SURETY TODAY PRESENTATION
Given by
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The Surety and Chapter 11 Bankruptcy Plan Release and Injunction Provisions

Introduction (George)

Today, Mike Stover and I will discuss the effect of the Chapter 11 Bankruptcy Plan Release and Injunction Provisions on the surety and the surety's rights to indemnity and collateral from the debtor and others. Because of the complex and stylized wording in some Chapter 11 Bankruptcy Plans, and to make our lives easier, we have already provided you with Examples of such provisions in our Surety Today Notice along with some of the definitions that relate to those provisions (please see the attached Examples). It would be helpful for you to have the Examples in front of you during this presentation.

We don't intend to examine those definitions or provisions in detail. Rather, we will discuss the concepts that those provisions address, how they may affect the surety and its rights, and what the surety may do to combat those provisions. We will use two situations – one subdivision bond case and one commercial surety bond case – to highlight how the Chapter 11 Bankruptcy Plan Release and Injunction Provisions may affect the surety rights and liabilities.

Chapter 11 and Reorganization Plans Generally. (Mike)

The reorganization of a corporation under the Bankruptcy Code is intended to strike a balance between the need of a corporate debtor in financial hardship to be made economically sound and the desire to preserve creditors' and stockholders' legal rights to the extent possible. Thus, a chapter 11 reorganization is a complex exercise of legal procedure, corporate finance and business management. Chapter 11 is based on the belief that it is generally preferable to enable a debtor to continue to operate and reorganize its financial affairs as a going concern rather than shut the business down and conduct a liquidation. Under Chapter 11 there is a presumption that the debtor's business will continue to operate and that the debtor will remain in possession after the entry of an order for relief. These presumptions assure the debtor considerable control over plan negotiations.

Upon commencement of a case, all of the debtor's property becomes property of the bankruptcy estate. The debtor and the property are protected by the automatic stay in bankruptcy. The debtor in possession is given the ability to use, sell, or lease property of the estate, even if the property is subject to the interest of a creditor after offering adequate protection of such interests. The debtor in possession may assume or reject executory contracts or leases and it may recover property transferred and avoid obligations prior to the commencement of the case in the same manner as a trustee in chapter 7. Further, the U.S. trustee is required to appoint a committee of unsecured creditors and may appoint additional committees of creditors or equity security holders.

Focusing on the reorganization plan, the hallmark of a chapter 11 is flexibility. The debtor in possession is offered considerable discretion in the operation of the business, constrained generally only by the business judgment rule. The debtor is given 120 days to exclusively propose a plan and that time period may be extended for up to 18 months. During this period no other entity may propose a plan. The plan negotiation process is designed to lead to a consensual plan under which the debtor and a majority of creditors have agreed to both business and financial plans that offer some realistic chance of success. The bankruptcy courts are given considerable discretion in evaluating a debtor's proposed use of property, offers of adequate protection, the debtor's proposed borrowing and other business decisions.

Under Section 1123 of the Code, a plan must:

1. Classify claims and interests, such as a class for trade claims, a class for bonds, etc.
2. Specify any classes of claims or interests that are not impaired under the plan
3. Specify the treatment of impaired classes
4. Provide the same treatment for each member of a class unless a holder of a particular claim agrees to less favorable treatment
5. Provide adequate means of implementing the plan
6. and other provisions.

Once a plan is filed with the court, the debtor must file a disclosure statement. The disclosure statement must contain adequate information to enable those who must vote on the plan to make an informed decision. The disclosure statement contains an explanation of the provisions of the plan, a description of how the plan will be implemented, financial forecasts and a discussion of tax consequences.

The creditors vote on the plan and the court must confirm the plan if the requirements of Section 1129(a) are met. These requirements include:

1. That the plan was proposed in good faith
2. That each creditor or equity interest holder have accepted the plan or be entitled to receive at least what it would receive in a chapter 7 liquidation of the debtor and
3. That each class has either accepted the plan or is not impaired under the plan.

Chapter 11 Plan Release and Injunction Provisions (George)

To help explain the effect of Plan Release and Injunction Provisions on a surety, we have provided you with Examples along with the Notice of this Surety Today presentation (please see the attached Examples). The Examples actually address a number of other issues that we have **omitted** from the Examples and won't discuss today. We will only review the Plan Release and Injunction Provisions.

We have included with the Plan Release and Injunction Provisions certain definitions, some of which are statutory and are found in the Bankruptcy Code and some of which are defined in the Plan. Simply stated, under Article IX.C of the Plan and the Examples heading of "Releases by Holders of Claims," as of the Effective Date of the Confirmed Plan, each "Releasing Party" releases and discharges each "Released Party" from any and all "Claims and

Causes of Action." The Examples and the defined terms provide answers to the following three questions.

Question #1 – Is the surety a defined "Releasing Party" under the Plan Release Provision? The answer is **YES**.

1. The surety is within the definition of a "Holder of Claims." The surety "holds claims" against the Debtor at common law, in equity, and under the indemnity agreement.
2. As a "Holder of Claims," the surety is, therefore, a defined "Releasing Party" under the Plan Release Provision.

Question #2 – Who is the surety releasing?

