USW Ruling Highlights Successor Liability In Bankruptcy Sale

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Bankruptcy Code Section 363(f) authorizes a debtor to sell assets "free and clear" of "any interest" in property asserted by nondebtors. This is an important tool designed to maximize value for the benefit of stakeholders in a debtor's bankruptcy case.

However, the potential to strip away a party's interest in property through a Section 363 bankruptcy sale may be objectionable to some, resulting in litigation among the purported interest holder, the debtor-seller and/or the asset purchaser.

In the recent decision in United Steel, Paper and Forestry, Rubber, Manufacturing, Energy Allied Industrial and Service Workers International Union AFL-CIO, CLC v. Braeburn Alloy Steel LLC, the U.S. District Court for the District of Delaware examined whether the term "any interest" in property includes post-sale successor liability obligations under the National Labor Relations Act, notwithstanding language in the sale approval order transferring the debtor's assets to the purchaser "free and clear" of successor liability obligations, and held that it does not.[1]

"Free and Clear" Section 363 Sales in Bankruptcy

Section 363(b)(1) of the Bankruptcy Code provides in relevant part that a debtor, "after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate."

Courts generally apply some form of a business judgment test in determining whether to approve a proposed sale of estate property under Section 363(b)(1).[2] Under this deferential standard, a bankruptcy court will generally approve a reasoned decision by a debtor to sell estate property outside the ordinary course of business.[3]

Section 363(f) of the Bankruptcy Code authorizes a debtor to sell estate property "free and clear of any interest in such property of an entity other than the estate" if:

> (1) applicable nonbankruptcy law permits sale of such property free and clear of such interest; (2) such entity consents; (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property; (4) such interest is in bona fide dispute; or (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

Many courts have construed the term "interest in property" broadly to encompass obligations that flow from the ownership of property: e.g., many "successor liability" claims are included within the scope of "interests" under Section 363(f), such that asset sales in bankruptcy may occur "free and clear" of successor liability claims, provided one of the requirements in Sections 363(f)(1)-(5) is met.[4]

In the Braeburn decision, the district court addressed whether an asset purchaser was subject to successor liability for obligations imposed on it under the NLRA following the sale.

CCX Bankruptcy and Sale Overview

CCX Inc. was a specialty steel manufacturer that operated a factory in Pennsylvania, where it employed hourly workers represented by the United Steelworkers. CCX and the union were parties to a collective bargaining agreement, which set forth the terms and conditions of employment for those union-represented workers.

On March 27, 2022, CCX filed a Chapter 11 bankruptcy petition in the U.S. Bankruptcy Court for the District of Delaware.[5] On April 21, 2022, the bankruptcy court entered a bidding procedures order authorizing Braeburn Alloy Steel to be designated the stalking horse bidder for the proposed sale of substantially all of CCX's assets.[6]

During the negotiation of the asset purchase agreement and the contract assumption and assignment process, Braeburn declined to assume the CBA. At the sale hearing, the union expressed its hope that Braeburn would offer jobs to CCX's employees, but the union did not object to the proposed sale.[7]

The bankruptcy court entered an order[8] that approved the proposed sale, approved the asset purchase agreement, and provided that Braeburn could acquire substantially all of CCX's assets "free and clear of all liens, claims, rights, encumbrances, and other interests of any kind or nature whatsoever ... and any rights or claims based on any taxes or successor or transferee liability."[9]

Moreover, the sale order expressly enjoined all persons "holding liens, claims, encumbrances, and/or other interests of any kind or nature whatsoever ... against or in the Seller or the Purchased Assets" from asserting those claims, "and any rights or claims based on any taxes or successor or transferee liability" against Braeburn.[10]

The sale of CCX's assets closed on May 27, 2022, and thereafter "Braeburn hired essentially all of CCX's Union-represented employees under new terms of employment and continued the same business."[11]

