc.), 717 F.2d 1264, 1266-69 (9th Cir. 1983). The injunction could not be one to protect or effectuate a bankruptcy court judgment, because the bankruptcy court never addressed the claimants' interests in the property. See id. at 1269-73. Moreover, because the bankruptcy court no longer had jurisdiction to adjudicate the claimants' interests in the property, the injunction could not be in aid of the bankruptcy court's jurisdiction, in spite of various claims that the collateral suit would somehow interfere with administration of the bankruptcy estate. See id. at 1273-75.

309. Interestingly, like the modern class action, see supra note 57, the historical antecedent of the modern-day “in aid of jurisdiction” injunction is the equitable bill of peace, “which enabled a single party facing a multitude of independent yet related claims to compel all claimants to bring suit in a single court of equity.” American Law Inst., supra note 48, § 5.04, reporter's note 2 to cmt. a, at 267. With respect to its stay of actions against the debtor, bankruptcy's automatic stay functions as such a channeling injunction—channeling all claims against the debtor into the bankruptcy court for efficient, centralized resolution, rather than allowing piece-
improperly convert the procedural channeling injunction into a tool for summarily expunging creditors' substantive in personam rights against non-debtors.

Settled principles regarding federal "in aid of jurisdiction" injunctions refute the contention that non-debtor releases are a perfectly acceptable exercise of channeling powers. In fact, even temporary non-debtor stays are beyond the traditional channeling powers of federal courts to the extent that the stay promotes something other than a bankruptcy court's resolution of the non-debtor dispute—namely, the debtor's successful reorganization.310 Thus, any validity of non-debtor stays and releases must rest upon unique aspects of bankruptcy jurisdiction and "any powers traditionally exercised by a bankruptcy court that are not encompassed by the All Writs Statute."311

B. Summary Jurisdiction to Enjoin Under the Bankruptcy Act of 1898

Bankruptcy courts' powers to enjoin collateral litigation developed under the 1898 Act, predecessor to the current Bankruptcy Code. The injunctive powers of bankruptcy courts were codified in the 1898 Act's jurisdictional grant in section 2a(15), the statutory precursor to section 105(a) of the Bankruptcy Code.312 The contours of this injunctive jurisdiction are very instructive with respect to the

meal adjudications in various state and federal courts. See supra Part II.A; see also LoPucki, supra note 157, at 346-48; Nimmer, supra note 113, at 1016.

310. In the equitable receivership context, the Tenth Circuit refused to permit temporary stay of a non-debtor action, requested on grounds similar to those relied upon to support temporary non-debtor stays in Chapter 11 reorganization proceedings, and emphasized that permanently enjoining the non-debtor action would never be proper, because the receivership court would not adjudicate the non-debtor action. See Commodity Futures Trading Comm'n v. Chilcott Portfolio Management, Inc., 713 F.2d 1477, 1483-86 (10th Cir. 1983); see also Greenbaum v. Lehrenkrauss Corp., 73 F.2d 285, 287 (2d Cir. 1934) (holding, in equitable receivership proceedings, that stay of suits against debtor's non-debtor subsidiaries and affiliates was improper, "and the present case permits us definitely to repudiate the idea that, because it may be convenient for all persons interested to have a single reorganization of the receivership defendant and all its subsidiaries, this can be accomplished by merely filing a bill in equity against the parent corporation").


[C]ourts of bankruptcy . . . are hereby invested . . . with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act . . . to—

. . .

(15) Make such orders, issue such process, and enter such judgments, in addition to those specifically provided for, as may be necessary for the enforcement of the provisions of this Act: Provided, however, That an injunction to restrain a court may be issued by the [district court] judge only[.]

1898 Act § 2a(15), reprinted in 1 Collier (14th ed. 1974), supra note 46, at 131, 134. Under bankruptcy statutes predating the 1898 Act, injunctive powers were implicit in grants of equity jurisdiction over "all matters and proceedings in bankruptcy." See Babbitt v. Dutcher, 216 U.S. 102, 105-08 (1910) (stating that section 2 of the 1898 Act, including section 2a(15), granted jurisdiction substantially identical to jurisdiction under the Bankruptcy Acts of 1841 and 1867 over
modern jurisdictional issues with which the Supreme Court recently wrestled in *Celotex Corp. v. Edwards*, including questions as to the appropriate division of jurisdictional authority between federal district courts and their adjunct bankruptcy courts. Under the 1898 Act, because of a recognized distinction between jurisdiction to enjoin and jurisdiction to adjudicate, courts presiding over bankruptcy proceedings could enjoin collateral disputes of all kinds through summary proceedings—even disputes beyond bankruptcy jurisdiction to adjudicate through summary proceedings.

Jurisdiction under the 1898 Act was essentially in rem jurisdiction over property in the actual or constructive possession of the court and proceedings to administer that property for the benefit of creditors. This in rem jurisdiction to administer property in the possession of the court was commonly denoted summary jurisdiction. The summary jurisdiction label was a useful convention not only to distinguish summary in rem jurisdiction from in personam jurisdiction over individual parties to a dispute (known as plenary jurisdiction), but also to accurately describe the more informal procedures used in summary matters.

Of course, a debtor’s property often included things not within the possession of the court, such as a disputed cause of action against a third party or tangible property held under a substantial claim of right by a third party, a so-called adverse claimant. A federal bankruptcy court had no summary jurisdiction to adjudicate disputes with

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315. *See 2 Collier* (14th ed. 1976), *supra* note 46, ¶ 23.02[1]. A plenary suit was an ordinary civil action conducted according to normal rules of civil procedure, including summons and complaint, formal pleadings, discovery and trial, all according to the timetables for a normal civil action. Summary proceedings, by contrast and as the name indicates, were much less formal and more expeditious, initiated by a motion or petition, with a relatively short notice period before a hearing, where the evidence would often be presented through affidavits. *See generally 2 id. ¶ 23.02[2]. With respect to the procedural differences, the summary/plenary distinction roughly corresponds to the current distinction in bankruptcy proceedings between adversary proceedings, largely conducted according to the Federal Rules of Civil Procedure, and contested matters, initiated by motion contemplating a hearing. *See Fed. R. Bankr. P.* pt. VII (defining matters that constitute adversary proceedings; incorporating and modifying Federal Rules of Civil Procedure); Fed. R. Bankr. P. 9014 & advisory committee note (all proceedings that are not adversary proceedings are contested matters conducted by motion and hearing). *See generally John* Silas Hopkins, *III, The Bankruptcy Litigator’s Handbook* chs. 16-18 (1993).

316. *See 2 Collier* (14th ed. 1976), *supra* note 46, ¶¶ 23.05[3], at 480-83, 23.05[4], 23.06[1], at 494.
adverse claimants. Such a dispute could be resolved only by an ordinary civil action (a plenary suit), and the 1898 Act conferred very little plenary bankruptcy jurisdiction on the federal courts. By and large, a trustee or receiver could bring a plenary suit only in a state or federal court that would have independent jurisdiction over the action, without regard to the pending bankruptcy proceedings. Federal bankruptcy jurisdiction under the 1898 Act, then, was largely summary in rem jurisdiction, with only limited plenary jurisdiction over in personam actions between adverse claimants.

The 1898 Act vested federal bankruptcy jurisdiction over both summary and plenary proceedings in the first instance in the U.S. district courts, sitting as "courts of bankruptcy." However, adjuncts to the district courts, entitled bankruptcy referees, were authorized to exercise most of the district court's summary jurisdiction through a referral system. Nonetheless, a referee's jurisdiction over proceedings in referred cases was limited, not only by some specific exceptions in the 1898 Act itself, but also by an interpretation of the 1898 Act that limited a referee to the exercise of summary jurisdiction. A referee had no jurisdiction over plenary matters, but the referee's

317. See 2 id. ¶ 23.06[1], at 494-95.
318. Thus, while section 2a(7) of the 1898 Act gave federal courts jurisdiction to "cause the estates of bankrupts to be collected . . . and determine controversies in relation thereto," the scope of this jurisdiction was restricted by the proviso "except as herein otherwise provided." 1898 Act § 2a(7), reprinted in 1 COLLIER (14th ed. 1974), supra note 46, at 133. Section 23 of the 1898 Act provided otherwise with respect to plenary suits, giving the federal courts jurisdiction only "in the same manner and to the same extent as though such [bankruptcy] proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants." 1898 Act § 23a, reprinted in 2 COLLIER (14th ed. 1976), supra note 46, at 431. See generally 2 COLLIER (14th ed. 1976), supra note 46, ¶ 23.12. The primary exceptions were federal jurisdiction by consent and federal plenary jurisdiction over suits to avoid liens and recover preferences and fraudulent conveyances. See generally 2 id. ¶¶ 23.08, 23.14, 23.15. In addition, section 23 did not apply to restrict plenary jurisdiction in corporate reorganization proceedings under Chapter X. See Williams v. Austrian, 331 U.S. 642, 661-62 (1947). See generally 6 COLLIER (14th ed. 1978), supra note 46, ¶ 3.18.
319. See 1898 Act § 1(10) (district courts are "courts of bankruptcy"), and id. § 2a ("[C]ourts of bankruptcy . . . are hereby invested . . . with . . . original jurisdiction in proceedings under this Act."), reprinted in 1 COLLIER (14th ed. 1974), supra note 46, at 43, 131.
320. Referees were officers of the district court, appointed by the district court judges for terms of six years. See 1898 Act §§ 33, 34a, reprinted in 2A COLLIER (14th ed. 1978), supra note 46, at 1331, 1341.
321. When a bankruptcy case was referred to a referee, the 1898 Act gave referees "jurisdiction to . . . perform such of the duties as are by this Act conferred on courts of bankruptcy . . . except as herein otherwise provided." 1898 Act § 38(6), reprinted in 2A COLLIER (14th ed. 1978), supra note 46, at 1391. In addition, the 1898 Act contained a definition of "court" that included both the district court and the referee, making clear that in referred cases, the referee acted as the court. See 1898 Act § 1(10) (definition of "court"), and id. § 1(20) (definition of "judge"), and id. § 1(26) (definition of "referee"), reprinted in 1 COLLIER (14th ed. 1974), supra note 46, at 43, 44.1; see also White v. Schloerb, 178 U.S. 542, 546 (1900) (stating that when a "case in bankruptcy is referred by the court of bankruptcy to a referee, . . . he exercises much of the judicial authority of that court"). In many cases, rules provided for automatic reference to the referee. See 2 COLLIER (14th ed. 1976), supra note 46, ¶ 22.03.
322. See Weidhorn v. Levy, 253 U.S. 268, 274 (1920). The only exception was that the parties could consent to summary proceedings before the referee. See MacDonald v. Plymouth.
summary jurisdiction was indistinguishable from that of the district court, including the power to enter orders reviewable only by appeal\(^{323}\) and carrying the full collateral preclusiveness of res judicata.\(^{324}\)

Injunctive orders pursuant to section 2a(15) were a matter so closely tied to administration of the bankruptcy estate that they could issue in summary proceedings.\(^{325}\) Early cases involved injunctions concerning property deemed within the possession of the court; therefore, summary in rem jurisdiction to protect that possession by injunctive order was quite unexceptional.\(^{326}\) The scope of summary jurisdiction to issue section 2a(15) injunctions, though, extended well beyond property in the possession of the court, as illustrated by the seminal case on the injunctive powers of federal bankruptcy courts, *Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Railway Co.*\(^{327}\)

In that case, those companies comprising the Chicago, Rock Island railway system were undergoing a reorganization pursuant to the railroad reorganization provisions of the 1898 Act.\(^{328}\) Various banks that had loaned money to the debtors held marketable securities issued by the debtors as collateral for the loans. These securities were, in turn, secured by liens on the debtors' property.\(^{329}\) The district court presiding over the reorganization proceedings, fearing that release of the securities into the marketplace would unduly complicate the debtors' task of formulating a reorganization plan, temporarily enjoined the banks from disposing of the pledged securities, through summary

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325. Indeed, in what has been described as a chain of decisions affirming and reaffirming general principles of summary jurisdiction, the first, White v. Schoerb, 178 U.S. 542 (1900), addressed an injunctive order issued under the authority of section 2a(15). See 2 Collier (14th ed. 1976), supra note 46, ¶ 23.04[2], at 453-56 (citing White v. Schoerb).

326. In White v. Schoerb, the district court, through summary proceedings, issued an order restraining disposition and directing return of goods seized by replevin after they were deemed to pass into the constructive possession of the court through the debtors' bankruptcy filing, and the Supreme Court held that the district court's order properly issued in summary proceedings. See 178 U.S. at 542-48. The Court subsequently held that a referee also had summary jurisdiction to order turnover of property in the constructive possession of the court. See Mueller v. Nugent, 184 U.S. 1, 4, 11-18 (1902).

327. 294 U.S. 648 (1935).

328. 1898 Act § 77, reprinted in 5 Collier (14th ed. 1978), supra note 46, at 431-68.

329. See 294 U.S. at 656-60.
proceedings. The Supreme Court, in affirming the propriety of the injunction, also rejected the banks' jurisdictional objection.

The banks claimed that because the property at issue, the pledged securities, was in their possession and not the court's, the district court had no summary jurisdiction to enjoin their disposition of the property. The Court's response to this contention is the key to deciphering the jurisdictional quandary presently facing the courts with respect to non-debtor injunctions:

[T]he claim of the [banks] in respect of their rights in the collateral security or the rank of their liens [was not] questioned by the debtor. In short, no adverse claim was brought forward by either of the parties to the controversy. The only question was in respect of the [banks'] remedy; and the sole point is as to the authority of the bankruptcy court to delay for a reasonable time an interference with the reorganization proceeding which would result from an immediate sale of the collateral.

Thus, the Court recognized and articulated a critical distinction between jurisdiction to adjudicate an underlying controversy and jurisdiction to provisionally enjoin an action that might prove harmful to the bankruptcy estate. While the former might be outside the summary jurisdiction of a bankruptcy court—for example, a proceeding challenging the validity or enforceability of the banks' liens on the collateral—the latter is a separate and distinct inquiry. The temporary injunction does not have as its purpose or effect an adjudication of any such controversy; it merely preserves the status quo.

Just two years later, the Court applied this distinction to restraint of a collateral lawsuit in Steelman v. All Continent Corp. The ultimate dispute in that case centered around more than a half million dollars in securities held by stockbrokers in Philadelphia, who held the securities for the account of the All Continent Corporation. A man named Fox had filed a bankruptcy petition in New Jersey, and in those proceedings the bankruptcy trustee was actively investigating whether the All Continent Corporation was a sham devised to shelter Fox's assets, in the hopes of bringing the corporation's assets into Fox's bankruptcy estate. In the meantime, the corporation commenced a proceeding in a federal district court in Pennsylvania to clear its pur-

330. See Continental Ill. Nat'l Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co. (In re Chicago, Rock Island & Pac. Ry. Co.), 72 F.2d 443, 447-48 n.3 (7th Cir. 1934) (setting forth findings and order of district court), aff'd, 294 U.S. 648 (1935). The district court's order was based on a finding that sale of the pledged collateral "would hinder, impede, obstruct, delay, and in effect prevent the orderly preparation and consummation of a plan of reorganization." Id. at 447 n.3. The court of appeals, in melodramatic fashion, transformed this into a finding that sale of the pledged collateral would make reorganization "impossible." Id. at 451 ("If it would be quite impossible to proceed with any reorganization."). aff'd, 294 U.S. at 664-67, 678-79.

331. See discussion infra notes 345-47 and accompanying text.
332. See 72 F.2d at 449.
333. 294 U.S. at 681.
334. 301 U.S. 278 (1937).
ported title to the securities held by the stockbrokers. In summary proceedings, the New Jersey district court presiding over Fox's bankruptcy proceedings enjoined All Continent from further prosecution of the Pennsylvania action, in order to allow the trustee to go forward with his suit against All Continent in an appropriate forum, joining all interested parties and resolving title to all of the corporation's assets, not merely the securities held in Philadelphia.

All Continent challenged the summary jurisdiction of the New Jersey court of bankruptcy to enjoin the Pennsylvania action, as the securities that were the subject of the Pennsylvania action were not in the possession of the bankruptcy court. The New Jersey bankruptcy court responded with the distinction enunciated in Continental Illinois. The injunction itself would not adjudicate the parties' adverse claims to the property, it would merely preserve the status quo pending such adjudication in a proper forum. Therefore, a summary injunctive order was entirely proper. The Supreme Court affirmed the opinion of the New Jersey district court, and in specifically addressing All Continent's jurisdictional objection the Court said, "[t]he argument misconceives the grounds upon which the trustee looks to us for aid."