1. As a "Releasing Party" under the Plan, the surety is releasing the "Released Party" or "Released Parties."
2. Included within the defined term "Released Party" are many entities, whether they exist before or after the filing of the Bankruptcy proceeding or after the Effective Date of the confirmation of the Plan, including entities created by or affiliated with the Debtor and the Reorganized Debtor and other entities such as the Debtor's pre-petition lender, the DIP lender during the Debtor's Chapter 11 proceeding, or the subsequent post-petition lender to the Reorganized Debtor after the confirmation of the Plan.

Question #3 – What is the surety releasing?

The surety, as a "Releasing Party," is releasing each "Released Party" from all "Claims" and "Causes of Action" to enforce the surety's rights and remedies for any of the surety's claims.

In addition to the above releases, the Plan Injunction Provision in Article IX.E of the Plan also enjoins a "Releasing Party" from enforcing its rights against a "Released Party." A "Releasing Party" attempting to enforce its rights against a "Released Party" may be liable for violating the Plan Injunction Provision as approved in the Confirmation Order entered by the Bankruptcy Court.

Before we look at the effect on the surety in certain circumstances with respect to "who" the surety is releasing, what "Claims" and "Causes of Action" the surety is releasing, and the injunction against the surety taking action against a "Released Party" upon the confirmation of the Plan, the next questions are whether such Plan Release and Injunction Provisions are legally valid in a Debtor's Plan and under what circumstances will they be approved and enforced by the Bankruptcy Courts in the Plan Confirmation Order.

Are Broad Plan Release and Injunction Provisions Legal? (Mike)

As George just noted, one question to consider is whether a broad plan release and injunction are legally valid in a debtor's plan? What we are focusing on today is the release and injunction provisions of a reorganization plan that are so broad that they purport to release claims of a third party against another third party. We all understand that generally speaking under the

Bankruptcy Code the bankruptcy courts have fairly broad powers to deal with claims against debtors. But what about a release of a claim of a third party obligee for example against a bond issued by a surety of the debtor. The surety and obligee generally are not parties in the bankruptcy.

Generally, the Supreme Court has noted that a bankruptcy court has jurisdiction over a debtor's property and the disposition of that property. But third-party claims belong to third parties, not the estate. Thus, as a general rule, a bankruptcy court typically has no power to say what happens to property that belongs to a third party, even if that third party is a creditor or otherwise is a party in interest.[1] Section 524(e) of the Bankruptcy Code specifically 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."[2] Moreover, the Bankruptcy Code provides that a bankruptcy court lacks the power to confirm plans of reorganization which do not comply with applicable provisions of the Bankruptcy Code. 11 U.S.C. § 1129(a)(1).

Given the general law and Code provisions it would seem that broad release and injunction provisions affecting the rights between third parties would not be permissible. However, Section 105 (a) of the Code provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."[3] Some courts seize upon Section 105 of the Code as authority to implement such broad release and injunction provisions. Other courts recognize that Section 105 does not provide power to issue orders that are inconsistent with the other provisions of the Code, such as Section 524(e).

Thus, there is a split among the Circuits on the issue of whether bankruptcy courts can release third parties from claims held by other third parties in connection with a debtor's reorganization plan. Some Circuits, such as the Fifth, Ninth, and Tenth Circuits, have held that third-party releases are categorically beyond the power of a bankruptcy court.[4] Other Circuits, such as the Sixth, Second, Fourth and Eleventh Circuits, have held that such plan releases are permissible under certain circumstances, recognizing that such provisions are only proper in unusual, extraordinary or rare circumstances.[5] The Third Circuit has indicated that it *may be*

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[1] *See Callaway v. Benton*, 336 U.S. 132, 136-41, 69 S.Ct. 435, 93 L.Ed. 553 (1949).

[2] 11 U.S.C. § 524(e).

[3] 11 U.S.C.A. § 105.

[4] *See Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (In re Pac. Lumber Co.)*, 584 F.3d 229, 251-53 (5th Cir. 2009);*Matter of Zale Corp.*, 62 F.3d 746, 760 (5th Cir. 1995) ("we must overturn a § 105 injunction if it effectively discharges a nondebtor"); *Resorts International, Inc. v. Lowenschuss (In re Lowenschuss)*, 67 F.3d 1394, 1401 (9th Cir. 1995); *Landsing Diversified Properties-II v. The First National Bank and Trust Co. of Tulsa (In re Western Real Estate Fund, Inc.)*, 922 F.2d 592, 601-02 (10th Cir. 1990) ("while a temporary stay prohibiting a creditor's suit against a nondebtor ... during the bankruptcy proceeding may be permissible to facilitate the reorganization process ... the stay may not be extended post-confirmation in the form of a permanent injunction that effectively relieves the nondebtor from its own liability to the creditor.).