Separately, on Aug. 15, 2022, the union and CCX filed with the bankruptcy court a stipulation reflecting their agreement to terminate the CBA and to resolve various claims that arose under the CBA prior to the closing date of the sale.[12] This stipulation made clear that it did not affect any claims by the union against Braeburn, stating it "shall only address and resolve disputes involving the Debtor and the Union and Union Retirees."[13]

The Dispute and the Bankruptcy Court Decision

The same day the sale closed, the union requested that Braeburn, as an alleged "perfectly clear"[14] successor employer under the NLRA, recognize the union as the collective bargaining representative of Braeburn's hourly employees. Braeburn refused, arguing it had no successor liability to the union based on the union's past dealings with CCX, which caused the union to pursue relief with the National Labor Relations Board.

On Oct. 14, 2022, the NLRB issued a consolidated complaint against Braeburn, which alleged that Braeburn had (1) failed to recognize and bargain with the union and (2) made unlawful unilateral changes from the terms and conditions of employment that had

prevailed under the union's CBA with CCX.

Before the NLRB issued the consolidated complaint, Braeburn moved the bankruptcy court for an order enforcing the sale order and enjoining the union from pursuing any claims that Braeburn had an obligation to recognize or bargain with the union.

The union and the NLRB objected, arguing that a bankruptcy court may not insulate a purchaser from successor liability — here, the obligation to bargain with the union — imposed on it by the NLRA based on the purchaser's post-closing conduct.[15]

In granting Braeburn the relief it sought, the bankruptcy court noted that "the Sale Order imposes an injunction on the Union and enjoins it ... from making a complaint with the National Labor Relations Board about whether the CBA is still in effect or whether Braeburn is obligated to negotiate and recognize the Union under terms and conditions of the CBA," and enjoined the union "from asserting, pursuing or otherwise taking any action, directly or indirectly, with respect to any allegation that Braeburn is bound to (1) the CBA or (2) the terms and conditions of the CBA by operation of law."[16]

More specifically, the bankruptcy court held that the CBA was an interest in property, that the debtor's assets could be sold free and clear of the CBA pursuant to Section 363(f), and that the union consented to the sale free and clear of the CBA by virtue of its participation in the sale hearing and its failure to raise an objection.

The District Court Decision

Following the bankruptcy court's decision, Braeburn began "actively negotiating a collective bargaining agreement with the Union."[17] As a result, Braeburn argued to the district court that the union's appeal was moot and should be dismissed. The district court rejected this argument and held that a "live" controversy existed because the bankruptcy court's order enforcing the sale order constrained the "Union's behavior in pressing forward with unfair labor practice charges against Braeburn based on Braeburn's actions post-sale."[18]

As to the merits, the district court held that Braeburn's post-closing obligation to bargain with the union existed independently of the CBA and was rooted in the NLRA.[19] As a result, according to the district court, "whether the CBA is an 'interest in [ ] property' [subject to Section] 363(f) is irrelevant to a determination of whether the NLRB could assess violations of the NLRA based on Braeburn's post-sale conduct."[20]

The key question, according to the district court, was whether Braeburn's post-closing bargaining obligation under the NLRA was an interest in property such that the obligation could be extinguished in a bankruptcy sale.

After noting that the Bankruptcy Code does not define the term "interest in property,"[21] the district court, relying on the U.S. Court of Appeals for the Third Circuit's 2003 decision in In re: Trans World Airlines,[22] held that the term is "intended to refer to obligations that are connected to, or arise from, the property being sold."[23]

After concluding that "successorship obligations under the NLRA do not depend on the transfer or sale of property; rather, such obligations derive from a successor's conduct in hiring a majority of its workforce from the predecessor and maintaining substantial continuity in business operations,"[24] the district court held that Braeburn's post-closing bargaining obligation under the NLRA was not an "interest in property"[25] such that the debtor could sell its assets to Braeburn free and clear of the post-closing obligations that the

NLRA imposed on Braeburn due to its post-sale conduct.