Thus, the distinction between jurisdiction to adjudicate and jurisdiction to provisionally enjoin was firmly established in the 1898 Act's jurisprudence. The lower courts recognized the distinction and repeatedly invoked their summary section 2a(15) powers to enjoin actions and proceedings that could be adjudicated on the merits only through a plenary suit. These injunctions issued by orders both from district courts, sitting as "courts of bankruptcy," and from bank-

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335. See id. at 279-82. Prior to Fox's bankruptcy filing, a creditor with an unsatisfied judgment against Fox obtained a restraining order from a New York state court, preventing the brokers from releasing the securities to All Continent, on the same theory that the trustee was pursuing—that the securities really belonged to Fox. This prompted All Continent's action to quiet title to the securities. See id. at 281-82.

336. See id. at 282-84. The trustee commenced such a suit within a week. See id. at 283.


338. See 301 U.S. at 288 (“[W]e think the court of bankruptcy has been armed with abundant power to preserve the status quo until there can be an adequate trial with all the necessary parties and a judgment on the merits.”).

339. 301 U.S. at 290.

340. See, e.g., Halpert v. Engine Air Serv., Inc., 212 F.2d 860, 862-63 (2d Cir. 1954) (affirming order enjoining disposition of property pending plenary suit by trustee to recover property); Magidson v. Duggan, 180 F.2d 473, 475-77 (8th Cir. 1950) (affirming order enjoining state court suit pending plenary suit by trustee in federal court); Atlanta Flooring & Insulation Co. v. Russell, 146 F.2d 884, 889 (5th Cir. 1945) (discussing injunction of state court suit pending plenary suit by trustee); In re Standard Gas & Elec. Co., 139 F.2d 149, 153 (3d Cir. 1943) (affirming order enjoining shareholder derivative suit); Peck v. Howard, 130 F.2d 1001, 1002-03 (9th Cir. 1942) (affirming order enjoining state court water rights dispute pending determination by district court whether there were claims adverse to those of the estate); Zelenik v. Grand Riviera Theater Co., 128 F.2d 533, 537 (6th Cir. 1942) (shareholder derivative suit); In re Mitchell, 278 F. 707, 709-10 (2d Cir. 1922) (disposition of property pending plenary suit by trustee); Sproul v. Gambone, 34 F. Supp. 441, 442-43 (W.D. Pa. 1940) (same); In re Central Forging Co.,
ruptcy referees.\textsuperscript{341} For all practical purposes, a referee’s injunctive powers under section 2a(15) were coextensive with those of the district court and included jurisdiction to enjoin collateral suits that were beyond the referee’s summary jurisdiction to adjudicate.\textsuperscript{342}


\textsuperscript{341} See, e.g., Milens v. Bostian, 139 F.2d 282, 285 (8th Cir. 1943) (affirming order enjoining disposition of assets being administered in state probate proceedings pending plenary suit by trustee); Goggin v. Bolsa Chica Oil Corp. (\textit{In re Sterling}), 125 F.2d 104, 106-07 (9th Cir. 1942) (affirming order enjoining non-debtor’s improper use of its property); \textit{In re Metzger’s, Inc.}, 68 F. Supp. 663, 666-67 (W.D. Mich. 1946) (affirming order enjoining disposition of property pending plenary suit by trustee); \textit{In re Custom Shop, Inc.}, 1 F. Supp. 32, 33 (S.D.N.Y. 1932) (same); \textit{In re Wilkes}, 112 F. 975, 976-77 (E.D. Ark. 1902) (same).

\textsuperscript{342} Referees could issue such injunctions, despite the proviso in section 2a(15) “[t]hat an injunction to restrain a claim may be issued by the [district court] judge only.” \textit{1898 Act} § 2a(15), \textit{reprinted in 1 Collier} (14th ed. 1974), \textit{supra} note 46, at 134. This proviso was added by the Chandler Act of 1938. Pub. L. No. 75-696, ch. 575, 52 Stat. 840, 843 (1938). The purpose of the amendment was to make clear that referees did have the power to issue injunctions:

There has also been some question about the power of referees to issue injunctions. The weight of authority seems to be that the referees may enjoin the parties to a suit, although they are prohibited by General Order XII, clause 3, from enjoining the court itself, this power, being reserved to the judge. As a matter of actual practice, of course, injunctions are not issued to restrain the court, but to restrain the parties litigating therein. These matters should be cleared up.

H.R. Rep. No. 75-1409, at 19 (1937). \textit{See generally 1 Collier} (14th ed. 1974), \textit{supra} note 46, ¶ 2.64: A. Alan Reich, \textit{Injunctive Relief Under the Bankruptcy Act}, 19 BROOK. L. REV. 222, 222 (1953). Contemporaneously, in the bankruptcy context, the Supreme Court articulated the distinction between enjoining a court and enjoining the litigants before the court, in the \textit{All Continen-t} case, discussed \textit{supra} notes 334-39 and accompanying text: “We are unable to yield assent to the statement of the court below that ‘the restraint of a proper party is legally tantamount to the restraint of the court itself.’ The reality of the distinction has illustration in a host of cases.” Steelman v. All Continent Corp., 301 U.S. 278, 291 (1937); \textit{see also Ex parte Christy, 44 U.S. (3 How.) 292, 318 (1845) (Story, J.) (“We entertain no doubt that, under the provisions of the [Bankruptcy Act of 1841], the District Court does possess full jurisdiction to suspend or control such proceedings in the state courts, not by acting on the courts, . . . but by acting on the parties through the instrumentality of an injunction.”). Moore’s states that “as a general rule . . . the restraint of a party is not equivalent to the direct restraint of a court.” 1A, pt.2 Moore, \textit{supra} note 60, ¶ 0.208[3.—1], at 2315 (citing \textit{All Continent} and discussing Anti-Injunction Act jurisprudence as an exception to the general rule). Restraint of litigants, rather than another court, is an English doctrine devised by Sir Francis Bacon in 1616, to permit the chancery courts to enjoin proceedings in courts of law. \textit{See} Mary Brigid McManamon, \textit{Dispelling the Myths of Pendent and Ancillary Jurisdiction: The Ramifications of a Revised History}, 46 WASH. & LEE L. REV. 863, 888 n.164 (1989). Consistent with this long-standing distinction, then, courts interpreted the proviso to section 2a(15) of the 1898 Act to permit referees to enjoin parties from pursuing collateral litigation, as long as the referee did not directly restrain a court from acting. \textit{See}, e.g., Stout v. Green, 131 F.2d 995, 996, 997 (9th Cir. 1942); Seattle Curb Exch. v. Knight (\textit{In re Cochran’s Estate}), 46 F.2d 34, 36 (9th Cir. 1931), aff’g 40 F.2d 282, 284-85 (W.D. Wash. 1930); \textit{In re Roger Brown & Co.}, 196 F. 758, 762 (8th Cir. 1912) (dicta); \textit{In re Coger}, 319 F. Supp. 859, 861 (W.D. Va. 1970); \textit{Metzger’s}, 68 F. Supp. at 666-67; \textit{In re California Pea Prods., Inc.}, 37 F. Supp. 658, 662-63 (S.D. Cal. 1941); \textit{In re Lombardy Inn Co.}, 266 F. 394, 394-95 (D. Mass. 1919); \textit{In re Mustin}, 165 F. 506, 507-08 (N.D. Ala. 1910); \textit{In re Adams}, 134 F. 142, 142-43 (D. Conn. 1905); \textit{In re Martin}, 105 F. 753, 753-54 (W.D.N.Y. 1900); \textit{In re Steuer}, 104 F. 976, 980 (D. Mass. 1902) (dicta); \textit{In re Booth}, 96 F. 943, 943-44 (N.D. Ga. 1899); E.C. Ernst Int’l Corp. v. Andary (\textit{In re E.C. Ernst, Inc.}), 1 B.R. 262, 264 (Bankr. S.D.N.Y. 1979). For a case in which it was necessary
C. Non-Debtor Stays and Releases Under the Bankruptcy Act of 1898

In its *Continental Illinois* decision, the Supreme Court planted the seeds for temporary non-debtor stays in reorganization cases, but they would not fully take root until passage of the Bankruptcy Reform Act of 1978, over forty years later. Even though the reasoning of the *Continental Illinois* case would support temporary non-debtor stays, the lower courts consistently concluded that they had no jurisdiction to enjoin non-debtor actions.

While *Continental Illinois* established the distinction between jurisdiction to adjudicate and jurisdiction to enjoin, in discussing the injunctive powers of bankruptcy courts, the Court explained them as a corollary of jurisdiction to adjudicate. Although the two are not coextensive, they are inextricably intertwined:

> [C]ourts of bankruptcy . . . are essentially courts of equity, and their proceedings inherently proceedings in equity . . . . The power to issue an injunction when necessary to prevent the defeat or impairment of its jurisdiction is, therefore, inherent in a court of bankruptcy, as it is in a duly established court of equity. . . . An injunction may be issued . . . for the purpose of protecting and preserving the jurisdiction of the court "until the object of the suit is accomplished and complete justice done between the parties."  

Of course, this was merely an explication of the general "in aid of jurisdiction" powers of federal courts. In discussing the jurisdiction that a reorganization court protects and preserves by injunction, though, the Court said:

> [B]y section 2(15) of the Bankruptcy Act, courts of bankruptcy are invested with such authority in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings . . . . It may be that in an ordinary bankruptcy proceeding the issue of an injunction in the circumstances here presented would not be sustained. . . . But a [reorganization] proceeding . . . is not an ordinary proceeding in bankruptcy. It is a special proceeding which seeks only to bring about a reorganization, if a satisfactory plan to that end can be devised. And to prevent the attainment of that object is to defeat the very end the accomplishment of which was

for a federal district court, sitting as a court of bankruptcy, to directly enjoin a state court judge, see In re William E. De Lany & Co., 124 F. 280 (N.D.N.Y. 1903).


345. 294 U.S. at 675-76 (citing former version of the All Writs Act and quoting Looney v. Eastern Tex. R.R. Co., 247 U.S. 214, 221 (1918)).

346. See *supra* Part IV.A.
the sole aim of the [reorganization statute], and thereby to render its provisions futile. 347

Thus, the Court viewed section 2a(15) as a broad grant of power to enjoin actions that would interfere with the reorganization proceedings, which conceivably could include actions and suits between non-debtors. Nonetheless, the lower courts did not take the Continental Illinois rationale that far under the 1898 Act.

An oft-repeated principle under the 1898 Act was that Congress did not give federal courts jurisdiction over all controversies that are in some way related to pending bankruptcy proceedings. 348 As a general matter, the courts concluded that there was no bankruptcy jurisdiction whatsoever, neither summary nor plenary, to decide disputes between two non-debtors, even if the cause of action arose out of the parties' relationship with the debtor. 349 Of course, absence of jurisdic-

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347. 294 U.S. at 676 (citation omitted).
348. This principle is most often attributed to Callaway v. Benton, 336 U.S. 132, 142 (1949) ("There can be no question, however, that Congress did not give the bankruptcy court exclusive jurisdiction over all controversies that in some way affect the debtor's estate."). This case is discussed infra Part IV.G.2.
349. See, e.g., Uranga v. Geib (In re Paso Del Norte Oil Co.), 755 F.2d 421, 423-25 (5th Cir. 1985); Gordon v. Shirley Duke Assoc., (In re Shirley Duke Assoc.), 611 F.2d 15, 18-19 (2d Cir. 1979); First State Bank & Trust Co. v. Sand Springs State Bank, 528 F.2d 350, 353-54 (10th Cir. 1976); Richmond v. United States (In re Richmond), 456 F.2d 458, 463-65 (3d Cir. 1972); Kaplan v. Guttman, 217 F.2d 481, 484-85 (9th Cir. 1954); Evarts v. Eloy Gin Corp., 204 F.2d 712, 717 (9th Cir. 1953); Sylvan Beach, Inc. v. Koch, 140 F.2d 852, 861-62 (8th Cir. 1944); Central Hanover Bank & Trust Co. v. Kelby, 133 F.2d 873, 875-76 (2d Cir. 1943); McGrath v. Lubliner & Trinz Theatres, Inc. (In re Lubliner & Trinz Theatres, Inc.), 100 F.2d 646, 650-52 (7th Cir. 1938); Morrison v. Rockhill Improvement Co., 91 F.2d 639, 642 (10th Cir. 1937); Smith v. Chase Nat'l Bank, 84 F.2d 608, 612-16 (8th Cir. 1936); Nixon v. Michaels, 38 F.2d 420, 422-25 (8th Cir. 1930); Crocker v. Chakos (In re Chakos), 24 F.2d 482, 485 (7th Cir. 1928); Henrie v. Henderson, 145 F. 316, 319-20 (4th Cir. 1906); Brumby v. Jones, 141 F. 318, 320-23 (5th Cir. 1905).

Section 2a(6) of the 1898 Act conferred bankruptcy jurisdiction to "[b]ring in and substitute additional persons or parties in proceedings under this Act when necessary for the complete determination of a matter in controversy." 1898 Act § 2a(6), reprinted in 1 COLLIER (14th ed. 1974), supra note 46, at 133. Thus, bankruptcy courts would adjudicate a non-debtor controversy only if they thought resolution of the dispute was "necessary" to administration of the debtor's estate, with the necessity standard being "that a bankruptcy court does have jurisdiction to resolve a dispute between third parties if it is impossible to administer completely the estate of the bankrupt without determining the controversy." Uranga v. Geib, 755 F.2d at 425 (emphasis added) (quoting First State Bank, 528 F.2d at 353). Given such a stringent standard, very few non-debtor disputes were considered necessary to administration of the debtor's estate, and these generally concerned conflicting claims to ownership of the stock interests or debt obligations of the debtor. See, e.g., McGuire v. Cohen (In re Brookwood Country Club), 338 F.2d 562, 564 (7th Cir. 1964) (determining that resolution of a dispute over ownership of the reorganization debtor's stock was necessary for purposes of shareholder voting on reorganization plan); Reconstruction Fin. Corp. v. Riverview State Bank, 217 F.2d 455, 458-60 (10th Cir. 1954) (concluding that resolution of a dispute over ownership of a secured claim was necessary to creditor voting on plan of reorganization); In re International Power Sec. Corp., 170 F.2d 399, 402-06 (3d Cir. 1948) (holding that resolution of a dispute over ownership of the debtor's bonds was necessary to determine the debtor's setoff rights); In re Burton Coal Co., 126 F.2d 447, 448-49 (7th Cir. 1942) (reasoning that determination of the validity of a creditor's lien on shares of stock in the reorganization debtor was necessary to determine the validity and extent of creditors' secured and/or unsecured claims against the debtor for purposes of voting on the plan of reorganization); J. Henry Schroder Banking Corp. v. L.S. Branch Mfg. Corp. (In re Railroad Supply Co.), 78 F.2d 530, 531-33 (7th Cir. 1935) (concluding that resolution of dispute over ownership of a claim
tion to adjudicate disputes between non-debtors need not have been fatal to attempts to enjoin litigation of such disputes during reorganization proceedings. To the extent that collateral litigation between non-debtors could improperly interfere with the debtor's reorganization efforts, the rationale of Continental Illinois would seem to support bankruptcy jurisdiction to temporarily stay such suits by injunction, without regard to the court's jurisdiction to adjudicate the non-debtor action.

Lower courts, however, refused to approve even temporary stays of suits between non-debtors, reasoning primarily from their lack of bankruptcy jurisdiction to adjudicate non-debtor disputes—often emphasizing the statutory jurisdictional grant in reorganization cases over "the debtor and its property" and the fact that these non-debtor suits were not directed against the debtor or its property. When presented with an argument, à la Continental Illinois, of interference with the debtor's reorganization, the courts almost invariably concluded that any incidental effects of a non-debtor action on the debtor or its reorganization attempt were insufficient to overcome the perceived jurisdictional impediment.

against the debtor was necessary to determine the party entitled to dividends from the estate); New York Life Ins. Co. v. Irving Trust Co. (In re United Cigar Stores Co.), 75 F.2d 290, 291-92 (2d Cir. 1935) (same).