[5] *See Menard-Sanford, et al. v. Mabey, et al. (In re A.H. Robins Company, Inc.)*, 880 F.2d 694 (4th Cir. 1989); *Stuart, LLC v. First Mount Vernon Industrial Loan Association (In re Peramco International, Inc.)*, 3 Fed. Appx. 38, 42 (4th Cir. 2001); *Behrmann v. National Heritage Foundation*, 663 F.3d 704, 712 (4th Cir. 2011); *Airadigm Comm., Inc. v. Federal Comm. Commission (In re Airadigm Communications, Inc.)*, 519 F.3d 640 (7th Cir. 2008) (approving nondebtor release when release was necessary for the reorganization and appropriately tailored ... affected only claims arising out of or in connection with the reorganization itself, not blanket immunity); *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136 (2d Cir. 2005) (warning that "a nondebtor release is a device that lends itself to abuse" and "[n]o case has tolerated nondebtor releases absent the finding of circumstances that may

willing to allow for such releases.[6] But the Court expressly declined to "establish [its] own rule regarding the conditions under which non-debtor releases and permanent injunctions are appropriate or permissible." *Id.* at 214. Thus, the split among the Circuits occupies the spectrum between "impossible" and "very rare."[7]

The leading decision on this subject permitting the release of third-party claims against nondebtors is the Sixth Circuit's opinion in *Class Five Nevada Claimants v. Dow Corning Corp. (In re Dow Corning Corp.)*, 280 F.3d 648, 658 (6th Cir. 2002). In that case, the Court held that while such releases were not categorically prohibited by the Bankruptcy Code, such provisions remain an exception, not the rule. The Court stated such measures are dramatic and should be used cautiously and that "enjoining a non-consenting creditor's claim is only appropriate in unusual circumstances."[8]

To analyze whether broad release and injunction provisions in plans should be approved, the Dow Corning court held that such nonconsensual provisions may be "appropriate" if seven factors that it created were present. These factors have been adopted by many of the other Circuits that permit such provisions. Generally, the factors look at whether:

(1) There is an identify 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 the assets of the estate;
(2) The non-debtor has contributed substantial assets to the reorganization;
(3) The injunction is essential to reorganization, namely the reorganization hinges on the debtor being free from indirect suits against parties who would have indemnity or contribution claims against the debtor;
(4) The impacted class, or classes, have overwhelmingly voted to accept the plan;
(5) The plan provides a mechanism to pay for all or substantially all of the class or classes affected by the injunction;
(6) The plan provides an opportunity for those claimants who choose not to settle to recover in full; and
(7) The bankruptcy court made a record of specific factual findings that support its conclusions.

In performing the research, it becomes clear that the seminal cases where such broad releases have been used are all in the massive tort litigation matters where releases were

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be characterized as unique," and holding that the bankruptcy court finding that the nondebtor seeking the release made a material contribution to the reorganization was not independently sufficient to justify such a release); *Securities and Exchange Commission v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Group, Inc.)*, 960 F.2d 285 (2d Cir. 1992); *SE Prop. Holdings, LLC v. Seaside Eng'g 7 Surveying (In re Seaside Eng'g & Surveying, Inc.)*, 780 F.3d 1070, 1078 (11th Cir. 2015) (holding that releases and bar orders are permitted but "ought not to be issued lightly, and should be reserved for those unusual cases in which such an order is necessary for the success of the reorganization, and only in situations in which such an order is fair and equitable under all the facts and circumstances").

[6] *In re Continental Airlines*, 203 F.3d 203 (3d Cir. 2000).

[7] *In re Firstenergy Sols. Corp.*, 606 B.R. 720, 733 (Bankr. N.D. Ohio 2019).

[8] *Dow Corning*, 280 F.3d at 658 (citing *Drexel Burnham Lambert*, 960 F.2d at 293; *A.H. Robins*, 880 F.2d at 702; and *Johns-Manville Corp.*, 837 F.2d at 93-94).

necessary in exchange for insurers funding huge trusts or other claim resolution mechanisms such as in asbestos cases and other product liability cases. In all of these types of cases, a plan was negotiated in exchange for significant contributions from third parties and large groups of creditors approved the plan.

Despite the seemingly narrow circumstances under which broad release and injunction provisions are permitted, if permitted at all, it has become common place to find such provisions in reorganization plans. Accordingly, sureties should determine if such release provisions are permissible in the applicable jurisdiction and whether the circumstances warrant such provisions.

The Cautionary Tale! (Mike)

If a plan of reorganization has been confirmed and it has a broad release and injunction provision, the surety must be extremely careful to determine exactly what the scope of the provisions are, whether the surety is included and whether the surety's actions post-confirmation comply with the provisions. The case of *In re Kimbell Hill, Inc.*, 565 B.R. 878 (Bankr. N.D. Ill. 2017), in the United States Bankruptcy Court for the Northern District of Illinois provides a chilling and cautionary tale. In that case, the surety was found liable for breaching the confirmed plan's release and injunction provisions and was ordered to pay over $9.5 million in damages this past January. There are multiple decisions regarding the matter and the facts are long and complicated.

Essentially, the surety wrote a series of subdivision bonds for its principal, Kimbell Hill, Inc. ("Kimbell"), which was the developer of several subdivisions in various jurisdictions. Kimbell entered into Annexation Agreements with the municipalities having jurisdiction over the subdivisions. Each Annexation Agreement contained terms and conditions under which the subdivision development would proceed pursuant to the Illinois Municipal Code, and the Agreements were recorded in the applicable land records. In April 2008, Kimbell filed a chapter 11 bankruptcy. The surety filed proofs of claim in the bankruptcy. In 2009, the Court confirmed a Plan of Liquidation.