Finally, the district court held that the bankruptcy court erred in finding that the union consented to the bankruptcy sale free and clear of Braeburn's post-closing bargaining obligation under the NLRA. Neither the union's appearance at the sale hearing without objection to the sale nor its consent to the debtor's rejection of the CBA was sufficient to satisfy Section 363(f)(2).[26]

Conclusion

Notably, neither the sale order nor the asset purchase agreement obligated Braeburn to hire any of CCX's employees or negotiate and bargain with the union. Had such obligations been included in one or both documents, Braeburn's conduct in hiring the employees arguably might not have been viewed as a post-sale action. It is unclear whether the outcome would have been different had such obligations been included in the asset purchase agreement or the sale order.

In reaching its decision, the district court also recognized the tension presented between the NLRA, a federal statute imposing post-sale obligations on certain asset purchasers, and the Bankruptcy Code, a federal statute authorizing debtors to sell and purchasers to buy assets free and clear of successor liability claims.

In addressing that tension, the district court held that the "Bankruptcy Code and the NLRA are 'capable of coexistence,' [and] the court has a duty [] to regard each as effective."[27] The district court's analysis might have been different had state law, not the NLRA, been implicated.

The Braeburn decision is a reminder to potential asset purchasers when analyzing a potential asset sale to evaluate and consider whether any successor liability claims could potentially take root under a federal statute, independent of and not resulting from the asset sale, and whether such claims arguably arise post-closing of the sale.

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[1] United Steel, Paper, and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union, AFL-CIO/CLC v. Braeburn Alloy Steel LLC, Civ. No. 22-1563 (GBW) (D. Del. Sept. 18, 2023) at Docket No. 18 (the Braeburn Decision).

[2] See ASARCO Inc. v. Elliott Mgmt. (In re ASARCO LLC), 650 F.3d 593, 601 (5th Cir. 2011); In re Stearns Holdings LLC, 607 B.R. 781, 792 (Bankr. S.D.N.Y. 2019).

[3] See In re Alpha Nat. Res. Inc., 546 B.R. 348, 356 (Bankr. E.D. Va.), aff'd, 553 B.R. 556 (E.D. Va. 2016). Note, however, that when a proposed sale would be to an "insider," courts apply heightened scrutiny to ensure that the transaction does not improperly benefit the insider at the expense of other stakeholders. See In re Alaska Fishing Adventure LLC, 594

B.R. 883, 887 (Bankr. D. Alaska 2018); In re Family Christian LLC, 533 B.R. 600, 622, 627 (Bankr. W.D. Mich. 2015).

[4] See Ind. State Police Pension Trust v. Chrysler LLC (In re Chrysler LLC), 576 F.3d 108, 124 (2d Cir. 2009) (approving a sale of assets to a newly formed acquisition entity free and clear of the debtor's liability for certain vehicle defects), vacated on other grounds, 558 U.S. 1087 (2009); In re Trans World Airlines Inc., 322 F.3d 283, 290 (3d Cir. 2003) (approving a section 363 sale free and clear of employment discrimination claims arising from conduct prior to the sale); UMWA 1992 Benefit Plan v. Leckie Smokeless Coal Co. (In re Leckie Smokeless Coal Co.), 99 F.3d 573, 586 (4th Cir. 1996) (holding debtor coal operators could sell their assets free of successor liability that would otherwise arise under the Coal Industry Retiree Health Benefit Act of 1992); In re Norrenberns Foods Inc., 642 B.R. 825 (Bankr. S.D. Ill. 2022) (granting debtor's motion to sell substantially all of its assets free and clear of claims asserted by a union pension fund against the debtor and the purchaser for withdrawal liability under ERISA); In re Catalina Sea Ranch LLC, 2020 WL 1900308, *13 (Bankr. C.D. Cal. Apr. 13, 2020) (holding chapter 11 debtor could sell assets to an insider affiliate and secured creditor under section 363(f) free and clear of wrongful death successor liability claims); In re K & D Indus. Servs. Holding Co. Inc., 602 B.R. 16 (Bankr. E.D. Mich. 2019) (authorizing sale of chapter 11 debtors' assets free and clear of successor liability claims for ERISA withdrawal liability).