350. The various reorganization chapters under the 1898 Act all contained a nearly identical jurisdictional grant of "exclusive jurisdiction of the debtor and its property wherever located." 1898 Act § 111 (Chapter X corporate reorganizations), reprinted in 6 COLLIERS (14th ed. 1978), supra note 46, at 395; see also id. § 311 (Chapter XI arrangements), reprinted in 8 COLLIERS (14th ed. 1978), supra note 46, at 141; id. § 411 (Chapter XII real property arrangements), reprinted in 9 COLLIERS (14th ed. 1978), supra note 46, at 787; id. § 611 (Chapter XIII wage earners' plans), reprinted in 10 COLLIERS (14th ed. 1978), supra note 46, at 73. The railroad reorganization jurisdictional grant at issue in Continental Illinois was also one of "exclusive jurisdiction of the debtor and its property wherever located." 294 U.S. at 663 n.4 (quoting 1898 Act § 77(a)). Nonetheless, in its discussion of the source of the reorganization court's injunctive powers, the Supreme Court emphasized the court's jurisdiction over the debtor's reorganization, not its jurisdiction over the debtor's property. See id. at 675-76.

351. See, e.g., Amadori Constr. Co. v. Hoffenberg (In re Stanndco Developers, Inc.), 534 F.2d 1050, 1052-54 (2d Cir. 1976) (suit against debtor's surety); In re Unishops, Inc., 494 F.2d 689, 690 (2d Cir. 1974) (suit against debtor's subsidiary); United States v. Ash (In re Weissberg Corp.), 458 F.2d 975, 976 (7th Cir. 1972) (suit against debtor's trustee as responsible party for taxes of debtor's subsidiary); Baker & Taylor Drilling Co. v. Stafford, 369 F.2d 551, 556 (9th Cir. 1966) (suit against debtor's co-owner of oil well); In re South Jersey Land Corp., 361 F.2d 610, 613-14 (3d Cir. 1966) (foreclosure suit against property of debtor's subsidiary); In re Journal-News Corp., 193 F.2d 492, 492 (2d Cir. 1951) (sale of debtor's stock by a shareholder); Curtis v. O'Leary, 131 F.2d 240, 244-46 (8th Cir. 1942) (suit between debtor's shareholders for fraud and breach of contract in sale of debtor's stock); Thomas v. Rosseter (In re 4145 Broadway Hotel Co.), 124 F.2d 891, 891-92 (7th Cir. 1941) (libel suit against debtor's reorganization trustee); In re Prudence Bonds Corp., 79 F.2d 212, 215-17 (2d Cir. 1935) (suit on notes and mortgages issued by non-debtor and guaranteed by debtor's affiliate). But see In re Federal Biscuit Co., 203 F. 37, 38-39 (2d Cir. 1913) (staying suit against debtor's surety, where debtor's assets secured indemnity obligation to surety, pending plenary suit to determine whether transfer of security was preferential transfer of debtor's assets).

352. See, e.g., Parkview-Gem, Inc. v. Stein (In re Parkview-Gem, Inc.), 516 F.2d 807, 811 (8th Cir. 1975) (stating that even if "the termination of the lease of the [debtor's] subsidiary would adversely affect the debtor," such "an adverse affect upon the debtor is not an adequate
basis for granting the bankruptcy court jurisdiction"); Feldman v. Trustees of Beck Indus., Inc. (In re Beck Indus., Inc.), 479 F.2d 410, 419 (2d Cir. 1973) (concluding that there was no jurisdiction to enjoin a state court suit against debtor's subsidiary, even if "restraint of the . . . suit will facilitate . . . administration of the debtor's estate, already a complicated task, since [the trustees] will otherwise be forced to divert their energies to defense of that suit in an inconvenient forum in order to preserve the value of the debtor's stock interest in [its Subsidiary]"); In re Magnus Harmonica Corp., 237 F.2d 867, 869 (3d Cir. 1956) (holding that officers/guarantors' indemnification claims against the debtor provided no basis for the injunction of a creditor's suit against officers/guarantors); In re Magnus Harmonica Corp., 233 F.2d 803, 803-04 (3d Cir. 1956) (holding that it was improper to enjoin a creditor's suit against the debtor's officers/guarantors, even if the officers' assets subject to execution in the suit were essential patents being licensed to the debtor); First Citizens Bank & Trust Co. v. Martin (In re Hotel Martin Co.), 94 F.2d 643, 643 (2d Cir. 1938) (concluding that lower court had no jurisdiction to enjoin the sale of bonds issued by the debtor, owned by debtor's president/trustee, and posted as collateral for a loan to the president, and "[n]o sufficient reason is advanced why the sale or disposition of the [debtor's] bonds would in any wise interfere with the reorganization of the debtor"); Northern Paper Mills v. Cary (In re Patten Paper Co.), 86 F.2d 761, 762, 764-66 (7th Cir. 1936) (holding that lower court had no jurisdiction to enjoin a foreclosure sale of stock owned and pledged by non-debtors to permit the reorganization debtor and non-debtors to sell their stock jointly as a control block at a substantially higher price than the zero sales price); General Am. Tank Car Corp. v. Adolf Gobel, Inc. (In re Adolf Gobel, Inc.), 80 F.2d 849, 852-53 (2d Cir. 1936) ("The argument that [the statute] has for its object reorganization, and grants to the court power to enjoin an action in the state court which renders reorganization more difficult, is . . . without merit. . . . Thoough facility in reorganization is desirable, it is not the sole consideration. It is merely a basis for the exercise of jurisdiction in cases where jurisdiction exists." (citation omitted)); In re New York & Worcester Express, Inc., 294 F. Supp. 1163, 1164-65 (S.D.N.Y. 1968) (concluding that there was no jurisdiction to enjoin labor grievances proceeding against the debtor's owner, even if an award would impede financing of the debtor's reorganization and even if the owner will file an indemnification claim against the debtor); Roll Form Prods., Inc. v. All State Trucking Co. (In re Roll Form Prods., Inc.), 8 B.R. 479, 483-85 (Bankr. S.D.N.Y.) (stating that the mere fact that a carrier's efforts to collect shipping charges from the debtor's customers and suppliers was hurting debtor's business "cannot be deemed an interference with the administration of a [reorganization] case justifying the issuance of an injunction under § 2(a)(15)"). rev'd on other grounds, 662 F.2d 150 (2d Cir. 1981). Although reported opinions refused to approve temporary non-debtor release and injunction, reorganization court enjoined state court action against non-debtor guarantor upon commencement of reorganization proceedings).

In a prominent and rare 1898 Act case that approved a non-debtor injunction, the court did so only after concluding that it did have jurisdiction to adjudicate creditors' fraud claims against the debtor's subsidiaries, through necessity jurisdiction, and only after permitting the creditors to present those non-debtor fraud claims for resolution in the debtor's reorganization proceedings. See In re Equity Funding Corp., 396 F. Supp. 1266, 1268-70, 1271-74 (C.D. Cal. 1975); see also supra note 349 (discussing necessity jurisdiction). The non-debtor fraud actions at issue were numerous individual and class actions arising out of transactions in the debtor's securities, and most of the suits had been consolidated in multidistrict litigation proceedings in federal court. See Equity Funding, 396 F. Supp. at 1268. The bankruptcy court found necessity jurisdiction over these non-debtor suits, because stock in the debtor's subsidiaries served as collateral for secured bank loans, and the outcomes of the non-debtor actions could have a material effect on the value of that collateral. Therefore, resolution of the non-debtor claims was deemed necessary to valuation of the secured and/or unsecured portions of the banks' claims against the debtor for purposes of voting and proper claim treatment under the debtor's plan of reorganization. See id. at 1272-74; see also In re Samoset Assocs., 654 F.2d 247, 253-54 (1st Cir. 1981) (ruling that a bankruptcy judge could enjoin state court litigation between non-debtors where the resolution of a dispute under a three-way contract involving the debtor was necessary to administer the estate completely and the bankruptcy judge would adjudicate the non-debtors' dispute); In re Bargain City U.S.A., Inc., 212 F. Supp. 111, 115-16 (E.D. Pa. 1962) (enjoining a lessor's state court claim against the debtor's assignor and allowing the lessor to prosecute its non-debtor action against the assignor in the debtor's arrangement proceedings). The manner in which the Equity Funding court subsequently resolved the enjoined non-debtor actions, though,
Because courts under the 1898 Act, as a rule, refused to enjoin suits between non-debtors, even temporarily, it is not at all surprising that these courts also rejected occasional efforts to obtain permanent non-debtor releases through a plan of reorganization—most of which involved plan provisions that purported to release contractual guarantors from their personal liability for the debtor’s obligations. The courts’ apprehensions about non-debtor injunctions, however, disappeared with enactment of the Bankruptcy Reform Act of 1978.

D. Temporary Non-Debtor Stays Under the Bankruptcy Reform Act of 1978

The Bankruptcy Reform Act of 1978 (the Reform Act) brought sweeping changes to bankruptcy law, repealing the 1898 Act and enacting the current Bankruptcy Code. Undoubtedly the most significant changes came through an expansive grant of federal bankruptcy jurisdiction. The courts promptly seized upon this enlarged bankruptcy jurisdiction to find jurisdiction to enjoin non-debtor actions, and the Supreme Court recently held that the courts do have bankruptcy jurisdiction to temporarily stay non-debtor actions.

made the Equity Funding injunction resemble a permanent non-debtor release. The plan of reorganization approved by the court imposed a mandatory settlement of the fraud claims against the debtor’s subsidiaries. See In re Equity Funding Corp., 416 F. Supp. 132, 139, 142, 150-52, 154 (C.D. Cal. 1975); see also supra Part III.A.

353. See, e.g., Union Carbide Corp. v. Newboles, 686 F.2d 593, 594-95 (7th Cir. 1982) (refusing to give res judicata effect to the plan release of contractual guarantors of the debtor’s obligations); Weber v. Diversey Bldg. Corp. (In re Diversey Bldg. Corp.), 86 F.2d 456, 456-58 (7th Cir. 1936); Commercial Wholesalers, Inc. v. Investors Commercial Corp., 172 F.2d 800, 801 (9th Cir. 1949) (concluding that a final decree, entered after a plan of arrangement was confirmed, purporting to release non-debtors and permanently enjoin suits against them was “void for want of jurisdiction”); Nine N. Church St., 82 F.2d at 187-89 (reversing a permanent injunction of suits against the debtor’s guarantor entered in conjunction with a plan release of the guarantor); cf. Prudence Bonds, 79 F.2d at 215-17 (reasoning that because there was no jurisdiction over notes and mortgages issued by the non-debtor and guaranteed by the debtor’s affiliate, “[i]t follows that this property cannot be included in any plan or plans for reorganization of the debtor; hence it was error to stay the prosecution of the [creditor’s] foreclosure suit”); In re 1775 Broadway Corp., 79 F.2d 108, 110 (2d Cir. 1935) (stating in dicta that the reorganization “court did not have jurisdiction of nonassenting note holders to release tort claims against the [non-debtor] seller of the [debtor’s] notes” in approving the debtor’s plan of reorganization); In re Emergency Beacon Corp., 40 B.R. 113, 115-18 (Bankr. S.D.N.Y. 1984) (holding that there was no jurisdiction to permanently enjoin the creditor from pursuing an action against the reorganization debtor’s guarantor). But cf. Equity Funding, 416 F. Supp. at 139, 142, 150-52, 154, discussed supra note 352.

355. See id. §§ 401, 402(a), 92 Stat. at 2682.
356. See Celotex Corp. v. Edwards, 514 U.S. 300 (1995), discussed infra notes 365-81 and accompanying text. The Marathon case, holding the Reform Act’s jurisdictional provisions unconstitutional, was not directed to the broad grant of bankruptcy jurisdiction per se; it only condemned exercise of the full range of bankruptcy jurisdiction by non-Article III adjuncts. See infra Part IV.E (discussing Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982)). The Celotex holding did not require consideration of the implications of Marathon. See infra notes 399-401 and accompanying text. The impact of the Marathon holding on jurisdiction to enjoin non-debtor actions is addressed infra Part IV.E-G.1.
The Reform Act created federal bankruptcy jurisdiction over all matters “related to” a bankruptcy case.\textsuperscript{357} The Reform Act also created a new court to exercise this broad bankruptcy jurisdiction: an adjunct to each federal district court, denominated the “United States Bankruptcy Court for the district.”\textsuperscript{358} Thus, the new jurisdictional scheme removed the summary in rem strictures that confined the power of the former referees and gave the newly created bankruptcy courts both in rem\textsuperscript{359} and full in personam jurisdiction over any controversy related to a bankruptcy case.\textsuperscript{360}

The Reform Act provisions regarding injunctive powers of the new bankruptcy courts were remarkably similar to those under the 1898 Act. On their face, then, those provisions would appear to give bankruptcy courts no more power to enjoin actions between non-debtors than existed under the 1898 Act.\textsuperscript{361} But with the new expan-

\textsuperscript{357} The Reform Act gave federal district courts “original and exclusive jurisdiction of all [bankruptcy] cases” and “original but not exclusive jurisdiction of all civil proceedings arising under [the Bankruptcy Code] or arising in or related to [bankruptcy] cases.” Pub. L. No. 95-598, § 241(a), 92 Stat. at 2668 (enacting 28 U.S.C. § 1471(a)-(b) (1982) (repealed 1984)).

\textsuperscript{358} Id. § 201(a), 92 Stat. at 2657 (enacting 28 U.S.C. § 151(a) (1982) (repealed 1984)). Although bankruptcy jurisdiction was initially vested in federal district courts, the Reform Act provided that “[t]he bankruptcy court for the district in which a [bankruptcy] case is commenced shall exercise all of the jurisdiction conferred by this section on the district courts,” id. § 241(a), 92 Stat. at 2668 (enacting 28 U.S.C. § 1471(c) (1982) (repealed 1984)), with only ordinary appellate review by the district court, see id. § 236(a), 92 Stat. at 2668 (enacting 28 U.S.C. § 1334 (1982) (amended 1984)). In lieu of appeals to the district court, the Reform Act authorized circuit courts to establish bankruptcy appellate panels composed of three bankruptcy judges, and by consent of the parties, they could directly appeal to the circuit court of appeals. See id. §§ 201(a), 236(a), 241(a), 92 Stat. at 2659, 2667, 2671 (enacting 28 U.S.C. §§ 160, 1293, 1482 (1982) (repealed 1984)). The Reform Act jurisdictional provisions were to be phased in over a transition period, with former referees continuing service as bankruptcy judges and exercising all of the expanded jurisdiction granted to the new bankruptcy courts. See id. §§ 404-405, 92 Stat. at 2683-85 (repealed 1984). See generally 1 COLLIER ON BANKRUPTCY ¶¶ 7.02, at 7-4 to -5, 7.05[4][5] (Lawrence P. King ed., 15th ed. 1996).

\textsuperscript{359} The in rem jurisdiction of the new bankruptcy courts came via a grant of “exclusive jurisdiction of all of the property, wherever located, of the debtor, as of the commencement of such [bankruptcy] case.” Pub. L. No. 95-598, § 241(a), 92 Stat. at 2669 (enacting 28 U.S.C. § 1471(e) (1982) (repealed 1984)). This was substantially the same as the summary in rem jurisdiction of reorganization courts under the 1898 Act. See supra note 350; 6 COLLIER (14th ed. 1978), supra note 46, ¶ 3.05 (Chapter X corporate reorganizations); 8 id. ¶ 3.02 (Chapter XI arrangements); 9 id. ¶ 3.01[1][2] (Chapter XII real property arrangements).

\textsuperscript{360} Actions that formerly had to be tried in State court or in Federal district court, at great cost and delay to the estate, may now be tried in the bankruptcy courts. The idea of possession or consent as the sole bases for jurisdiction is eliminated. The bankruptcy court is given in personam jurisdiction [sic] as well as in rem jurisdiction to handle everything that arises in a bankruptcy case.