The Plan and the Confirmation Order discharged and released all claims of parties that voted in favor of the Plan against the Debtors, specifically providing that holders of claims and interests *voting to accept* the Plan have conclusively and irrevocably released and discharged the Debtors and a whole host of other entities and all were defined as the Released Parties from any and all claims, interests, obligations, rights, suits, damages, causes of Action, etc. whatsoever, whether known or unknown, foreseen or unforeseen, existing or hereafter arising, in law, equity, or otherwise, that such entity would have been legally entitled to assert. The surety voted in favor of the plan and was thus bound by the terms of the release.

In furtherance of the Release, both the Plan and the Confirmation Order contained a broad injunction stating that all entities who have held claims or interests that have been released are permanently enjoined from commencing or continuing any action or other proceeding of any kind on account of or in connection with or with respect to any such claims or interests that were released or settled in the plan.

The Plan created a trust for post confirmation administration of the bankruptcy estate known as the "KHI Trust", and all or substantially all of the Debtors' remaining assets were placed in the KHI Trust "free and clear of any and all liens, claims, encumbrances and interests of all other entities to the maximum extent contemplated by and permissible under the Bankruptcy Code. Further, the KHI Trust, as a successor to the Debtors, was entitled to the benefit of the Release and the Plan Injunction. The plan provided "The rights, benefits, and obligations of any Entity named or referred to in the Plan shall be binding on, and shall inure to the benefit of any heir, executor, administrator, successor or assign, affiliate, etc. of each Entity." As a result, the indemnity agreements from the debtor to the surety were no longer binding. However, the Annexation Agreements ran with the land and remained binding.

The KHI Trust agreed to sell all of its right, title and interest in the bonded subdivisions to JNI, LLC. JNI, LLC, subsequently sold the bonded properties to an entity known as TRG. During the plan, several of the municipalities sought relief from the injunction to enforce their rights against the surety to enforce the Annexation Agreements. The surety, debtor and municipalities entered into stipulations that were approved by the Court allowing the municipalities to declare the debtor in default, proceed against the surety and establish liability of the debtor solely for purposes of claiming against the bonds. While the stipulations modified the Plan for the limited purposes, they did not alter the surety's obligation to comply with the Plan release and injunction. The municipalities filed separate lawsuits against the surety for each development. The surety then added TRG to the suits as successor in interest to the debtor, the principal on the bonds. TRG moved for dismissal in the suits and dismissal was granted in most, but appeals were filed.

While the state court litigation was pending, TRG filed a motion in the bankruptcy alleging that the surety had violated the Plan and Confirmation Order injunction and release by asserting claims against TRG in the state court litigation. In response to the TRG motion, the surety asserted arguments of abstention, estoppel and laches and contended that the transfer of the Properties to TRG did not invalidate the Annexation Agreements, that TRG was independently liable to the surety on the bonds because the bonds were unaffected by the Plan, because the Annexation Agreements bind successors in interest and because the state law gave rise to a common law obligation between the parties, irrespective of the Plan's treatment of the surety's claims against the debtor.

The bankruptcy court found that the surety was aware of the release and injunction and that the action of adding TRG to the state court litigation was an act that would violate the release and injunction of the Plan if TRG was within the scope. On the issue of whether TRG and the claims asserted against TRG were covered by the Plan, the Surety did not dispute that TRG, as a successor to or assign of the Debtors through the KHI Trust, was entitled to the benefit of the Release and Injunction. Rather, the Surety argued that the claims it asserted against TRG were independent from the claims subject to the Release and Injunction. This argument was based on the appellate decisions overturning some of the dismissals in the state court litigation. The bankruptcy court rejected the argument that the surety's common law indemnity rights against TRG were any different that the surety's indemnity rights that were released in the Plan. Even if such indemnity rights were different, they were still "future rights" which were released according to the court. A separate hearing was held as to damages and the surety was found

liable for $9.5 million, which included $1.2 million in attorney fees and $7.7 million in lost property value.

As the Kimbell case makes clear, the surety must be extremely careful to determine exactly what the scope of the provisions are, whether the surety is included and whether the surety's actions post-confirmation comply with the provisions.

The Release and Injunction Provisions in Commercial Surety Cases (George)

I want to address the issues from a recent large commercial surety bankruptcy case where: (a) the Debtor's Plan contained the Release and Injunction Provisions that we have provided in our Examples; and (b) the surety held an Irrevocable and Unconditional Letter of Credit as collateral for the issuance of the surety bonds. Initially, one of the difficulties in tracking and understanding large commercial surety bankruptcy cases is the enormous amount of paper – pleadings, agreements, orders, etc. – filed with the Bankruptcy Court that need to be reviewed to determine their effect on the surety and its rights, including:

1. First Day Motions and Orders.
2. Cash Collateral Orders.
3. Financing Orders.
4. Specific Orders affecting the surety's bond obligations. (Examples include utility bonds, workers' compensation bonds, and other commercial surety bonds remaining in place during the Chapter 11 case).
5. Multiple filed Plans, Disclosure Statements and Plan Supplements.