[5] In re CCX Inc., Case No. 22-10252 (JTD) (Bankr. D. Del. Mar. 27, 2022) at Docket No. 1.

[6] In re CCX Inc., Case No. 22-10252 (JTD) (Bankr. D. Del. Apr. 21, 2022) at Docket No. 83.

[7] The Union also did not appeal the entry of the Sale Order.

[8] In re CCX Inc., Case No. 22-10252 (JTD) (Bankr. D. Del. May 9, 2022) at Docket No. 124.

[9] Sale Order ¶ 12. In fact, the Sale Order included a statement that Braeburn would not be deemed a successor to or a continuation of the Debtor, and that Braeburn would not have any successor, transferee, derivative, or vicarious liabilities for any claims, including, without limitation, under any theory of successor or transferee liability. See id. ¶ L.

[10] Id. ¶ 13.

[11] Braeburn Decision at 1.

[12] In re CCX Inc., Case No. 22-10252 (JTD) (Bankr. D. Del. Aug. 15, 2022) at Docket No. 175. On September 8, 2022, the Bankruptcy Court entered an order at Docket No. 190 approving the proposed stipulation.

[13] Id. at Docket No. 175-3 (fourth Ordered paragraph).

[14] Braeburn Decision at 4.

[15] Neither the Union nor the NLRB alleged that Braeburn was or could be bound to the CBA.

[16] In re CCX Inc., Case No. 22-10252 (JTD) (Bankr. D. Del. Nov. 18, 2022) at Docket No.

280.

[17] Braeburn Decision at 10.

[18] Id. at 10-11.

[19] Id. at 17 ("While the NLRB may look to a CBA to ascertain the prevailing terms and conditions of employment that a successor employer may be obligated, as a matter of law, to maintain as a result of its post-closing conduct, the CBA between a union and predecessor employer cannot dictate whether the buyer is obligated to maintain those conditions; only the successor employer's post-closing conduct will establish the extent of its labor law obligations.").

[20] Id.

[21] The District Court also noted the lack of any decision in any jurisdiction holding or suggesting that a sale under section 363(f) excuses a buyer from complying with its statutory obligations arising under the NLRA stemming from its post-sale conduct. See id. at 20.

[22] 322 F.3d 283 (3d Cir. 2003).

[23] Id. at 289.

[24] Braeburn Decision at 18. Under the NLRB's approach to successorship, if a majority of the employees of the new employer are not drawn from the union-represented ranks of the old employer, the new employer is not a "successor" and has no obligation to bargain with the union. See Nat'l Labor Relations Bd. v. Burns Int'l Sec. Servs. Inc., 406 U.S. 272, 281 (1972). Similarly, if there is not "substantial continuity in the employing enterprise," the new employer is not a successor and is not obligated to bargain with the union. See Fall River Dyeing & Finishing Corp. v. Nat'l Labor Relations Bd., 482 U.S. 27, 43 (1987).

[25] To support its theory that it had no obligation to bargain with the Union following closing of the sale, Braeburn cited many cases that hold section 363(f) may extinguish pre-sale liability against a debtor, which, according to the District Court, are clearly different from the facts presented to it, i.e., where Braeburn (the asset purchaser) sought to extinguish its post-sale obligations. Braeburn Decision at 19-20.

[26] "[U]ntil Braeburn actually employed essentially all of CCX's union-represented employees [post-closing], Braeburn would have no obligation to bargain with the Union [, and therefore could not have consented to waive that right at the sale hearing, enabling the Debtor to satisfy section 363(f)(3)]. Second, CCX's motion to reject its CBA with the Union, pursuant to § 1113 [,] resulted in a stipulation between the Union and CCX reflecting their agreement to terminate the CBA and to resolve the various pre-sale claims-claims which arose under the CBA prior to the May 27, 2022 closing of the sale to Braeburn. This stipulation made clear that it did not impact any claims by the Union against Braeburn." Id. at 22.

[27] Id. at 20 (internal quotations omitted).