\textsuperscript{361} Section 105(a) of the Bankruptcy Code gave bankruptcy courts the power, substantially similar to that formerly possessed by referees, to “issue any order, process or judgment that is necessary or appropriate to carry out the provisions of” the Bankruptcy Code. 11 U.S.C. § 105(a) (1994); see 1898 Act § 2a(15), quoted supra note 312. This power also came with the same proviso as under section 2a(15) of the 1898 Act, that “[a] bankruptcy court . . . may not
sive bankruptcy jurisdiction, the 1898 Act’s presumed jurisdictional
obstacle to such injunctions evaporated. The courts quickly concluded
that section 105 of the Bankruptcy Code, in conjunction with the
broad jurisdictional grant, gave bankruptcy courts jurisdiction to en-
join an action between non-debtors if the action was, in the words of
the jurisdictional grant, “related to” the pending bankruptcy case.362
In Chapter 11 reorganization cases, the courts have held that jurisdic-
tion to enjoin attaches if prosecution of the non-debtor action would
interfere with the debtor’s prospects for a successful reorganization.363


362. See, e.g., Old Orchard Inv. Co. v. A.D.I. Distrib., Inc. (In re Old Orchard Inv. Co.), 31
denying motion to amend 21 B.R. 777, 778 (Bankr. D.N.M. 1982); First Fed. Sav. & Loan Ass’n v. Pettit,
690, 700-01 (Bankr. S.D.N.Y. 1984); In re Ms. Kipps, Inc., 34 B.R. 91, 92-93 (Bankr. S.D.N.Y.
1983); In re Brentano’s, Inc., 27 B.R. 90, 91-92 (Bankr. S.D.N.Y. 1983); Landmark Air Fund II v.
BancOhio Nat’l Bank (In re Landmark Air Fund II), 19 B.R. 556, 558-59 (Bankr. N.D. Ohio
the most influential formulation of the “related to” nexus necessary for jurisdiction to enjoin a
non-debtor suit: “failure to enjoin would affect the bankruptcy estate and would adversely or
detrimentally influence and pressure the debtor through that third party.” 21 B.R. at 778.
The courts have largely adopted this Otero Mills standard for jurisdiction to enjoin non-debtor ac-
tions. See, e.g., In re G.S.F. Corp., 938 F.2d 1467, 1474 (1st Cir. 1991); A.H. Robins Co. v.
Piccinin, 788 F.2d 994, 1003 (4th Cir. 1986); Gathering Restaurant, Inc. v. First Nat’l Bank (In re
Gathering Restaurant, Inc.), 79 B.R. 992, 996 (Bankr. N.D. Ind. 1986); MacDonald/Assocs., Inc.
v. Stillwagon (In re MacDonald/Assocs., Inc.), 54 B.R. 865, 867-68 (Bankr. D.R.I. 1985); In re
Dore & Assocs., 54 B.R. 353, 357 (Bankr. W.D. Wis. 1985); In re Sondra, 44 B.R. 205, 207

363. See, e.g., Monarch Life Ins. Co. v. Ropes & Gray, 65 F.3d 973, 979 (1st Cir. 1995)
(holding that jurisdiction to enjoin attaches if “such [non-debtor] actions would entail or
threaten adverse ‘impact’ on the administration of the Chapter 11 estate”); Willis v. Celotex
Corp., 978 F.2d 146, 149 (4th Cir. 1992) (“[T]he bankruptcy court may ‘enjoin a variety of [non-
debtor] proceedings . . . which will have an adverse impact on the Debtor’s ability to formulate
a Chapter 11 plan.’” (quoting Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-
Robins Co.), 828 F.2d 1023, 1025 (4th Cir. 1987) (holding that the reorganization court had
power to stay non-debtor “litigation that could interfere with the reorganization of the debtor”);
that a court may enjoin non-debtor litigation “to provide the debtor with a realistic opportunity
to formulate a plan of reorganization”); In re Celotex Corp., 128 B.R. 478, 484 (Bankr. M.D. Fla.
1991) (“[T]he role of Section 105 in this type of case is first to protect the reorganization pro-
cess.”); In re John Renton Young, Ltd., 87 B.R. 635, 636 (Bankr. D. Nev. 1988) (holding that a
motion to “enjoin activities which will allegedly interfere with [debtor’s] ability to reorganize
[was within] subject matter jurisdiction”); In re Monroe Well Serv., Inc., 67 B.R. 746, 753 (Bankr.
E.D. Pa. 1986) (concluding that jurisdiction depends upon “the impact upon the debtors which
would follow if the lien creditors were allowed to exercise their state created rights against
non-debtors); Rustic Mfg., Inc. v. Marine Bank Dane County (In re Rustic Mfg., Inc.), 55 B.R. 25, 27
(Bankr. W.D. Wis. 1985) (“[A] significant impact on the debtor’s chances to reorganize [is] suffi-
cient relation to the bankruptcy case . . . to secure jurisdiction.”); In re Emergency Beacon Corp.,
40 B.R. 113, 117 (Bankr. S.D.N.Y. 1984) (finding that non-debtor actions “would adversely affect
collection efforts against a third party . . . if those efforts would impair a debtor’s ability to
reorganize”).
Of course, this approach to jurisdiction to stay non-debtor actions is precisely in accord with the Supreme Court's view of the role of injunctions in reorganization cases, as originally articulated in the Continental Illinois case: a tool to protect and promote the debtor's reorganization effort. Moreover, the Supreme Court recently held this to be a proper jurisdictional foundation for temporary non-debtor stays in the case of Celotex Corp. v. Edwards.

The non-debtor stay that the Supreme Court considered in Celotex was issued in the Chapter 11 reorganization proceedings of Celotex Corporation—one of many asbestos manufacturers whose massive potential liability for asbestos personal injuries precipitated a Chapter 11 filing. When Celotex filed its Chapter 11 petition, it was appealing adverse judgments in more than one hundred personal injury suits in state and federal courts. For each of these judgments on appeal, Celotex had posted a supersedeas bond to stay collection on the judgment pending the outcome of the appeal. A third party acting as surety on the bond, undertaking to pay the amount of the judgment should Celotex lose the appeal. Celotex, in turn, not only promised to pay the surety in the event it paid on the supersedeas bond, but also secured this obligation by granting the surety various property interests as collateral. In many instances, Celotex's liability insurers served as sureties for Celotex's supersedeas bonds, and often Celotex secured its reimbursement obligation on those bonds by promising the insurance company an offset against any insurance proceeds Celotex would otherwise be entitled to receive.

Shortly after Celotex filed Chapter 11, the bankruptcy court presiding over the reorganization proceedings issued a section 105 injunction as a supplement to the automatic stay of section 362, staying all proceedings involving Celotex, including any action against a supersedeas bond posted by Celotex. The bankruptcy court refused all re-

368. See 140 B.R. at 913-14; 128 B.R. at 479-80, 482-83. These supersedeas bonds involved several different sureties and 227 judgment creditors with judgments totaling nearly $70 million. See 514 U.S. at 302 n.2, 304 n.4; 140 B.R. at 916; 128 B.R. at 479-80, 482-83. These suits in which judgment was already entered against Celotex were but a small subset of the more than 141,000 asbestos personal injury suits pending against Celotex when it filed its Chapter 11 petition. See 128 B.R. at 479.
370. See 514 U.S. at 303. The bankruptcy court subsequently lifted the stay to allow pending appeals to proceed, but continued to stay any action against supersedeas bonds, even in those cases where all appeals had concluded in favor of a judgment creditor, unless the judgment creditor first asked the bankruptcy court to vacate the § 105 stay. Various plaintiffs whose judg-
quests to proceed against Celotex's sureties, primarily citing the sureties' corresponding offset rights against Celotex's insurance proceeds and the difficulties this would cause in Celotex's attempts to resolve coverage disputes with its insurers, which "may well be the linchpin of [Celotex's] formulation of a feasible plan."\(^{371}\)

Despite the bankruptcy court's section 105 stay, some plaintiffs whose judgments were affirmed on appeal sought permission to execute on posted supersedeas bonds, not from the bankruptcy court, but from those courts in which the bonds had been posted.\(^{372}\) The Fifth Circuit affirmed a Texas district court that permitted plaintiffs to execute on a Celotex supersedeas bond, but the Supreme Court reversed the Fifth Circuit decision.\(^{373}\) Because it was not a direct review of the bankruptcy court's section 105 stay order, the Supreme Court did not assess the propriety of the injunction. Rather, the Court limited its inquiry to whether the bankruptcy court had jurisdiction to stay execution on the supersedeas bond—an action against a non-debtor—and was thus an order that should be respected in the collateral execution proceedings.\(^{374}\)

In approving execution on the supersedeas bond, the Fifth Circuit acknowledged that jurisdiction over any matter "related to" a bankruptcy case was broad enough to encompass temporary stays of actions against non-debtors.\(^{375}\) But the "related to" link that the Fifth Circuit applied was whether "pursuing actions pending in other courts [would] threaten the integrity of a bankrupt's estate."\(^{376}\) Because the court concluded that the unfavorable outcome of its appeal left Celotex with no further interest in the supersedeas bond, the court perceived no threat to the integrity of Celotex's estate from execution on

\(^{371}\) 140 B.R. at 915. The court also relied on the possibility that certain judgment creditors' claims might be subject to subordination or avoidance pursuant to the Bankruptcy Code. See id. at 914. Thus, the bankruptcy court continued the § 105 stay of actions against sureties, but set a deadline for Celotex to commence any action to avoid or subordinate judgment creditors' claims. In order to preserve the status quo, the court also set forth conditions to assure that judgment creditors' rights against the sureties were adequately protected pending formulation of a plan of reorganization that could comprehensively provide for Celotex's various obligations, presumably with payment in full for any bonded judgment creditor whose claim was not avoided or subordinated. See id. at 914-17.

\(^{372}\) When a federal district court in Virginia granted permission to execute on a supersedeas bond, the Fourth Circuit vacated the order, holding that the bankruptcy court was within its jurisdiction in enjoining actions against Celotex's sureties. See Willis v. Celotex Corp., 978 F.2d 146, 149-50 (4th Cir. 1992).


\(^{374}\) See 514 U.S. at 312-13. The Court applied the standards for determining when persons subject to an injunctive order are bound to obey it, namely that the order was issued by a court with jurisdiction and that the order had more than a frivolous pretense of validity. See id. at 306 (citing GTE Sylvania, Inc. v. Consumers Union of United States, Inc., 445 U.S. 375, 386-87 (1980)).

\(^{375}\) See 6 F.3d at 318.

\(^{376}\) Id. at 320 (citing In re Davis, 730 F.2d 176, 184 (5th Cir. 1984)).
the bond.\textsuperscript{377} The Supreme Court, though, evidently viewed the Fifth Circuit's approach as a throwback to the in rem jurisdictional precepts that deterred lower courts from enjoining non-debtor actions under the 1898 Act,\textsuperscript{378} saying "that the 'related to' language . . . must be read to give . . . jurisdiction over more than simply proceedings involving the property of the debtor or the estate."\textsuperscript{379} Instead, the Court reaffirmed the vitality of the \textit{Continental Illinois} rationale for injunctions in reorganization cases, prominently citing that case for the proposition that jurisdiction may extend more broadly in reorganization cases than in liquidation cases.\textsuperscript{380} Consistent with \textit{Continental Illinois}, the Court also adopted the approach of those lower courts that find a sufficient "related to" connection to temporarily stay a non-debtor action if continuation of the action would impede the debtor's ability to successfully reorganize.\textsuperscript{381}

The one thing that \textit{Celotex} makes crystal clear is that the supposed jurisdictional constraints under the 1898 Act, which discouraged lower courts from extending \textit{Continental Illinois} to temporary stays of non-debtor actions, are now gone. Jurisdiction over Chapter 11 reorganization proceedings includes the power to protect that jurisdiction by staying suits that could endanger the debtor's ability to reorganize, even if those suits are solely between non-debtors and are not directed against the debtor's property. Nonetheless, the \textit{Celotex} case expressly left open important jurisdictional questions with respect to temporary non-debtor stays, and even more arise when one attempts to apply this jurisdictional framework to permanent non-debtor releases. All of these questions revolve around the 1984 bankruptcy jurisdiction amendments, which were necessitated when the Supreme Court declared the Reform Act's jurisdictional scheme unconstitutional in \textit{Northern Pipeline Construction Co. v. Marathon Pipe Line Co.}\textsuperscript{382}

\textsuperscript{377} See \textit{id.}
\textsuperscript{378} See \textit{supra} Part IV.C.
\textsuperscript{379} 514 U.S. at 308.
\textsuperscript{380} See \textit{id.} at 310 (citing \textit{Continental Ill. Nat'l Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co.}, 294 U.S. 648, 676 (1935)).
\textsuperscript{381} The Court upheld the jurisdiction of the \textit{Celotex} bankruptcy court to stay execution against \textit{Celotex}'s sureties based upon the bankruptcy court's findings that bonded judgment creditors' immediate execution on the bonds, in the words of the Supreme Court, "would have a direct and substantial adverse effect on \textit{Celotex}'s ability to undergo a successful reorganization." \textit{Id.} It is unclear whether the Court intended the "direct and substantial adverse effect" language as a jurisdictional prerequisite for non-debtor stays. In surveying circuit court opinions that the Court said are in accord with its holding, it described the jurisdictional connection as "affect administration of debtor's reorganization plan," "might impede the reorganization process," and "would interfere with debtor's reorganization." \textit{Id.} at 310-11. These characterizations suggest that the Court was not announcing a test for the necessary jurisdictional nexus to stay a non-debtor action.
\textsuperscript{382} 458 U.S. 50 (1982).
E. Marathon and the 1984 BAFJA Amendments

After the Supreme Court struck down the Reform Act's jurisdictional provisions as unconstitutional, Congress responded not by reducing the scope of federal bankruptcy jurisdiction, but by reducing the jurisdiction exercised by the adjunct bankruptcy judges. Thus, although Celotex holds that temporary non-debtor stays are within the bounds of federal bankruptcy jurisdiction, the lingering uncertainty is whether such a non-debtor injunction can issue from an adjunct bankruptcy court.

The adjunct bankruptcy courts created by the Reform Act exercised all of the new expansive bankruptcy jurisdiction, yet the Reform Act bankruptcy judges did not enjoy the Article III protections of lifetime tenure with undiminished compensation. In Marathon, the Court found this jurisdictional design violative of Article III as applied to the case before it, a suit by a Chapter 11 debtor to recover damages from a third party for breach of contract. Of course, under the 1898 Act, such a suit would have been a plenary action against an adverse party, outside the summary jurisdiction of a bankruptcy referee, requiring plenary suit in a state court or a federal district court. Under the Reform Act, however, this suit fell within the broad “related to” jurisdiction of the new bankruptcy courts. A plurality of the Court concluded that this grant of jurisdiction to bankruptcy judges had “impermissibly removed most, if not all, of the essential attributes of the judicial power’ from the Art. III district court, and ha[d] vested those attributes in a non-Art. III adjunct.”

383. See supra notes 357-60 and accompanying text.
384. U.S. Const. art. III, § 1. Specifically, the bankruptcy judges were to be appointed by the President for 14-year terms only, and they were subject to removal during their terms by their circuit judicial councils. See Pub. L. No. 95-598, § 201(a), 92 Stat. 2549, 2657-58 (1978) (enacting 28 U.S.C. §§ 152-153 (1982) (repealed 1984)). In addition, the Reform Act set bankruptcy judges' salaries, but made them subject to adjustment under the Federal Salary Act. See id. § 201(a), 92 Stat. at 2658 (enacting 28 U.S.C. § 154 (1982) (repealed 1984)).
385. See 458 U.S. at 56 (suit for breach of contract and warranty, with allegations of misrepresentation, coercion, and duress).
386. See supra notes 314-24 and accompanying text.
387. See 458 U.S. at 54.
388. 458 U.S. at 87 (Brennan, J., plurality opinion). The concurring Justices agreed that jurisdiction to adjudicate the debtor's action, which would exist in essentially the same form even if the debtor had not filed bankruptcy, could only be vested in an Article III judge. See id. at 89-92 (Rehnquist, J., concurring opinion). Perhaps the broadest proposition on which both the plurality and concurrence agreed was this: “It is clear that, at the least, the new bankruptcy judges cannot constitutionally be vested with jurisdiction to decide this state-law contract claim against [defendant] Marathon.” Id. at 87 n.40 (Brennan, J., plurality opinion); see also id. at 92 (Burger, J., dissenting) (describing narrow basis of concurrence as holding of the Court). The Court subsequently characterized the Marathon holding as “establish[ing] only that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review.” Thomas v. Union Carbide Agric. Prods. Co., 473 U.S. 568, 584 (1985); see also Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833, 838-39 (1986) (quoting Union Carbide, 473 U.S. at 584). Both the plurality and concurring opinions agreed that the unconstitutional portions of the jurisdictional grant could not be sev-
Congress' response to the *Marathon* holding was the Bankruptcy Amendments and Federal Judgeship Act (BAFJA) of 1984,\(^{389}\) which put in place the current bankruptcy jurisdictional structure. The BAFJA amendments are essentially a return to a system of jurisdiction by referral, similar to that of the 1898 Act.\(^{390}\) The BAFJA amendments retained the adjunct bankruptcy courts for each district and retained the Reform Act's broad grant of bankruptcy jurisdiction over any matter "related to" a bankruptcy case.\(^{391}\) Unlike the Reform Act, however, the BAFJA amendments did not commit all of this jurisdiction to bankruptcy judges.