In my recent case, the Debtor filed a Plan containing the Release and Injunction Provisions. As a result, the surety's concern became the effect of those provisions on a surety's rights to draw on the letter of credit and enforce its rights against the lender, the issuer of the letter of credit. The questions are:

1. Will the surety, a "Releasing Party," be able to draw on the letter of credit <u>after</u> the Plan is confirmed and the Plan Release and Injunction Provisions become effective?
2. If the Debtor's lender, the issuer of the letter of credit and a "Released Party," has been released of any claims, will the surety's attempted draw on the letter of credit <u>after</u> the Plan is confirmed be determined to be a "surety claim" against a "Released Party?"
3. And, if it is, and the lender refuses to pay the surety's draw under the letter of credit, has the surety released its "cause of action" against the lender and will the surety be enjoined from instituting a "cause of action" to enforce the surety's right to payment by the lender under the letter of credit?

Under those circumstances, the surety may have a legal right to payment under the letter of credit, but subject to the lender's defense of a release under the Plan. However, the surety may have no means to enforce its rights and seek a remedy for the lender's breach of its obligation to pay under the letter of credit. By filing a "cause of action" to enforce its rights and remedies under the letter of credit, the surety may face a lender's defense of release and, in addition, potential damages for violation of the Plan Injunction Provision.

Assuming that the letter of credit is unconditional and the surety has the right to draw on the letter of credit, and the surety wants to preserve its rights to its collateral, there are two possibilities:

1. The surety may negotiate language with the Debtor to protect the surety's rights to draw on the letter of credit at any time, including after the confirmation of the Plan; or
2. The surety may draw on the letter of credit prior to the confirmation of the Plan and avoid any Debtor arguments that the surety has released its rights against the letter of credit and the lender under the confirmed Plan Release and Injunction Provisions.

The surety may face pushback and opposition from the Debtor and others for drawing on the letter of credit, especially if there are no open claims against the surety's bonds. Furthermore, the surety may face the Debtor's claims that the surety is holding "excess proceeds," namely, more collateral than is necessary for the surety to avoid risk and exposure to loss under its bonds (an issue that we have addressed in prior Surety Today presentations). But, the surety may have no other option if appropriate language is not agreed upon to protect the surety's rights to draw on the letter of credit at some future time, including after the confirmation of the Plan. The next questions are what is the "appropriate language" and whether it belongs in the Plan or the Confirmation Order?

There is no language that will fit every case, but the following concepts must be considered – and, as discussed below, placed in the Confirmation Order and not the Plan itself to preserve the Surety's Rights.

First, the surety must retain and must not waive any of its claims, rights, abilities and protections under the letter of credit and against the lender – which I will hereinafter refer to as the "Surety's Rights."

Second, none of the Surety's Rights shall be released, changed, modified or amended under any provision of the Plan, any Plan Supplement, or the Confirmation Order. Namely, some loose language that may appear in some other document or Bankruptcy Court filing can't be allowed to affect the Surety's Rights as set forth in the agreed language in the Confirmation Order.

Third, there needs to be a description of the "paper trail" concerning the "issuer" of and the "lender" under the letter of credit. Assuming that the letter of credit was issued by the pre-petition lender for the Debtor, there needs to be language that describes whether the DIP lender during the Debtor's Chapter 11 proceeding has assumed the pre-petition lender's obligations under the letter of credit and whether the pre-petition lender has been "released" of those obligations under the DIP Financing Order. Namely, have the Surety's Rights under the pre-petition letter of credit become the obligation of a different lender, the DIP lender? Then, continuing up the chain, will the DIP lender's obligations be assumed by the post-petition lender to the Reorganized Debtor after the confirmation of the Plan? Furthermore, will that assumption release the DIP lender and make the post-petition lender to the Reorganized Debtor liable for and subject to the Surety's Rights under the letter of credit? The appropriate language must "connect

the dots" to make certain that the Surety's Rights either continue through the full chain of lenders or be the liability of the lender that eventually gets stuck with the obligations to pay the surety under the letter of credit.

Fourth, the Reorganized Debtor may want to replace the original letter of credit with a new letter of credit after the Effective Date of the Confirmation Order. The surety should require the specific terms and the necessity of the surety's consent for any such post-confirmation replacement of the surety's original letter of credit.

While the Plan sets forth the Debtor's contractual obligations to its creditors, the language in the Confirmation Order governs and controls over the language in the Plan if there are conflicts, inconsistencies or ambiguities. Therefore, the language protecting the Surety's Rights must be in the Confirmation Order and not in the Plan. More importantly, the language should state that "no provisions of the Plan or any other provision contained in the Confirmation Order" shall change or modify the letter of credit language agreed upon by the surety and the Debtor and contained in the Confirmation Order.

Procedurally, if the surety's letter of credit is going to be assumed after the Effective Date of the Confirmation Order by a post-petition lender to the Reorganized Debtor, the Debtor should give notice to the surety of that fact in either or both the Notice of the Entry of the Confirmation Order and the Notice of the Effective Date of the Confirmed Plan.

