

Jevic: U.S. Supreme Court Strikes Down Nonconsensual “Structured Dismissals” That Violate Bankruptcy Priority Rules

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The United States Supreme Court in a 6-2 decision in *Czyzewski v. Jevic Holding Corp.* (“*Jevic*”) put an end to the increasingly popular practice in the bankruptcy world known as “structured dismissals,” at least on a nonconsensual basis. While bankruptcy practitioners were nervous that the Supreme Court’s *Jevic* decision might put an end to all types of pre-Chapter 11 plan distributions that violate the priority scheme embodied in the Bankruptcy Code, trade creditors, employees and lenders can breathe a sigh of relief because *Jevic* acknowledged that certain types of payments that are often approved by the bankruptcy court at the outset of a Chapter 11 case are not prohibited under the appropriate circumstances. Moreover, fully consensual structured dismissals are still permitted. However, lacking a fully consensual structured dismissal, the *Jevic* decision will leave debtors (and lenders funding a Chapter 11 case) with the choice of having to fund and confirm a Chapter 11 plan, dismiss the Chapter 11 case (without a structured dismissal order), or convert the Chapter 11 case to a Chapter 7 bankruptcy.

In the *Jevic* case, the creditors’ committee sued Sun Capital Partners and CIT Group, arguing that a pre-bankruptcy leveraged buyout hastened *Jevic*’s bankruptcy by saddling *Jevic* with debts that it could not service. The debtor, creditors’ committee, Sun and CIT ultimately reached a “structured dismissal” settlement that failed to provide for any distributions to a class of former *Jevic* truck drivers (the “WARN Claimants”) that held \$8.3 million in priority wage claims for pre-bankruptcy state and federal WARN Act violations.

The Bankruptcy Court approved the structured dismissal—despite the

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inclusion of a provision whereby low-priority general unsecured creditors would receive a distribution while the WARN Claimants would not be getting anything—over the objections of the WARN Claimants and the United States Trustee. The Bankruptcy Court ruled that such dismissals are justified in exceptional circumstances where a better alternative is not available. The District Court and Third Circuit Court of Appeals affirmed with the Third Circuit cautioning that priority-skipping structured dismissals should be approved only in “rare” circumstances.

On appeal, the Supreme Court reversed, explaining that the “rare case” exception would open the floodgates and holding that a bankruptcy court cannot “approve a structured dismissal that provides for distributions that do not follow ordinary priority rules without the affected creditors’ consent.” The Supreme Court explained that while the Bankruptcy Code grants a court the power to dismiss a Chapter 11 case, it does not authorize the approval of *final* and *end-of-case* distributions that deviate from the Bankruptcy Code’s priority scheme.

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of interim distributions in Chapter 11 cases and that “serv[e] significant Code-related objectives.” Specifically, the Supreme Court noted (without expressly ruling) that the following types of orders, under the appropriate circumstances, can be approved:

- “Critical vendor” orders that allow payment of essential suppliers’/ trade vendors’ prepetition unsecured claims;
- “First-day” wage orders that allow payment of employees’ prepetition wages;
- “Roll ups” that allow lenders that continue financing the debtor to be paid first on their prepetition claims; and
- Interim distributions of settlement proceeds to fund a litigation trust that would press claims on the estate’s behalf, but in a situation where the Chapter 11 case remains pending. ■