The BAFJA amendments permit the district courts to refer to bankruptcy judges all bankruptcy cases and proceedings within the district court's broad bankruptcy jurisdiction.\(^{392}\) Yet, the power of bankruptcy judges with respect to referred proceedings differs markedly depending upon whether the proceedings constitute what the


\(^{390}\) See supra Part IV.B.

\(^{391}\) A bankruptcy judge is a non-Article III "unit of the district court," with the bankruptcy judge serving "as a judicial officer of the district court." 28 U.S.C. § 151 (1994). Bankruptcy judges are appointed by the circuit courts of appeals for 14-year terms. See id. § 152(a)(1). As under both the 1898 Act and the Reform Act, federal district courts continue to be the initial repositories of bankruptcy jurisdiction, with the jurisdictional grant being exactly the same as that of the Reform Act: "original and exclusive jurisdiction of all [bankruptcy] cases" and "original but not exclusive jurisdiction of all civil proceedings arising under [the Bankruptcy Code], or arising in or related to [bankruptcy] cases." Id. § 1334(a)-(b); see supra note 357 (quoting Reform Act jurisdiction provisions). The district courts also continue to have "exclusive jurisdiction of all of the property, wherever located, of the debtor as of the commencement of such [bankruptcy] case, and of property of the estate." 28 U.S.C. § 1334(e); see supra notes 350 and 359 (quoting 1898 Act and Reform Act jurisdiction provisions).

statute designates "core proceedings arising under [the Bankruptcy Code], or arising in a [bankruptcy] case." In a so-called core proceeding, a bankruptcy judge has the power to "hear and determine" the controversy and "enter appropriate orders and judgments," subject to review only through conventional appellate procedures.

In a core proceeding, a bankruptcy judge is given unrestricted jurisdiction to adjudicate parties' disputes. By contrast, a non-core proceeding is, in the words of the statute, "a proceeding that is not a core proceeding but that is otherwise related to a [bankruptcy] case." In these non-core, "related to" proceedings, a bankruptcy judge's powers are greatly restricted. A bankruptcy court can hear a non-core proceeding. However, unless the parties consent to a final determination by the bankruptcy judge, the bankruptcy judge's province is limited to submitting proposed findings of fact and conclusions of law to the district court, for entry of any final order or judgment after a de novo review. Thus, under the current jurisdictional system, determining which proceedings are within the core jurisdiction of bankruptcy courts is a critical inquiry.

The core/non-core distinction takes on peculiar twists as applied to non-debtor injunctions. The courts developed the jurisdictional test for temporary non-debtor stays before the BAFJA amendments and under the rubric of jurisdiction to enjoin non-debtor actions "related to" the bankruptcy case. The Supreme Court subsequently approved this jurisdictional standard in Celotex. But with the advent of BAFJA and the core/non-core dichotomy, if the non-debtor action is merely a non-core, "related to" proceeding, is a temporary stay of the non-debtor action now a matter outside the core jurisdiction of bank-

394. The statute provides as follows:
Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.
Id. Initial appeals are to the district court or, by consent of the litigants, to bankruptcy appellate panels composed of three bankruptcy judges. See id. § 158(a)-(b). Thereafter, appeal is to the courts of appeals. See id. § 158(d).
395. Id. § 157(c)(1).
396. In that event, the bankruptcy judge's role is exactly the same as in a core proceeding.
See id. § 157(c)(2).
397. The statute provides as follows:
A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.
Id. § 157(c)(1).
398. A prominent treatise opines that "[t]he determination of whether or not a particular proceeding is a core proceeding may be among the most important questions in any bankruptcy case." 1 NORTON, supra note 21, ¶ 4:21, at 4-153.
399. See supra Part IV.D.
ruptcy courts? The *Celotex* majority opinion expressly avoided that issue because the parties did not raise it. The dissent, however, questioned both the core jurisdiction of the bankruptcy court and whether a bankruptcy court has any authority at all to enjoin collateral litigation. Solving the core/non-core mystery, therefore, is a significant issue in its own right. More importantly, though, deciphering the jurisdictional obscurities of temporary non-debtor stays reveals the dubious jurisdictional basis for permanent non-debtor releases.

F. Core Jurisdiction to Temporarily Stay Non-Debtor Actions

Although a non-debtor action is at best only a non-core proceeding, outside a bankruptcy court’s core jurisdiction to adjudicate, a bankruptcy judge nonetheless has core jurisdiction to temporarily stay a non-debtor action. The *Continental Illinois* distinction between jurisdiction to enjoin and jurisdiction to adjudicate means that a bankruptcy judge’s core jurisdiction to temporarily stay a non-debtor action is not dependent upon jurisdiction to adjudicate that non-debtor action.

Restricting the jurisdiction of bankruptcy courts to core proceedings was obviously an attempt to cure the constitutional infirmities of the Reform Act. The terminology of “core” bankruptcy proceedings has no statutory ancestors and is apparently taken from Justice Brennan’s plurality opinion in *Marathon*, wherein he said that “the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power, must be distinguished from the adjudication of state-created private rights, such as the right to recover contract damages that is at issue in this case.” In considering the appropriate legislative response to *Marathon*, then, this terminology of “core” proceedings became a way of referring to those matters within the traditional, historical reach of bankruptcy laws and summary referee jurisdiction and, therefore, presumably appropriate for adjudication by a non-Article III bankruptcy judge.
Nowhere does the statute define a "core" proceeding.\textsuperscript{405} Nonetheless, meaning can be divined from the statutes' "arising under" and "arising in" jurisdictional nexus.\textsuperscript{406} A proceeding is one "arising under" the Bankruptcy Code when a claim is made pursuant to a cause of action created by the Bankruptcy Code.\textsuperscript{407} A proceeding "arising in" a bankruptcy case, although not grounded in a cause of action created by the Bankruptcy Code, is a proceeding that would have no existence in the absence of the bankruptcy case.\textsuperscript{408}

to determine what matters can be considered at the 'core' of bankruptcy administration, making possible an exercise of full judicial power by a non-article III officer."; cf. Marathon, 458 U.S. at 99 (White, J., dissenting) ("I take it that the Court does not condemn as inconsistent with Art. III the assignment of these functions—i.e., those within the summary jurisdiction of the old bankruptcy courts—to a non-Art. III judge, since, as the plurality says, they lie at the core of the federal bankruptcy power."); S. Elizabeth Gibson, Jury Trials and Core Proceedings: The Bankruptcy Judge's Uncertain Authority, 65 AM. BANKR. L.J. 143, 170 (1991) ("It appears that the Court might have in mind the bankruptcy court's old summary jurisdiction when it considers what Congress could permissibly commit to bankruptcy court jurisdiction.").

\textsuperscript{405} The closest thing to a definition is a noneclusive list of matters included within core proceedings, including the catch-all categories of "matters concerning the administration of the estate" and "other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship." 28 U.S.C. § 157(b)(2)(A), (O) (1994). The second catch-all core category, like the "core" terminology itself, also apparently has its origins in Justice Brennan's Marathon opinion, quoted supra text accompanying note 403. See 1 COLLI\textsuperscript{er} (15th ed.), supra note 40, ¶ 3.02[3][d][ii], at 3-43.

\textsuperscript{406} The statute uses this terminology in conjunction with both the initial grant of bankruptcy jurisdiction to district courts, 28 U.S.C. § 1334(b), quoted supra note 391, and the grant of core jurisdiction to bankruptcy judges, id. § 157(b)(1), quoted supra note 394. Compare 1 COLLI\textsuperscript{er} (15th ed.), supra note 40, ¶ 3.02[2], at 3-33 (stating that "core" proceedings are the equivalent of proceedings "arising under" and "arising in"), with 1 NORTON, supra note 21, § 4.21, at 4-159 to -160 (stating that "core" proceedings may be independent of nexuses, but a bankruptcy court can only adjudicate a core proceeding that also satisfies the nexus requirements).

\textsuperscript{407} See 1 COLLI\textsuperscript{er} (15th ed.), supra note 40, ¶ 3.01[4][c][i]; 1 NORTON, supra note 21, § 4.38, at 4-231. For example, a proceeding to recover a preferential transfer pursuant to § 547 of the Bankruptcy Code would be a proceeding "arising under" the Bankruptcy Code. A preference action is also included among the statutes' illustrative listing of core proceedings. See 28 U.S.C. § 157(b)(2)(F). By including "arising under" bankruptcy jurisdiction in the 1978 Reform Act, Congress intended to replicate "arising under" federal question jurisdiction, embodied in id. § 1331. See H.R. REP. NO. 95-595, at 445 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6400. See generally 1 COLLI\textsuperscript{er} (15th ed.), supra note 40, ¶ 3.01[4][c][ii]; 1 NORTON, supra note 21, § 4.38, at 4-225 to -231.

\textsuperscript{408} See 1 COLLI\textsuperscript{er} (15th ed.), supra note 40, ¶ 3.01[4][c][iv], at 3-27; 1 NORTON, supra note 21, § 4:38, at 4-231. An example is allowance or disallowance of a creditor's disputed claim against the debtor's estate. The underlying dispute as to the claim itself could be grounded upon a traditional state-law cause of action. Yet, allowance of claims against a bankruptcy estate traditionally has been regarded as an integral part of the in re process of distributing the assets of the bankruptcy estate, distinct from a nonbankruptcy adjudication of the claim. See Katchen v. Landy, 382 U.S. 323, 329-30 (1966) ("'The whole process of proof, allowance, and distribution is, shortly speaking, an adjudication of interests claimed in a res,' and thus falls within the principle ... that bankruptcy courts have summary jurisdiction to adjudicate controversies relating to property within their possession." (citation omitted) (quoting Gardner v. New Jersey, 329 U.S. 565, 574 (1947))); see also Langenkamp v. Culp, 498 U.S. 42, 44 (1990) ("[T]he claims-allowance process ... is integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction."); Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 57-59 (1989). Thus, claims allowance proceedings are considered "arising in" core proceedings and are also expressly included within the statutory list of core proceedings. See 28 U.S.C. § 157(b)(2)(B);
An action between non-debtors, such as a suit by a creditor to recover its claim from a personally responsible third party, cannot be considered a core proceeding. The creditor’s cause of action is founded on nonbankruptcy law making the non-debtor personally liable to the creditor, and such a non-debtor action would exist in exactly the same form irrespective of the debtor’s bankruptcy proceedings. At best, then, such an action could be a non-core proceeding “related to” the debtor’s bankruptcy case, but outside the scope of a bankruptcy court’s core jurisdiction to adjudicate. In fact, the two prototypical non-core, “related to” proceedings are (1) an action by a debtor against a third party, such as the breach of contract suit at issue in Marathon, and (2) suits between non-debtors that could have an effect on the bankruptcy estate. The Supreme Court in Celotex cited these two examples of “related to” proceedings and said that “[t]he instant case involves the second type of ‘related to’ proceeding.”

If the non-debtor action sought to be stayed in Celotex was only “related to” the debtor’s bankruptcy case, this might lead one to believe that the non-debtor stay at issue in the Celotex case must be a non-core, “related to” proceeding, outside the core jurisdiction of the bankruptcy court. Likewise, in determining jurisdiction to temporarily stay a non-debtor action, both the Supreme Court and lower courts have framed the issue as whether the action is “related to” the bankruptcy case—that could also lead one to believe that a temporary stay of such a “related to” proceeding must likewise be a non-core, “related to” matter. Indeed, that was the approach of the dissenting opinion in Celotex. This line of reasoning, though, loses sight of the historical distinction between jurisdiction to adjudicate the dispute underlying an action and jurisdiction to provisionally enjoin that action in order to preserve the status quo.

A temporary status quo injunction simply does not adjudicate the parties’ underlying dispute. Thus, jurisdiction to temporarily stay

Wood v. Wood (In re Wood), 825 F.2d 90, 97 (5th Cir. 1987); 1 Collier (15th ed.), supra note 40, ¶ 3.01(4)[c][iv], at 3-27.
410. See 1 Collier (15th ed.), supra note 40, ¶¶ 3.01(4)[c][ii], at 3-23, 3.02[2], at 3-33.
412. See supra Part IV.D.
413. Starting from the proposition that the judgment creditor’s non-debtor action against Celotex’s surety was a “related to” proceeding, the dissent concluded that the jurisdictional statute that gives bankruptcy courts jurisdiction to “hear and determine” core matters, 28 U.S.C. § 157(b)(1) (1994) (quoted supra note 394), and jurisdiction only to “hear” (but not “determine”) non-core, “related to” proceedings, id. § 157(c)(1) (quoted supra note 397), does not give bankruptcy courts jurisdiction to enter a binding injunctive order directed at such a non-core, “related to” proceeding. Celotex, 514 U.S. at 317-24 (Stevens, J., dissenting).
414. The Celotex majority opinion hinted at this idea in a footnote that (1) raised, but left unresolved, the core/non-core issue, and (2) responded to the dissent’s argument, discussed
an action is not dependent upon jurisdiction to adjudicate the parties' controversy. Under the 1898 Act, status quo injunctions for the preservation of the estate (including protection of a reorganization endeavor) were so intimately connected to administration of the estate that they were within the summary jurisdiction of courts of bankruptcy (including referees), even with respect to actions that could be adjudicated only through a plenary suit.\footnote{415} Likewise, under the current jurisdictional scheme, a temporary non-debtor stay, premised upon preservation of a debtor's reorganization effort, is properly considered a core “matter[,] concerning the administration of the estate,”\footnote{416} even though the action being stayed is outside the bankruptcy court's core jurisdiction to adjudicate. Such a status quo injunction could well be considered a proceeding “arising under” the Bankruptcy Code, because the authority to issue such an injunction comes from section 105 of the Bankruptcy Code. Alternatively, the non-debtor stay is a proceeding uniquely “arising in” the bankruptcy reorganization case that has no separate existence absent the reorganization proceedings.\footnote{417} Even though the collateral non-debtor suit is one with an

\textit{supra} note 413, that the bankruptcy court was without jurisdiction to stay a “related to” proceeding that it could not “determine.” See \textit{Celojetx}, 514 U.S. at 309 n.7 (Rehnquist, C.J.). The majority de-emphasized that portion of the statute relied upon by the dissent that gives bankruptcy courts jurisdiction only to “hear” (but not “determine”) non-core, “related to” proceedings, and emphasized that portion of the statute that reserves to the district court jurisdiction to enter any “final order or judgment” in a non-core, “related to” proceeding. See 28 U.S.C. § 157(c)(1), quoted \textit{supra} note 397. Thus, the majority opined that the statute does not necessarily deprive a bankruptcy court of jurisdiction to temporarily stay a non-core, “related to” proceeding, because such a temporary stay is an interlocutory order, not a final order. See \textit{Celojetx}, 514 U.S. at 309 n.7; accord \textit{In re Davis}, 730 F.2d 176, 183 (5th Cir. 1984); Lesser v. A-Z Assocs. (\textit{In re Lion Capital Group}), 46 B.R. 850, 854 (Bankr. S.D.N.Y. 1985). This response is perhaps dangerously simplistic in ignoring the difference between a stay entered by the court presiding over the collateral litigation, which would be an interlocutory order, and a stay of collateral litigation entered by the bankruptcy court. The unique nature of bankruptcy proceedings has led to the development of more liberal standards of finality for purposes of appeal from orders in bankruptcy proceedings. See generally 1 \textit{Collier} (15th ed.), \textit{supra} note 40, § 5.07[1][b]; John P. Hennigan, Jr., \textit{Toward Regularizing Appealability in Bankruptcy}, 12 BANKR. DEV. J. 583 (1996). Consequently, a bankruptcy court order temporarily staying collateral litigation between non-debtors may be a final, appealable order. See Lomas Fin. Corp. v. Northern Trust Co. (\textit{In re Lomas Fin. Corp.}), 932 F.2d 147, 150-52 (2d Cir. 1991); Gathering Restaurant, Inc. v. First Nat'l Bank (\textit{In re Gathering Restaurant, Inc.}), 79 B.R. 992, 997-98 (Bankr. N.D. Ind. 1986). The majority's point, though, is essentially a restatement of the historical distinction between jurisdiction to “determine” or adjudicate a matter and jurisdiction to temporarily stay a collateral suit involving the matter. A temporary status quo injunction of collateral litigation does not “determine” or adjudicate any of the claims raised in the collateral litigation.

\footnote{415} See \textit{supra} Part IV.B.