When you go back over the Examples and the full text of the Plan Release and Injunction Provisions, which are essentially long run-on sentences that include the proverbial "kitchen sink" of "Released Parties" and released claims, causes of action, transactions, events, etc. (everything done before and during the Debtor's Bankruptcy proceeding up to the Confirmation Order), it becomes clear that a surety does not want to be in the position of later having to argue, after the confirmation of the Plan, whether the surety can draw on a letter of credit if it incurs losses under the surety bonds and the indemnity agreement. There are too many documents to review and too many angles and arguments that can be raised to contend that the surety has no ability to assert its rights to draw under the letter of credit after the confirmation of the Plan. Therefore, we provide the two options discussed above:

1. Draw on the letter of credit prior to the entry of a Confirmation Order that could prevent the surety from a later draw on the letter of credit as a result of the confirmed Plan Release and Injunction Provisions; or
2. Negotiate language to be placed in the Confirmation Order clarifying and protecting the Surety's Rights in the letter of credit and the surety's ability to draw on the letter of credit proceeds after the confirmation of the Plan.

SURETY TODAY PRESENTATION – DECEMBER 9, 2019

EXAMPLES

DEBTOR'S PLAN OF REORGANIZATION –
DEFINITIONS AND RELEASE AND INJUNCTION PROVISIONS

Plan of Reorganization – Article IX.

RELEASE, INJUNCTION, AND RELATED PROVISIONS

A. *Discharge of Claims and Termination of Equity Interests; Compromise and Settlement of Claims, Equity Interests, and Controversies.* **Omitted.**

B. *Releases by the Debtors.* **Omitted.**

C. ***Releases by Holders of Claims and Equity Interests***

NOTE: *The provision below is an actual Plan Release provision and provides for Releases by Holders of Claims of defined "Released Parties."* ***Highlighted in bold red*** *is the critical Plan language to review. The important defined terms are* ***highlighted in bold red and underlined in bold red,*** *and their definitions for purposes of the Plan Release provision are provided below this provision. Please note below that the surety is a "Holder of Claims" and, therefore, a "Releasing Party" for the purposes of Article IX.C. We have also* ***underlined in bold black*** *the word "****including****" in the Plan Release provision in order to discuss and highlight the breadth and extent of the releases granted under Article IX.C.*

NOTWITHSTANDING ANYTHING CONTAINED IN THE PLAN TO THE CONTRARY, AS OF THE EFFECTIVE DATE (OR SUCH LATER DATE AS PROVIDED FOR IN ARTICLE III.C), TO THE EXTENT PERMITTED BY LAW, EACH RELEASING PARTY IS DEEMED TO HAVE RELEASED AND DISCHARGED EACH DEBTOR, REORGANIZED DEBTOR, AND RELEASED PARTY FROM ANY AND ALL CLAIMS AND CAUSES OF ACTION, WHETHER KNOWN OR UNKNOWN, INCLUDING ANY DERIVATIVE CLAIMS, ASSERTED ON BEHALF OF THE DEBTORS THAT SUCH ENTITY WOULD HAVE BEEN LEGALLY ENTITLED TO ASSERT (WHETHER INDIVIDUALLY OR COLLECTIVELY), BASED ON OR RELATING TO, OR IN ANY MANNER ARISING FROM, IN WHOLE OR IN PART, THE DEBTORS (INCLUDING THE MANAGEMENT, OWNERSHIP, OR OPERATION THEREOF), THE DEBTORS' IN- OR OUT-OF-COURT RESTRUCTURING EFFORTS, ANY AVOIDANCE ACTIONS, THE FORMULATION, PREPARATION, DISSEMINATION, NEGOTIATION, OR FILING OF THE RESTRUCTURING SUPPORT AGREEMENT, OR ANY TRANSACTION CONTEMPLATED THEREBY, OR ANY CONTRACT, INSTRUMENT, RELEASE, OR OTHER AGREEMENT OR DOCUMENT (INCLUDING PROVIDING ANY LEGAL OPINION REQUESTED BY ANY ENTITY REGARDING ANY TRANSACTION, CONTRACT, INSTRUMENT, DOCUMENT, OR OTHER AGREEMENT CONTEMPLATED BY THE PLAN OR THE RELIANCE BY ANY RELEASED PARTY ON THE PLAN OR THE CONFIRMATION ORDER IN LIEU OF SUCH LEGAL OPINION) CREATED OR ENTERED INTO IN CONNECTION WITH THE RESTRUCTURING SUPPORT AGREEMENT, THE DISCLOSURE STATEMENT, THE PLAN, THE PLAN SUPPLEMENT, THE RIGHTS OFFERING, THE DIP FACILITIES, THE DIP CREDIT AGREEMENTS, THE DEBT