\footnote{417} The \textit{Celojetx} dissent expressed concern that this approach to core jurisdiction is a “jurisdictional bootstrap,” giving bankruptcy courts core jurisdiction to do anything and everything a party might request pursuant to § 105. 514 U.S. at 326-27 (Stevens, J., dissenting). In the context of non-debtor stays, the bootstrap is cut by the jurisdictional prerequisite that the non-debtor action pose a threat to the debtor's reorganization efforts. In addition, recognition of the crucial jurisdictional differences between a temporary non-debtor stay and a permanent non-debtor release, discussed \textit{infra} Part IV.G, would check the unlimited jurisdiction phenomenon that seems implicit in many courts' use of § 105 powers.
existence independent of the bankruptcy proceedings, a temporary stay of the non-debtor action does not involve the sort of adjudication of an independent action that motivated the Marathon holding and the subsequent core/non-core dichotomy.\(^{418}\) The bankruptcy proceed-

\(^{418}\) In addition to introducing the core/non-core division of bankruptcy jurisdiction, the BAFJA amendments also repealed the following provision of the Reform Act: “A bankruptcy court shall have the powers of a court of equity, law and admiralty, but may not enjoin another court . . . .” Pub. L. No. 95-598, § 241(a), 92 Stat. 2549, 2671 (1978) (enacting 28 U.S.C. § 1481 (1982) (repealed 1984)). Giving bankruptcy courts the powers of a court of equity, law, and admiralty was seen as a “concomitant of the bankruptcy courts [sic] increased jurisdiction” and “in addition to any power granted . . . under section 105 of the bankruptcy code.” H.R. REP. No. 95-595, at 448 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6404. This broader supplementary § 1481, then, rather than § 105, became the repository of the proviso, carried forward from § 105’s predecessor, prohibiting bankruptcy courts from enjoining another court. See supra notes 312, 342, and 361. Subsequent retraction of the bankruptcy court’s jurisdiction, necessitated by Marathon, resulted in repeal of § 1481 by the BAFJA amendments. See Pub. L. No. 98-353, § 113, 98 Stat. 333, 343 (1984). Mysteriously, though, § 1481 was repealed in its entirety, including the proviso limiting restraint of another court. The Celotex dissenting opinion attached great significance to this proviso and its subsequent repeal, apparently believing that the proviso denied bankruptcy courts the power to enjoin even the litigants before another court. See Celotex, 514 U.S. at 320-23 n.9, 327-29 (Stevens, J., dissenting); see also Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 85 n.37 (1982) (Brennan, J., plurality opinion) (erroneously equating scope of the § 1481 proviso with that of the Anti-Injunction Act, which forbids restraint of litigants). Of course, this interpretation completely misperceives the history of the proviso and its limited scope. Its predecessor under the 1898 Act only restricted a referee’s ability to directly restrain another court, not the parties to collateral litigation before another court. See supra note 342. Nothing in the legislative history indicates that Congress intended the proviso to have any other meaning under the Reform Act. See, e.g., Bankruptcy Court Revision: Supplementary Hearings on Courts and Administrative Structure for Bankruptcy Cases Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary, 95th Cong. 81-82 (1977) (testimony of Louis W. Levit, Esq., Chairman, Special Committee on the National Bankruptcy Act of the Commercial Law League of America) (“[T]he limitation on the injunctive powers would be intended to refer primarily, if not solely, to the power to enjoin another court . . . . It is, as we all know, extremely rare that such power is sought. It’s even more rare that it’s exercised by a district court today.”); see also Frank R. Kennedy, The Bankruptcy Court Under the New Bankruptcy Law: Its Structure and Jurisdiction, 55 AM. BANKR. L.J. 63, 90 (1981) (“Since the bankruptcy court can enjoin parties in litigation in other courts, the disability to enjoin other courts does not augur any serious difficulty.”) (footnote omitted)). In addition, courts construed the Reform Act proviso in exactly the same limited manner as under the 1898 Act. See, e.g., In re Davis, 730 F.2d 176, 183-84 (5th Cir. 1984); Davis v. Sheldon (In re Davis), 691 F.2d 176, 177 n.5 (3d Cir. 1982); Bank of Commonwealth v. Bevan, 13 B.R. 899, 995 n.11 (E.D. Mich. 1981); Apollo Molded Prods., Inc. v. Kleinman (In re Apollo Molded Prods., Inc.), 83 B.R. 189, 191 (Bankr. D. Mass. 1988); Cournoyer v. Town of Lincoln (In re Cournoyer), 43 B.R. 354, 360 n.7 (Bankr. D.R.I. 1984), aff’d in part, rev’d in part, 53 B.R. 478 (D.R.I. 1985), aff’d, 790 F.2d 971 (1st Cir. 1986); Redenbaugh v. Gahle (In re Redenbaugh), 37 B.R. 383, 385 (Bankr. C.D. Ill. 1984). But see Stuart Motel, Inc. v. Columbia Banking Savs. & Loan Ass’n (In re Stuart Motel, Inc.), 15 B.R. 28, 30 (Bankr. S.D. Fla. 1981) (relying erroneously on Anti-Injunction Act cases).

Proceeding from this erroneous assumption about the reach of the § 1481 proviso, the Celotex dissent then concluded that repeal of § 1481, in its entirety, should be construed as removing the only source of authority for bankruptcy courts to enjoin proceedings in other courts. See Celotex, 514 U.S. at 329 (Stevens, J., dissenting). This conclusion ignores the fact that § 1481 was a new, supplementary provision, and the primary source of a bankruptcy court’s power to enjoin collateral litigation under the 1898 Act was the predecessor to current Bankruptcy Code § 105, which of course, remains intact. See supra note 312 and accompanying text. Thus, Congress’ failure to reenact the proviso regarding restraint of another court when repealing § 1481 is best explained as an oversight. Nonetheless, it should not prove too troublesome, as direct restraint of another court is rarely necessary, and even federal district courts operate under a general rule
ing to stay the non-debtor action is distinct from the collateral
non-debtor litigation itself, as is the jurisdictional basis for each proceed-
ing, and a temporary non-debtor stay issued by a bankruptcy court is
properly considered a core proceeding.419

In the context of non-debtor stays, the distinction between juris-
diction to enjoin and jurisdiction to adjudicate has been blurred and
confused by the 1898 Act cases that refused to stay non-debtor actions
based on lack of jurisdiction to adjudicate420 and by the Bankruptcy
Code cases' misleading use of the "related to" terminology to describe
jurisdiction to stay non-debtor actions. Nonetheless, since enactment
of the BAFJA amendments, the lower courts that have confronted the
issue, for the most part, have correctly concluded that temporary non-
debtor stays are within the core jurisdiction of bankruptcy judges.421

that they should not enjoin another court if restraint of the parties would suffice. See W.K.
Ingram v. Martrac Farms, Inc., (In re Hurley), 553 F.2d 1096, 1102-03 (8th Cir. 1977); cf. State St.
(concluding that because "nothing short of enjoining the state court would appear capable of
completely stopping the proceedings here," and "[g]iven the uncertainty on this jurisdictional
question and the absence of precedent for injunctions directed specifically at state courts and
their judges, as opposed to the parties," then "any injunctive relief at this stage of the proceeding
would require an order entered by the district court").

419. The Celotex majority acknowledged this approach:

We recognize the theoretical possibility of distinguishing between the proceeding to
execute on the bond in the Fifth Circuit and the § 105 stay proceeding in the Bankruptcy
Court in the Eleventh Circuit. One might argue, technically, that though the proceeding to
execute on the bond is "related to" the title 11 case, the stay proceeding "arises under" title 11,
or "arises in" the title 11 case. We need not and do not decide this question here.

514 U.S. at 311 n.8 (citation omitted). Professor Zaretzky also concluded that temporary stay of
a non-debtor action should be considered a core proceeding within the jurisdiction of a bank-
ruptcy court to hear and determine. See Zaretzky, supra note 40, at 213, 222-23 nn.31 & 33.

420. See supra Part IV.C.

421. See Davis, 730 F.2d at 182-83 (applying substantially similar provisions of the Emer-
gency Rule); LTV Corp. v. Miller (In re Chateaugay Corp.), 109 B.R. 613, 620-21 (S.D.N.Y.
1990); Stadium Management Corp. v. Connecticut Bank & Trust Co. (In re Stadium Manage-
(In re Johns-Manville Corp.), 40 B.R. 219, 229-30 (S.D.N.Y. 1984) (applying Emergency Rule);
1996); New Magma Irrigation & Drainage Dist. v. Board of Supervisors (In re New Magma
Irrigation & Drainage Dist.), 193 B.R. 528, 531-33 (Bankr. D. Ariz. 1994); Carabetta Enters.,
Inc. v. City of Asbury Park (In re Carabetta Enters., Inc.), 162 B.R. 399, 403-04 (Bankr. D.
Conn. 1993); Sudbury, Inc. v. Escott (In re Sudbury, Inc.), 140 B.R. 461, 464 (Bankr. N.D. Ohio
1992); Deltacorp, Inc. v. Office of Thrift Supervision (In re Deltacorp, Inc.), 111 B.R. 419, 420-21
(Bankr. S.D.N.Y. 1990); Cardinal Indus., Inc. v. Buckeye Fed. Sav. & Loan Ass'n (In re Cardinal
Indus., Inc.), 102 B.R. 991, 993 (Bankr. S.D. Ohio 1989); Gathering Restaurant, Inc. v. First Nat'l
Bank (In re Gathering Restaurant, Inc.), 199 B.R. 992, 997-98 (Bankr. N.D. Ind. 1996); In re
Monroe Well Serv., Inc., 67 B.R. 746, 753-54 (Bankr. E.D. Pa. 1986); Rustic Mfg., Inc. v. Marine
Bank Dane County (In re Rustic Mfg., Inc.), 55 B.R. 25, 28-30 (Bankr. W.D. Wis. 1985); Lesser
Abrams (In re HBG Servicenter, Inc.), 45 B.R. 668, 671 (Bankr. E.D.N.Y. 1985); cf. Manville
Corp. v. Equity Sec. Holders Comm. (In re Johns-Manville Corp.), 801 F.2d 60, 64 (2d Cir. 1986)
("[I]n our view, if the bankruptcy court may ever use its equitable powers under section 105(a)
to enjoin actions pursued in other courts as [core proceedings] 'concerning the administration of
the estate' under [28 U.S.C.] section 157(b)(2)(A), it may exercise that power where there is a
basis for concluding that rehabilitation, the very purpose for the bankruptcy proceedings, might
be undone by the other action."). But see Clark Oil & Ref. Co. v. Chickasaw Pipe Line Co. (In re
G. Jurisdiction to Permanently Release Non-Debtors

For purposes of jurisdiction and the historical distinction between jurisdiction to enjoin and jurisdiction to adjudicate, temporary non-debtor stays must be distinguished from permanent non-debtor releases. While there is bankruptcy jurisdiction to temporarily stay a non-debtor action, there is no jurisdiction to permanently release a non-debtor action. Notwithstanding the confusion that the Celotex majority and dissenting opinions generate, the lower courts appear to have resolved adequately the issue of jurisdiction to temporarily stay non-debtor actions. They have not had similar success, however, with respect to jurisdiction to release and permanently enjoin non-debtor actions.

Courts disapproving non-debtor releases only occasionally assert lack of jurisdiction as a basis.\(^{422}\) On the other side of the issue, the Robins and Drexel releases were approved with little more than a passing mention of the courts’ jurisdiction,\(^{423}\) and there is very little in the way of analytical reasoning from either camp. Most courts, without regard to their view of the propriety of non-debtor releases, simply have applied to non-debtor releases the same jurisdictional framework used in temporary non-debtor stay cases: jurisdiction depends on whether the non-debtor action is “related to” the debtor’s reorganization case—“related to” meaning that continuation of the non-debtor action will make the debtor’s reorganization more difficult in some way—and the non-debtor release is a core proceeding respecting administration of the debtor’s estate and confirmation of the debtor’s plan of reorganization.\(^ {424}\)


As is true with temporary non-debtor stays, this jurisdictional threshold, as distinguished from the propriety of the release on the merits, usually is not difficult to meet. Prosecution of non-debtor actions might adversely impact the debtor’s reorganization in any number of ways, especially when courts consider potential loss of some contribution a non-debtor is willing to make to the debtor’s reorganization in exchange for a non-debtor release.\textsuperscript{425} Thus, this approach usually leads to the conclusion that a bankruptcy court has core jurisdiction to approve a non-debtor release.\textsuperscript{426} This approach, however, is fundamentally flawed, as it permits an oblique enlargement of courts’ bankruptcy jurisdiction. It abuses the historical distinction between jurisdiction to enjoin and jurisdiction to adjudicate, and it improperly assumes that facilitation of the debtor’s reorganization effort is an independent basis on which to adjudicate a non-debtor action. Most importantly, it ignores the Supreme Court case of \textit{Callaway v. Benton},\textsuperscript{427} which refused to take the \textit{Continental Illinois} reasoning beyond status quo injunctions to permanent non-debtor injunctions.

\textbf{1. The Indirect Jurisdictional Enlargement}

Jurisdiction to permanently release a non-debtor action is \textit{not} the equivalent of jurisdiction to temporarily stay a non-debtor action. The error in the two concepts is that it unthinkingly incorporates the historical distinction between jurisdiction to enjoin and jurisdiction to adjudicate. That distinction has shaped and is at the heart of the jurisdiction of bankruptcy courts to issue far-reaching status quo injunctions, touching matters well beyond their jurisdiction to adjudicate. In the case of a permanent non-debtor release and injunction, however, the distinction between jurisdiction to enjoin and

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\textsuperscript{425} See supra notes 120, 233, and accompanying text.

\textsuperscript{426} This reasoning appears to be the basis on which the \textit{Robins} and \textit{Drexel} courts found jurisdiction to approve the releases in those cases. See supra note 423.

\textsuperscript{427} 336 U.S. 132 (1949), discussed infra Part IV.G.2.
jurisdiction to adjudicate disappears, because the injunction does adjudicate. A non-debtor release is not a mere status quo injunction; a non-debtor release effectively adjudicates the released non-debtor action. The release operates as an adjudication on the merits, fully binding for res judicata/preclusion purposes.\footnote{See supra note 1 and accompanying text. In terms of Chief Justice Rehnquist’s formulation of the distinction between jurisdiction to enjoin and jurisdiction to adjudicate, discussed supra note 414, although stay of a non-debtor action is only interlocutory as to that collateral action, a non-debtor release is final.}

The non-debtor actions that are “adjudicated” through non-debtor releases are, at best, non-core, “related to” actions, beyond the power of a bankruptcy judge to determine by final order without consent of the litigants.\footnote{See supra Part IV.E.} Final resolution of such an action by a non-Article III bankruptcy judge, whether it be by traditional adjudication on the merits or by nonconsensual release, certainly approximates the sort of adjudication held unconstitutional in Marathon—closely enough, that is, to warrant a construction of the jurisdictional statute that denies bankruptcy courts core jurisdiction to approve non-debtor releases.\footnote{It is axiomatic that in the absence of a clear expression of congressional intent, a statute should be construed to avoid difficult constitutional questions. This approach applies equally to construction of bankruptcy statutes, see United States v. Security Indus. Bank, 459 U.S. 70, 82 (1982), and with special force in construing the reach of a non-Article III bankruptcy judge’s core jurisdiction, see In re Castlerock Properties, 781 F.2d 159, 162 (9th Cir. 1986) (noting that courts “should avoid characterizing a proceeding as ‘core’ if to do so would raise constitutional problems”).} By using their section 105 powers to release non-debtor actions they could not adjudicate directly, bankruptcy courts violate the cardinal principle that a court’s “in aid of jurisdiction” powers cannot be used to expand the court’s jurisdictional reach.\footnote{See 11 U.S.C. § 105(e) (1994), discussed supra note 271 and accompanying text; see also 9 Moore, supra note 60, ¶ 110.29, at 359 (stating that the All Writs Act “authorizes issuance of writs only in aid of the court’s jurisdiction, and confers on the district courts no original jurisdiction” (footnote omitted)).}

An even more troubling enlargement of jurisdiction through non-debtor releases\footnote{Limitations on a bankruptcy court’s core jurisdiction are not implicated where the district court enters the final order approving non-debtor release and injunction provisions. For example, the district court presided over the A.H. Robins reorganization and approved the Robins non-debtor releases. See In re A.H. Robins Co., 88 B.R. 742, 751-55 (E.D. Va. 1988), aff’d sub nom. Menard-Sanford v. Mabey (In re A.H. Robins Co.), 880 F.2d 694, 700-02 (4th Cir. 1989). Likewise, § 524(g) seems to avoid this jurisdictional problem by requiring the district court to issue or affirm permanent injunctions restraining non-debtor asbestos claims. See 11 U.S.C. § 524(g)(3)(A).} lies in the fact that many of these released non-debtor actions arguably fall completely outside “related to” jurisdiction to adjudicate. A non-debtor action that is not “related to” the debtor’s bankruptcy case cannot be adjudicated by either a bankruptcy court (by consent) or a district court, and therefore, neither a bankruptcy court nor a district court can properly “adjudicate” such a
non-debtor action through a non-debtor release.433 This is another reason why the courts' use of the "related to" terminology to describe jurisdiction to temporarily stay non-debtor actions is so pernicious.434 As applied by the courts, the "related to" standard for adjudication of a non-debtor action is very different from the "related to" standard for temporary stay of a non-debtor action.435 When confronted with a straightforward request to adjudicate a non-debtor action, rather than temporarily stay or permanently release it, the courts have concluded that many of these non-debtor actions are not sufficiently "related to" the debtor's reorganization to provide jurisdiction to adjudicate. A good example is the seminal case on "related to" jurisdiction, Pacor, Inc. v. Higgins.436

That case involved an asbestos personal injury suit in state court against an asbestos supplier, Pacor, Inc. In that suit, Pacor filed a third-party indemnification complaint against Johns-Manville Corporation, the original manufacturer of the asbestos. When Johns-Manville filed its Chapter 11 petition, Pacor sought to (1) remove the entire action to federal court as "related to" Manville's bankruptcy case,437 and (2) transfer the action to the district in which Manville's Chapter 11 proceedings were pending. If successful, then, both the personal injury claim against Pacor and Pacor's potential indemnification claim against Manville could be heard in the same forum, but only if the non-debtor action against Pacor was "related to" Manville's Chapter 11 case.438

Those courts approving non-debtor releases have placed great weight on the effect of potential contribution and indemnification claims against the debtor and the need to eliminate such claims by releasing creditors' non-debtor actions, such as the non-debtor asbestos personal injury claim against Pacor.439 Indeed, the proclaimed adverse effects of these contribution/indemnification claims on the

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433. This analysis is limited to that federal bankruptcy jurisdiction contained in 28 U.S.C. § 1334(b) (1994). Whether a federal court can, as an incident to such bankruptcy jurisdiction, adjudicate matters outside the bounds of the statutory grant through doctrines of supplemental jurisdiction is a matter of considerable doubt. See Susan Block-Lieb, The Case Against Supplemental Bankruptcy Jurisdiction: A Constitutional, Statutory, and Policy Analysis, 62 FORDHAM L. REV. 721 (1994); Fruchwald, supra note 269, at 23-33.

434. See supra text accompanying note 420.

435. Previous efforts to explain jurisdiction to enjoin non-debtor actions have been stymied by a failure to fully appreciate this divergence. See, e.g., Buschman & Madden, supra note 272, at 923-29 (equating "related to" jurisdiction to adjudicate with jurisdiction to enjoin non-debtor actions); cf. Block-Lieb, supra note 433, at 735-37 & n.91 (analyzing non-debtor stay cases against backdrop of jurisdiction to adjudicate and concluding that the non-debtor stay cases "possibly exceed[ ] the statutory mandates of 28 U.S.C. § 1334(b)").

436. 743 F.2d 984 (3d Cir. 1984).

437. The current version of the bankruptcy removal statute, which is substantially the same as the one at issue in Pacor, provides that "[a] party may remove any claim or cause of action in a civil action . . . to the district court for the district where such civil action is pending, if such district court has [bankruptcy] jurisdiction of such claim or cause of action." 28 U.S.C. § 1452(a).

438. See Pacor, 743 F.2d at 986.

439. See supra Part III.C.1.
debtor's ability to reorganize presumably means the underlying non-debtor action that gives rise to a contribution/indemnification claim is "related to" the debtor's bankruptcy case, under the "related to" standard developed in the non-debtor stay context. When that standard is mechanically transferred to the non-debtor release context, then, it appears that there is jurisdiction to "adjudicate" the non-debtor action through a non-debtor release. Yet, the Third Circuit held that the potential for an indemnification claim by Pacor against Manville's bankruptcy estate did not give federal courts "related to" bankruptcy jurisdiction to adjudicate the non-debtor action against Pacor.\(^440\)

Since Pacor, courts have not agreed on the circumstances under which a non-debtor action will fall within "related to" jurisdiction to adjudicate.\(^441\) Still, non-debtor actions of all kinds are permanently

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\(^{440}\) See Pacor, 743 F.2d at 995-96. In determining whether the non-debtor asbestos personal injury claim against Pacor was "related to" Manville's Chapter 11 proceedings, the Third Circuit set forth the dominant expression of the meaning of "related to" jurisdiction to adjudicate:

"[T]he test for determining whether a civil proceeding is related to bankruptcy is whether the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy . . . . An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankruptcy estate." Id. at 994. However, the court limited this broad statement by also stating that "the mere fact that there may be common issues of fact between a civil proceeding and a controversy involving the bankruptcy estate does not bring the matter within the scope of [related to] jurisdiction. Judicial economy itself does not justify federal jurisdiction." Id.

In Celotex, without adopting any particular test, the Supreme Court noted that the First, Fourth, Fifth, Sixth, Eighth, Ninth, Tenth, and Eleventh Circuits have adopted the Pacor test for "related to" jurisdiction, and that the Second and Seventh Circuits have a slightly different test. Celotex Corp. v. Edwards, 514 U.S. 300, 308-09 n.6 (1995). Nonetheless, the Court agreed with so much of the Pacor opinion as stated that "Congress intended to grant comprehensive jurisdiction to the bankruptcy courts so that they might deal efficiently and expeditiously with all matters connected with the bankruptcy estate." Id. at 308 (quoting Pacor, 743 F.2d at 994). The fact that most circuits have nominally adopted the Pacor test masks great disparities in their views as to its proper application. See Block-Lieb, supra note 433, at 735-37; Fruchwald, supra note 269, at 6-22; see also infra note 441 and accompanying text.

\(^{441}\) Compare National City Bank v. Coopers & Lybrand, 802 F.2d 990, 993-94 (8th Cir. 1986) (holding that there was no jurisdiction over a non-debtor professional malpractice action, because it was "at most a precursor to potential indemnification action" against the debtor), with Lindsey v. O'Brien, Tanski, Tanzer & Young Health Care Providers (In re Dow Corning Corp.), 86 F.3d 482, 490-94 (6th Cir. 1996) (holding that potential indemnification and contribution claims against the debtor by co-defendants in breast implant litigation were sufficient to give "related to" jurisdiction over non-debtor actions against the co-defendants), and Wood v. Wood (In re Wood), 825 F.2d 90, 94 (5th Cir. 1987) (holding that there was "related to" jurisdiction over a non-debtor action that alleged joint conduct on the part of debtor and non-debtors), and Kelley v. Nodine (In re Salem Mortgage Co.), 783 F.2d 626, 635 (6th Cir. 1986) (holding that there was "related to" jurisdiction over non-debtor actions where the parties to the challenged transactions were "more intertwined than the parties in Pacor"). See also Zerand-Bernal Group, Inc. v. Cox, 23 F.3d 159, 164 (7th Cir. 1994) (noting that the "larger question, on which the courts are divided, whether a suit that might trigger a related suit . . . is itself therefore a 'related' action"); Sykes v. Texas Air Corp., 834 F.2d 488, 488 n.2 (5th Cir. 1987) (noting that the existence of "related to" jurisdiction over a non-debtor action "probably turns on the precise nature of [non-debtor defendant's] claim against [debtor]"). Compare Pacor, 743 F.2d at 995-96 (distinguishing non-debtor actions on contractual guaranties of a debtor's obligations that are "related to" bankruptcy because of automatic indemnity action against the debtor), with River
extinguished en masse through blanket non-debtor releases, without even a mention of the court's jurisdiction to adjudicate those actions.\footnote{In fact, the extremely broad nature of most non-debtor releases—providing for wholesale release of any and all claims that any creditor or shareholder might have against the released non-debtor—makes a careful and discriminating analysis of jurisdiction to adjudicate each released claim virtually impossible.\footnote{For a rare case where a bankruptcy court recognized this aspect of the jurisdictional defects of non-debtor releases, see \textit{In re Market Square Inn, Inc.}, 163 B.R. 64, 67 (Bankr. W.D. Pa. 1994) (observing a "jurisdictional problem" in approving a non-debtor release, because there is "nothing which gives the bankruptcy court jurisdiction to adjudicate claims between two non-debtor third parties"). For a characteristically perceptive opinion by Learned Hand under the reorganization provisions of the 1898 Act, see \textit{Radin v. Chemical Bank & Trust Co. (In re Prudence Bonds Corp.)}, 75 F.2d 262, 263 (2d Cir. 1935) ("[S]ince this stay is permanent, and not merely to give the debtor or the trustee a chance so to intervene, it can be defended only in case the [non-debtor action] may eventually fall within the jurisdiction in \textit{invitum} of the bankruptcy court."). The Fifth Circuit, in a lengthy exploration of jurisdiction to approve a permanent non-debtor release and injunction as part of a debtor's settlement with its liability insurer, identified jurisdiction to approve the non-debtor release as dependent upon "related to" jurisdiction to adjudicate the released non-debtor actions. See \textit{Feld v. Zale}, 62 F.3d at 751-57. Yet, the court then incorrectly held that "related to" jurisdiction to adjudicate released non-debtor actions would give a bankruptcy court (as opposed to the \textit{district court}) jurisdiction to entertain the request for a permanent non-debtor release and injunction. See \textit{id.} at 757-59; see also \textit{In re Arrowmill Dev. Corp.}, 211 B.R. 497, 501-03 (Bankr. D.N.J. 1997); \textit{In re Sybaris Clubs Int'l, Inc.}, 189 B.R. 152, 155 (Bankr. N.D. Ill. 1995); \textit{cf. Monarch Life Ins. Co. v. Ropes & Gray (In re Monarch Capital Corp.)}, 173 B.R. 31, 37-38 (D. Mass. 1994) (noting that released non-debtor actions are non-core, but holding that non-debtor release is core and failing to recognize or explain the inconsistency), \textit{aff'd}, 65 F.3d 973 (1st Cir. 1995).\footnote{See, e.g., \textit{Monarch Life Ins. Co. v. Ropes & Gray}, 65 F.3d 973, 976 (1st Cir. 1995) (quoting non-debtor release provisions of bankruptcy court's confirmation order: "[T]his Order constitutes an injunction against all persons . . . from . . . commencement or continuation of any action or proceeding arising from or related to a claim against the Debtor . . . against or affecting any of [the released non-debtors]."); \textit{Drexel Burnham Lambert Group, Inc. v. Claimants Identified on Schedule 1 (In re Drexel Burnham Lambert Group, Inc.)}, 995 F.2d 1138, 1144 (2d Cir. 1993) (quoting release provisions as releasing non-debtors "from any and all claims, obligations, rights, causes of action and liabilities which . . . any holder of a Claim against or Equity Interest in the Debtors have asserted or may be entitled to assert . . . in any way relating to the Debtors"); \textit{In re A.H. Robins Co.}, 131 B.R. 292, 294 (E.D. Va. 1991) (quoting non-debtor release provisions of plan of reorganization: 
"[A]ll persons (i) who have held, hold or may hold Claims . . . or (ii) who have held, hold or may hold Robins Common Stock . . . will be deemed to have forever waived, released and discharged all rights or claims . . . which they hereafter possess or may possess against any Person . . . based upon or in any manner arising from or related to . . . the Dalkon Shield."); \textit{rev'd and remanded on other grounds sub nom. Dalkon Shield Claimants Trust v. Reiser (In re A.H. Robins Co.)}, 972 F.2d 77 (4th Cir. 1992).\footnote{\textit{Oaks Ltd. Partnership v. Things Remembered, Inc.}, No. 92 C 7877, 1993 WL 147409, at *2-3 (N.D. Ill. May 3, 1993) (discussing the split in the Seventh Circuit over whether a claim against a debtor's guarantor is "related to" bankruptcy); \textit{compare Feld v. Zale Corp. (In re Zale Corp.)}, 62 F.3d 746, 755-57 (5th Cir. 1995) (concluding that indemnification agreed to as part of a settlement approved by the bankruptcy court was insufficient to confer "related to" jurisdiction over non-debtor actions that might give rise to indemnification claims against debtor), \textit{with Michigan Employment Sec. Comm'n v. Wolverine Radio Co. (In re Wolverine Radio Co.)}, 930 F.2d 1132, 1142-43 (6th Cir. 1991) (concluding that there was "related to" jurisdiction over a non-debtor action because of the debtor's potential indemnification liability arising out of indemnification provisions of a purchase agreement embodied in the plan of reorganization and approved by the bankruptcy court}).}'}
2. Facility in Reorganization and the Forgotten Callaway v. Benton Case

The dominant approach to jurisdiction to permanently release and enjoin non-debtor actions, with its focus on interference with the debtor's reorganization, not only ignores the fact that this permits an indirect "adjudication by release" of non-debtor actions that could not be adjudicated directly, it also implicitly assumes that facilitation of the debtor's reorganization effort is an independent basis on which to adjudicate matters that are otherwise beyond the jurisdiction of the court.\textsuperscript{444} This takes the Continental Illinois notion of a general jurisdiction to protect and promote the debtor's reorganization, beyond status quo injunctions,\textsuperscript{445} to binding alterations of nonbankruptcy rights and obligations between non-debtors. Yet, in Continental Illinois, the Supreme Court repeatedly emphasized the temporary, status quo nature of the injunction at issue.\textsuperscript{446} Moreover, the Court subsequently refused to extend Continental Illinois to permanent alterations of non-debtor rights in Callaway v. Benton.\textsuperscript{447}

Callaway v. Benton, like Continental Illinois, involved railroad reorganization proceedings under the 1898 Act, for the Central of Georgia Railway Company (Central). Central had been leasing certain rail lines from the South Western Railroad Company (South Western) that were very important to Central's long-term operations, and Central wished to acquire these lines from South Western as part of its plan of reorganization. Thus, the plan proposed a purchase of these lines from South Western.\textsuperscript{448} South Western's directors formally re-

\textsuperscript{444} The court made this leap explicitly in Polygram Distribution, Inc. v. B-A Systems, Inc. (In re Burstine-Applebee Co.), 63 B.R. 1011 (Bankr. W.D. Mo. 1986). There, the bankruptcy court recognized that approval of a permanent non-debtor injunction would effectively adjudicate non-core matters, which the court believed would be at odds with the Marathon holding. \textit{See id.} at 1012-15. Nonetheless, the court held that the 1898 Act doctrine of necessity jurisdiction gave it core jurisdiction to issue the permanent non-debtor injunction. \textit{See id.} at 1018-22. As explained infra Part IV.G.2.a, such an application of necessity jurisdiction is suspect in light of Callaway v. Benton, and Marathon makes it doubly suspect. In addition, expansion of bankruptcy jurisdiction, to permit adjudication of non-debtor disputes that affect administration of the estate, makes the continued viability of any residual necessity jurisdiction highly questionable. And, of course, under the 1898 Act the necessity doctrine only provided a basis to actually hear and adjudicate the merits of an action between non-debtors—not to permanently expunge the non-debtor action through a non-debtor release. \textit{See supra} notes 349 and 352.


\textsuperscript{446} \textit{See Continental Illinois}, 294 U.S. at 679 ("[W]ithout the maintenance of the status quo for a reasonable length of time no satisfactory plan could be worked out."); \textit{id.} at 681 ("[S]ole point is as to the authority of the bankruptcy court to delay for a reasonable time an interference with the reorganization proceeding."); \textit{id.} at 685 ("It contemplates, as we have already suggested, only reasonable delay.").

\textsuperscript{447} 336 U.S. 132 (1949).