BACKSTOP AGREEMENT, THE EQUITY BACKSTOP AGREEMENT, THE NEW DEBT, THE NEW DEBT DOCUMENTATION, THE CHAPTER 11 CASES, THE FILING OF THE CHAPTER 11 CASES, THE PURSUIT OF CONFIRMATION, THE PURSUIT OF CONSUMMATION, THE ADMINISTRATION AND IMPLEMENTATION OF THE PLAN, INCLUDING THE ISSUANCE OR DISTRIBUTION OF SECURITIES PURSUANT TO THE PLAN, OR THE DISTRIBUTION OF PROPERTY UNDER THE PLAN, OR UPON ANY OTHER ACT OR OMISSION, TRANSACTION, AGREEMENT, EVENT, OR OTHER OCCURRENCE TAKING PLACE ON OR BEFORE THE EFFECTIVE DATE RELATED OR RELATING TO THE FOREGOING. NOTWITHSTANDING ANYTHING TO THE CONTRARY IN THE FOREGOING, THE RELEASES SET FORTH ABOVE DO NOT RELEASE (A) ANY POST-EFFECTIVE DATE OBLIGATIONS OF ANY PARTY OR ENTITY UNDER THE PLAN, ANY POST-EFFECTIVE DATE TRANSACTION CONTEMPLATED BY THE RESTRUCTURING, OR ANY DOCUMENT, INSTRUMENT, OR AGREEMENT (INCLUDING THOSE SET FORTH IN THE PLAN SUPPLEMENT) EXECUTED TO IMPLEMENT THE PLAN, INCLUDING THE ASSUMPTION OF THE INDEMNIFICATION PROVISIONS AS SET FORTH IN THE PLAN, (B) ANY INDIVIDUAL FROM ANY CLAIM RELATED TO AN ACT OR OMISSION THAT IS DETERMINED IN A FINAL ORDER BY A COURT OF COMPETENT JURISDICTION TO HAVE CONSTITUTED ACTUAL FRAUD, GROSS NEGLIGENCE, OR WILLFUL MISCONDUCT, OR (C) ANY UNIMPAIRED CLAIM UNLESS AND UNTIL RELEASED PURSUANT TO ARTICLE III.C. FURTHER, NOTHING IN THE PLAN, THE CONFIRMATION ORDER, OR SECTION 1141 OF THE BANKRUPTCY CODE, WILL BE CONSTRUED AS DISCHARGING, RELEASING OR RELIEVING THE REORGANIZED DEBTORS FROM ANY LIABILITY IMPOSED UNDER ANY LAW OR LEGALLY VALID REGULATORY PROVISION WITH RESPECT TO THE HEXION INC. PENSION PLAN. NEITHER THE PENSION BENEFIT GUARANTY CORPORATION NOR HEXION INC. PENSION PLAN WILL BE ENJOINED OR PRECLUDED FROM ENFORCING SUCH LIABILITY AGAINST ANY PARTY AS A RESULT OF ANY PROVISION OF THE PLAN OR THE CONFIRMATION ORDER.

SUBJECT TO ARTICLE III.C, ENTRY OF THE CONFIRMATION ORDER SHALL CONSTITUTE THE BANKRUPTCY COURT'S APPROVAL, PURSUANT TO BANKRUPTCY RULE 9019, OF THIS THIRD-PARTY RELEASE, WHICH INCLUDES BY REFERENCE EACH OF THE RELATED PROVISIONS AND DEFINITIONS CONTAINED HEREIN, AND, FURTHER, SHALL CONSTITUTE THE BANKRUPTCY COURT'S FINDING THAT THIS THIRD PARTY RELEASE IS: (1) CONSENSUAL; (2) ESSENTIAL TO THE CONFIRMATION OF THE PLAN; (3) GIVEN IN EXCHANGE FOR GOOD AND VALUABLE CONSIDERATION PROVIDED BY THE RELEASED PARTIES; (4) A GOOD-FAITH SETTLEMENT AND COMPROMISE OF THE CLAIMS RELEASED BY THE THIRD-PARTY RELEASE; (5) IN THE BEST INTERESTS OF THE DEBTORS AND THEIR ESTATES; (6) FAIR, EQUITABLE, AND REASONABLE; (7) GIVEN AND MADE AFTER DUE NOTICE AND OPPORTUNITY FOR HEARING; AND (8) A BAR TO ANY OF THE RELEASING PARTIES ASSERTING ANY CLAIM OR CAUSE OF ACTION RELEASED PURSUANT TO THIS THIRD PARTY RELEASE.

NOTE: The "**defined terms**" in this series of run-on sentences in this Plan Release provision include the following:

A. "**Plan**." The Debtor's Plan of Reorganization, including all Plan Supplements (including exhibits and schedules) that are incorporated by reference into the Plan.

B. "**Releasing Party**." A Releasing Party includes: "(o) all Holders of Claims that are presumed to accept the Plan; (p) all Holders of Claims who vote to accept the Plan; (q) all Holders of Claims or Interests who are entitled to vote on the Plan and (i) abstain from voting on the Plan or vote to reject the Plan and (ii) do not opt out of the releases provided by the Plan; (r) all Holders of Claims or Interests who are deemed to reject the Plan and do not timely object to confirmation of the Plan with respect to the releases; …"

C. "**Holders of Claims**." The question is whether a surety is the holder of a claim that would include the surety as a member of the defined group named "Releasing Party." That depends on the definition of Holder and the definition of Claims.

1. "**Holder**" under the Plan means "an Entity holding a Claim or Interest."
2. "**Claim**" means any claim against the Debtor as defined in §101(5) of the Bankruptcy Code.[9]

NOTE: The surety is a "Holder" of a "Claim" under the Plan against the Debtors under the indemnity agreement and pursuant to its common law and equitable rights. The surety's claim is for indemnity and reimbursement under the indemnity agreement and under the common law for any losses that the surety incurs under its bonds and in accordance with the terms of the indemnity agreement (such as attorneys' fees, expenses, etc.). Therefore, the surety, as a "Holder of Claims," is within the definition of a "Releasing Party." As a "Releasing Party," the surety is releasing the "Released Party" or "Released Parties" as defined in the Plan.

D. "**Released Party**." The parties who are released under Article IX.C. by the Releasing Parties include, among others, the Debtor, the Reorganized Debtor,[10] and all of the Lenders to the Debtor and the Reorganized Debtor (whether the Lender was a pre-petition Lender, a DIP Lender during the Debtor's Chapter 11 proceeding, or a Lender to the Reorganized Debtor after the Effective Date of the Confirmed Plan of Reorganization).

E. "**Claims**" and "**Causes of Action**." The Releasing Parties release and discharge the Released Parties, including the Lenders (who may be liable to a surety under a pre-petition Irrevocable Letter of Credit), from all Claims and Causes of Action. "Claims" have been defined previously. "Causes of Action" are defined in the Plan to include EVERYTHING, meaning EVERY ACTION that a surety could bring against a Released Party, including common law and

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[9] The Bankruptcy Code defines a "claim" in §101(5) as a:

> (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or
> (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.

[10] Under the Plan definitions, the "Reorganized Debtor" is the Debtor after the Effective Date of the Plan, any successors, assigns, prior and/or newly formed subsidiaries and/or affiliates, and other possible entities created by the Reorganized Debtor after the Effective Date of the Plan.

equitable rights and remedies and contract claims, rights and remedies under the indemnity agreement.

F. The "**Effective Date**" of the Plan is the date that all conditions of the Plan are satisfied or waived and the Plan becomes effective against all creditors and other parties.

D. Exculpation

NOTE: *Any detailed discussion of this provision is* ***Omitted****. However, the "Exculpated Parties" under the Plan include most if not all of the "Released Parties" under the Plan. Therefore, those Released Parties are not only released from liability, but they are also "exculpated"*[11] *for any liability for any of their acts or omissions during the Debtor's Chapter 11 proceeding.*

E. ***Injunction***

NOTE: *The provision below is an actual Plan Injunction provision which enjoins and prohibits Holders of Claims from pursuing their Claims and Causes of Action that have been released under Article IX.C of the Plan (as described above). Highlighted in* ***bold red*** *is the critical Plan language to review.*

EXCEPT AS OTHERWISE PROVIDED IN THE PLAN OR THE CONFIRMATION ORDER (AND, FOR THE AVOIDANCE OF DOUBT, SUBJECT TO ARTICLE III.C), ALL ENTITIES WHO HAVE HELD, HOLD, OR MAY HOLD CLAIMS, INTERESTS, CAUSES OF ACTION, OR LIABILITIES THAT: (A) ARE SUBJECT TO COMPROMISE AND SETTLEMENT PURSUANT TO THE TERMS OF THE PLAN; (B) HAVE BEEN RELEASED PURSUANT TO ARTICLE IX.B OF THE PLAN; (C) HAVE BEEN RELEASED PURSUANT TO ARTICLE IX.C OF THE PLAN, (D) ARE SUBJECT TO EXCULPATION PURSUANT TO ARTICLE IX.D OF THE PLAN (BUT ONLY TO THE EXTENT OF THE EXCULPATION PROVIDED IN ARTICLE IX.D OF THE PLAN), OR (E) ARE OTHERWISE DISCHARGED, SATISFIED, STAYED OR TERMINATED PURSUANT TO THE TERMS OF THE PLAN, ARE PERMANENTLY ENJOINED AND PRECLUDED, FROM AND AFTER THE EFFECTIVE DATE, FROM COMMENCING OR CONTINUING IN ANY MANNER, ANY ACTION OR OTHER PROCEEDING, INCLUDING ON ACCOUNT OF ANY CLAIMS, INTERESTS, CAUSES OF ACTION, OR LIABILITIES THAT HAVE BEEN COMPROMISED OR SETTLED AGAINST THE DEBTORS, THE REORGANIZED DEBTORS, OR ANY ENTITY SO RELEASED OR EXCULPATED (OR THE PROPERTY OR ESTATE OF ANY ENTITY, DIRECTLY OR INDIRECTLY, SO RELEASED OR EXCULPATED) ON ACCOUNT OF, OR IN CONNECTION WITH OR WITH RESPECT TO, ANY DISCHARGED, RELEASED, SETTLED, COMPROMISED, OR EXCULPATED CLAIMS, INTERESTS, CAUSES OF ACTION, OR LIABILITIES.

F. Setoffs and Recoupment. **Omitted.**

G. Release of Liens. **Omitted.**

[11] "Exculpate" means to absolve, acquit, clear from alleged blame or fault, exonerate, vindicate or agree that an "Exculpated Party" has done nothing wrong during the Debtor's Chapter 11 proceeding.