\textsuperscript{448} \textit{See} Benton v. Callaway, 165 F.2d 877, 878-80 (5th Cir. 1948), aff'd, 336 U.S. 132 (1949). In order to induce South Western to sell, Central's plan of reorganization provided that, in the event South Western did not sell, Central would reject its lease of these lines. \textit{See} 336 U.S. at 134-35.
solved to accept Central’s plan, subject to approval by a majority of South Western’s shareholders, who subsequently approved the plan by a two-thirds majority vote. Two of South Western’s dissenting minority shareholders, however, brought suit in state court seeking to enjoin South Western’s sale of its lines to Central. The minority shareholders contended that the sale of these lines to Central was a sale of substantially all of South Western’s assets, requiring unanimous approval of all of South Western’s shareholders pursuant to applicable Georgia state law.\textsuperscript{449}

On the authority of \textit{Continental Illinois}, the district court presiding over the reorganization proceedings permanently enjoined the state court suit. The reorganization court based its permanent injunction on a finding that “[t]he purpose, and, if the state court injunction had been allowed to stand, the effect of the suit . . . in the State Court, was to completely disrupt the reorganization proceeding by preventing the consummation of the plan.”\textsuperscript{450} The reorganization court went on to decide that “[i]n the exigencies which confront the South Western, it clearly has power to sell its property to the newly Reorganized Company without the unanimous consent of its stockholders.”\textsuperscript{451} The Supreme Court, in reversing the reorganization court, addressed two different aspects of the reorganization court’s decision: jurisdiction to adjudicate the non-debtor dispute\textsuperscript{452} and jurisdiction to permanently enjoin the collateral non-debtor action.\textsuperscript{453}

a. Jurisdiction to Adjudicate a Non-Debtor Action

The Supreme Court held that the reorganization court erred in adjudicating this non-debtor dispute “requir[ing] a determination of the rights of the stockholders of South Western inter se to sell” South Western’s lines to Central.\textsuperscript{454} This was a non-debtor dispute, outside the jurisdiction of the reorganization court, involving “internal management of the lessor . . . not properly subject to the court’s control.”\textsuperscript{455} In response to the assertion that the reorganization court could adjudicate the non-debtor dispute because its resolution was important to the debtor’s reorganization, the Court rejected the idea that the \textit{Continental Illinois} line of cases supported jurisdiction to adjudicate this non-debtor dispute:

\textsuperscript{449} See 165 F.2d at 885-86 n.2 (Hutcheson, C.J., dissenting opinion) (setting forth findings of fact of the district court presiding over the reorganization proceedings), aff’d, 336 U.S. at 135-36.

\textsuperscript{450} Id. at 887 n.4 (Hutcheson, C.J., dissenting opinion) (setting forth conclusions of law of the reorganization court).

\textsuperscript{451} Id. at 888 n.4 (Hutcheson, C.J., dissenting opinion) (setting forth conclusions of law of the reorganization court).

\textsuperscript{452} See 336 U.S. at 141-51.

\textsuperscript{453} See id. at 136-41.

\textsuperscript{454} Id. at 143.

\textsuperscript{455} Id. at 144.
No suggestion has been made that a final decision of the state law question will be unreasonably delayed. Under these circumstances, we do not believe that the [Continental Illinois] decision provides any support for the district court’s action. . . . Unless the offer is a sham and the lessor’s discretion illusory, the plan may be effectively consummated whether the offeree accepts or not. The district court did not merely postpone action which would have hindered the development of the plan; it took to itself the decision of a question which the plan left open for decision elsewhere.\(^{456}\)

The Callaway opinion is somewhat ambiguous on the question of whether Continental Illinois and facilitation of the debtor’s reorganization provide an independent basis for a federal bankruptcy court to adjudicate a non-debtor controversy otherwise outside its jurisdiction. Nonetheless, it suggests that this may be an improper basis on which to premise jurisdiction to finally adjudicate a non-debtor dispute, because it does more than “merely postpone” the non-debtor action pending formulation of a plan of reorganization.\(^{457}\) Likewise, many modern cases reject accommodation of the debtor’s reorganization effort as an independent basis on which to adjudicate a non-debtor dispute, characterizing it as jurisdiction without limits.\(^{458}\)

\(^{456}\) Id. at 149-50 (emphasis added).

\(^{457}\) It is unclear whether the Court would have allowed adjudication by the reorganization court if the terms of the plan made its entire consummation subject to acquisition of the South Western lines or if there were some other showing that resolution of the dispute was important to progress of the reorganization. The reorganization court and the dissent in the Fifth Circuit seemed to believe that such a showing had been made. See supra notes 450-51 and accompanying text for the reorganization court’s findings. See also Benton v. Callaway, 165 F.2d 877, 884 (5th Cir. 1948) (Hutcheson, C.J., dissenting opinion) (characterizing the acquisition of South Western lines as “vital to the reorganization” based upon the reorganization court’s findings), aff’d, 336 U.S. 132 (1949). This lends support to a reading of the Callaway opinion that such a showing is irrelevant to jurisdiction to adjudicate the non-debtor action.

\(^{458}\) A forceful articulation of this view is contained in Holland Industries, Inc. v. United States (In re Holland Industries, Inc.), 103 B.R. 461 (Bankr. S.D.N.Y. 1989). In that case, the Chapter 11 debtor sought to have the bankruptcy court vacate IRS liens on the property of certain non-debtors, because the debtor contemplated using that property to help finance its plan of reorganization, and alleged that “unless the liens are vacated prior to the confirmation hearing, confirmation of the plan will be ‘substantially impeded, if not defeated.’” Id. at 463-64. The bankruptcy court rejected this asserted adverse effect on the debtor’s reorganization as a jurisdictional basis for passing on the validity of the IRS liens:

The Debtor’s assertion that confirmation of its plan is impacted by the IRS lien is an argument asserting unlimited jurisdiction. The desires of every Chapter 11 debtor are affected by a myriad of external indirect effects created by the circumstances in which it operates. Whether they arise from the ebbs and flows of commerce, the effects of governmental action or the acts of third parties with respect to property of non-debtors, their impact on a debtor's attempt to reorganize does not affect the bankruptcy courts with jurisdiction to determine the dispute merely because of that impact.

Id. at 466; see also Mego Intl', Inc. v. Packaging & Assembly Mfg. Corp. (In re Mego Intl', Inc.), 30 B.R. 479, 483 (S.D.N.Y. 1983) (concluding that the “need to help Mego in its effort to reorganize is an inappropriate basis . . . for Bankruptcy Court jurisdiction . . . in a [non-debtor] contract action”).

In the Dow Corning case, in finding “related to” jurisdiction to adjudicate breast implant claims against the debtor’s co-defendants, the Sixth Circuit initially relied upon the practical
If facilitation of the debtor's reorganization does not supply jurisdiction to adjudicate a non-debtor action, then the courts are "adjudicating by release" many non-debtor actions they have held to be outside the scope of "related to" jurisdiction to adjudicate. More importantly, though, the Callaway opinion speaks to the direct and ultimate jurisdictional issue posed by non-debtor releases and holds that jurisdiction to release and permanently enjoin a non-debtor action is wanting without regard to jurisdiction to adjudicate the non-debtor action.

b. Jurisdiction to Release a Non-Debtor Action

Even assuming that the importance of a non-debtor dispute to a debtor’s reorganization effort might give a federal court bankruptcy jurisdiction to actually hear and adjudicate that dispute under governing nonbankruptcy law, can that jurisdiction to protect and promote reorganization be taken even further—can a federal court permanently extinguish the non-debtor action, without even purporting to address the merits of the underlying dispute, all in the interests of aiding the debtor’s reorganization? Whether this is couched in terms of jurisdiction or merely the proper reach of a bankruptcy court’s injunctive powers, the Callaway opinion, rather unambiguously, disapproved such an injunction:

The district court’s injunction was based primarily on the premise that the plan of reorganization requires the inclusion of South Western’s lines within the system of the reorganized company. The state action is said to be an attempt . . . ‘to prevent the consummation of the plan as respects South Western.’ . . . [T]he court held that ‘the question of the . . . sale, and under what conditions South Western may convey its property to the reorganized company, in consummation of the plan, is not a question of State law; it is a question of Bankruptcy law . . . .’ The court’s conclusion was, therefore, that although the question whether a Georgia railroad corporation can convey all of its properties without unanimous consent of its stockholders would ordinarily be one of state

litigation burdens the non-debtor actions would place upon the debtor—the same sort of litigation burdens used to justify temporary stay of non-debtor actions. Lindsey v. O’Brien, Tanzer & Young Health Care Providers (In re Dow Corning Corp.), 81 F.3d 635, 646-47, 648-49 (6th Cir.), amended, 86 F.3d 482 (6th Cir. 1996). The court subsequently withdrew those portions of the opinion, though, stating that “[u]pon reconsideration, we believe our finding that ‘related to’ jurisdiction exists is best supported by the [potential] contribution and indemnification.” 86 F.3d at 490 n.9. This reinforces the point that, as applied by the courts, “related to” for purposes of jurisdiction to temporarily stay a non-debtor action (meaning interference with the debtor’s reorganization effort) will not necessarily supply “related to” jurisdiction to adjudicate the non-debtor action. See supra notes 432-42 and accompanying text; see also Clark Oil & Ref. Corp. v. Chicap Pipe Line Co. (In re Apex Oil Co.), 88 B.R. 968, 971-72 (Bankr. E.D. Mo. 1988) (noting that interference with a debtor’s attempt to reorganize is sufficient for jurisdiction to stay a non-debtor action, even though it might be insufficient for jurisdiction to adjudicate).
law cognizable in the state's courts, under these circumstances the decision was one for the bankruptcy court applying federal law.

We do not agree. . . .

. . . . The [bankruptcy] statute does not . . . give the . . . court the right to require acceptance by a lessor not in reorganization of an offer for the purchase of its property . . . . The fact that the [state] law may make acceptance of the offer less likely than would be the case if the offeree were incorporated elsewhere does not change the picture. We do not believe that Congress intended to leave to individual judges the question of whether state laws should be accepted or disregarded, or to make the criterion to be applied the effect of the law upon the prospects of acceptance by the offeree.\footnote{459}

In other words, the reorganization court could not permanently release and enjoin enforcement of these non-debtor rights and obligations in order to facilitate the debtor's reorganization efforts. Whatever rights a South Western shareholder had to veto a sale of South Western's assets to the debtor must remain intact, regardless of their impact upon the debtor's reorganization.

The lower courts largely read \textit{Callaway} as a pronouncement of a lack of bankruptcy jurisdiction over non-debtor disputes and, as a corollary, that bankruptcy courts possess no power to enjoin such non-debtor actions, even temporarily.\footnote{460} The opinion, though, seems to explicitly reserve the possibility that \textit{Continental Illinois} permits a temporary, status quo stay of a non-debtor action when appropriate to develop the plan of reorganization.\footnote{461} \textit{Callaway}, then, seems to speak \textit{solely} to the impropriety of a \textit{permanent} non-debtor release and injunction.

With respect to temporary non-debtor stays, any misreading of the \textit{Callaway} opinion has been corrected, albeit awkwardly, through

\footnote{459} 336 U.S. at 136-41 (citation omitted). In the omitted portions of the quoted passage, the Court also emphasized that Central's plan of reorganization, by its own terms, did not require acquisition of the South Western lines and contemplated rejection of Central's lease on those lines should South Western refuse to sell them. \textit{See id.} However, the reorganization court had found that acquisition of those lines was important to Central's reorganization, nonetheless, and the plan's lease rejection provisions were, no doubt, intended to prod South Western to sell. \textit{See supra} notes 448 and 457. In fact, there are suggestions in the Court's opinion that rejection of the lease was not an attractive alternative for South Western. \textit{See} 336 U.S. at 134 (noting that, during Central's equity receivership and subsequent reorganization proceedings, "South Western's lease was adopted successively by Central's Receiver and Trustees," and South Western "has, in consequence, remained solvent, and no petition for reorganization has ever been filed in its behalf").

\footnote{460} \textit{See supra} Part IV.C.

\footnote{461} \textit{Callaway}, 336 U.S. at 150 ("The district court did not merely postpone action which would have hindered the development of the plan."). Of course, this is entirely consistent with \textit{Continental Illinois} and the historical distinction between bankruptcy jurisdiction to adjudicate and bankruptcy jurisdiction to enjoin. \textit{See supra} Part IV.B-C.
subsequent expansion of federal bankruptcy jurisdiction. In the process, however, Callaway's prohibition on permanent non-debtor releases has been completely ignored. Subsequent expansion of bankruptcy jurisdiction in no way denigrates the continuing vitality of the Callaway holding. In fact, this aspect of the Callaway opinion precedes any discussion of bankruptcy jurisdiction and is not premised upon presence or absence of jurisdiction to adjudicate the non-debtor dispute. Rather, Callaway disapproved the permanent non-debtor release and injunction because there was no explicit statutory authority for displacing and extinguishing the non-debtor rights and obligations.

In the end, then, the jurisdictional infirmity of permanent non-debtor releases and injunctions is that suggested by general "in aid of jurisdiction" jurisprudence. Whatever ambiguity may exist in attempts to distinguish procedure from substance in other contexts, those characterizations effectively capture the jurisdictional defect in non-debtor releases. The courts' procedural power to protect the integrity of the reorganization process, through channeling and status quo injunctions, cannot be converted into a substantive power to extinguish non-debtor rights and obligations, independent of any explicit statutory authorization. It is not a matter of determining whether Bankruptcy Code section 524(e) prohibits non-debtor releases; it is a matter of finding statutory authorization for non-debtor releases.

Section 105 alone, with its grant of a general equitable power to protect the integrity of the reorganization process by injunction, certainly cannot be the sole source of this new substantive power. Bankruptcy courts must respect the substantive rights created by state

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462. See supra Part IV.D.

463. See Callaway, 336 U.S. at 136-41. Even though this case arose under the 1898 Act, it retains its precedential authority under the Bankruptcy Code:

When Congress amends the bankruptcy laws, it does not write "on a clean slate." Furthermore, this Court has been reluctant to accept arguments that would interpret the Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history.


464. See supra Part IV.A.

465. See Bill Roderick Distrib., Inc. v. A.J. Mackay Co. (In re A.J. Mackay Co.), 50 B.R. 756, 762 (D. Utah 1985) ("They are procedural powers, not substantive powers.").

466. The 1898 Act cases disapproving non-debtor releases recognized this more readily than do modern cases. For example, both the Second and Seventh Circuits looked first to general "in aid of jurisdiction" powers for authority to approve the releases and concluded that non-debtor releases were beyond the appropriate reach of such injunctive powers, notwithstanding the authority of Continental Illinois. Bankruptcy Code § 524(e)'s predecessor, 1898 Act § 16, merely provided additional support for the conclusion that non-debtor releases were an improper use of "in aid of jurisdiction" injunctive powers. See Weber v. Diversey Bldg. Corp. (In re Diversey Bldg. Corp.), 86 F.2d 456, 457-58 (7th Cir. 1936); In re Nine N. Church St., Inc., 82 F.2d 186, 188-89 (2d Cir. 1936).
and federal nonbankruptcy law, except to the extent those rights are specifically modified by the Bankruptcy Code.\textsuperscript{467} Section 105 and the bankruptcy court's general equity powers are an inappropriate basis for creating new substantive rights or altering those substantive rights in a manner not authorized by the Bankruptcy Code.\textsuperscript{468} Non-debtor releases improperly extinguish creditors' substantive causes of action against non-debtors, without even a hint of congressional endorsement of the practice.

V. Conclusion

This article has argued that the bankruptcy courts' practice of discharging creditor actions against non-debtors is an abusive one, with no redeeming theoretical merit. Policy concerns advanced by proponents of non-debtor releases seem designed primarily to obfuscate the redistributational consequences of these liability releases. Most bewildering, though, is the fact that authority to issue these exceptional injunctions has been manufactured out of whole cloth, and in disregard of Supreme Court precedent prohibiting them. Given both the weight of this issue in complex reorganizations and the circuit split regarding authority to approve non-debtor releases,\textsuperscript{469} the matter seems ripe for resolution by the Supreme Court—again.

\textsuperscript{467} See Butner v. United States, 440 U.S. 48, 54-55 (1979); Ayer, Field Guide, supra note 159, at 886 ("It is axiomatic that bankruptcy respects rights established under state law.").

\textsuperscript{468} See, e.g., In re Lloyd, 37 F.3d 271, 275 (7th Cir. 1994) ("[A] bankruptcy court does not have 'free-floating discretion,' to create rights outside the Code."); United States v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986) ("That statute [§ 105] does not authorize the bankruptcy courts to create substantive rights that are otherwise unavailable under applicable law or constitute a roving commission to do equity." (footnote omitted)); In re Glenn, 760 F.2d 1428, 1440 (6th Cir. 1985) ("[A] bankruptcy court may not exercise its equitable powers to create substantive rights which do not exist under state law." (quoting Johnson v. First Nat'l Bank, 719 F.2d 270, 274 (8th Cir. 1983))); Southern Ry. Co. v. Johnson Bronze Co., 758 F.2d 137, 141 (3d Cir. 1985) ("[S]ection 105(a) does not authorize the bankruptcy court to create rights not otherwise available under applicable law.").

\textsuperscript{469} See authorities cited supra notes 4, 8, and 44.