By Gregory W. Werkheiser

When Do Court Orders Become Improper Advisory Opinions?

Gregory W. Werkheiser
Morris, Nichols, Arsht & Tunnell LLP
Wilmington, Del.

Gregory Werkheiser is a partner in the Business Reorganization and Restructuring Group of Morris, Nichols, Arsht & Tunnell LLP in Wilmington, Del.

On July 18, 1793, then-Secretary of State Thomas Jefferson wrote to Chief Justice John Jay and the associate justices of a fledgling U.S. Supreme Court asking for guidance on settling Revolutionary War pensions for widows and orphans. The justices' response was a resounding "No." Chief Justice Jay cited "the lines of separation drawn by the three departments of the government" that are "in certain respects checks upon each other." He also cited the Court's position as "a court in the last resort" as "considerations [that] afford strong arguments against the propriety of [the Court] extra-judicially deciding the questions alluded to, especially as the power given by the Constitution to the President, of calling on the heads of departments for opinions, seems to have been purposely as well as expressly united to the executive departments."[1] This concise letter became a foundational part of more than two centuries of jurisprudence negating the ability of Article III courts to render advisory opinions.

More than two centuries later, federal courts still struggle with the lines of demarcation between off-limits advisory opinions and those that properly adjudicate parties' rights and obligations in an actual case or controversy. Perhaps nowhere more is this line more blurred than in business bankruptcy proceedings.

Practical Necessity of Court Guidance in Business Bankruptcy Cases

Bankruptcy courts are not Article III courts. However, that does not free them to issue advisory opinions. Bankruptcy courts' subject-matter jurisdiction is derived from statutory grants of authority to the district courts, which pass to bankruptcy courts through the reference that is codified at 28 U.S.C. § 157(a). Accordingly, because district courts, as true Article III courts, lack the power to render advisory opinions, it is now accepted that bankruptcy courts, as units of the district courts, operate under the same limitation.[2]

However, the practical reality is that bankruptcy judges are frequently called upon to issue orders under circumstances that do not fit neatly into the definition of a "justiciable controversy." For example, in chapter 11 cases of large multinational companies, bankruptcy judges sometimes issue orders at the outset of such cases declaring the automatic stay to be applicable to the debtors' property located outside of the U.S. Another prophylactic order frequently entered in chapter 11 cases directs that claims of sellers of goods in transit on the petition date and received by the debtor on or after the petition date will be afforded administrative-expense priority in the debtor's bankruptcy case. Such orders reflect the reality that business debtors (and their creditors) often require some measure of certainty to successfully reorganize or maximize value. Given these tensions, it is no wonder then that the Third Circuit has observed that in bankruptcy cases, "[t]he precise analytical contours of what constitutes an advisory opinion … are less than clear."[3]

Relevant Background of *Lazy Days'*

The Third Circuit's opinion in *In re Lazy Days' RV Center Inc.*[4] illustrates some of the special challenges that bankruptcy courts face in attempting to distinguish requests for improper advisory opinions from those that are necessary to adjudicate an actual case or controversy. More than two years after the debtors, Lazy Days' RV Center Inc. and LDRV Holding Corp. (LDRV, and with Lazy Days', the "debtors" or "reorganized debtors") had successfully reorganized and closed their chapter 11 cases, the debtors returned to the U.S. Bankruptcy Court for the District of Delaware with a request to reopen their bankruptcy cases to issue an order that the reorganized debtors characterized as "enforcing" the terms of the order confirming their reorganization plan as it related to a lease of nonresidential real property that had been assumed under the debtors' plan (the "lease").

This motion involved a parcel of land in Florida owned by I-4 Land Holding Company, which I-4 had leased to Lazy Days' approximately a decade earlier. The lease contained an option that allowed Lazy Days' to purchase the property under certain conditions for an attractive price. In the year before the debtors' bankruptcy filing, disputes arose between Lazy Days' and I-4 over Lazy Days's obligation to pay rent under the lease and litigation was commenced in a Florida state court.

1 *See* 3 *Correspondence and Public Papers of John Jay* 486-89 (H. Johnston ed., 1891).
2 *See N.J. v. Heldor Indus. Inc.*, 989 F.2d 702, 707 n.8 (3d Cir. 1993) (citing *Northern Pipeline Const. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 76 (1982)).
3 *In re McDonald*, 205 F.3d 606, 608 (3d Cir. 2000).
4 724 F.3d 418 (3d Cir. 2013) ("*Lazy Days' III*").

In connection with negotiating their prepackaged bankruptcy plan, the debtors executed a settlement with I-4 pursuant to which the lease, with I-4's consent, would be assumed and assigned by Lazy Days' to LDRV. The debtors commenced their bankruptcy cases on Nov. 5, 2009, and their plan was confirmed and effective less than 50 days later. The cases were closed soon thereafter.

Approximately 14 months later, the reorganized debtors and I-4 found themselves once again embroiled in litigation. LDRV attempted to exercise the lease-purchase option, but I-4 refused to honor it. Within a month, both parties had filed competing lawsuits in Florida courts litigating whether the purchase option was available to LDRV. Section 13.1 of the lease prohibited assignment of the lease without I-4's prior written consent. Section 13.2, in turn, contained a limited exception that allowed the tenant to assign its interest in the lease to the surviving entity of a merger or consolidation with the tenant. Section 33.3 provided that the purchase option would remain available to the surviving entity in a § 13.2 assignment by merger or consolidation, but would be lost following an assignment pursuant to § 13.1.

Contemporaneous with LDRV's filing its Florida action, the reorganized debtors moved the bankruptcy court to reopen the chapter 11 cases to declare that the debtors' assumption and assignment of the lease to LDRV included the purchase option, and that § 365(f)(3) of the Bankruptcy Code precluded I-4 from relying on the anti-assignment language in the lease. The reorganized debtors disclaimed that they were seeking to have the bankruptcy court "adjudicate any issues related to the exercise of the Purchase Option other than the effect of 11 U.S.C. § 365(f) on the anti-assignment provision of the Lease."[5]

I-4 objected to the bankruptcy court's authority to reopen the cases. It argued that the lease dispute did not affect an "integral aspect of the bankruptcy process," and thus lacked a sufficient nexus to the bankruptcy cases to establish post-confirmation jurisdiction. In I-4's view, § 365(d)(3) was not implicated because determining whether the assignment was made under § 13.1 was a straightforward question of contract law.

At oral argument before the bankruptcy court, I-4 raised the specter that the reorganized debtors were seeking an improper advisory opinion. I-4 maintained that the bankruptcy court was being asked to apply § 365(f)(3) to a set of hypothetical facts that might never ripen into an actual controversy. Section 365(f)(3), I-4 asserted, would never be implicated if the Florida court determined as a matter of contract interpretation that the lease was assigned pursuant to § 13.2.

Bankruptcy Court Provides Guidance to State Court Litigants

The bankruptcy court quickly dispensed with I-4's challenges to its jurisdiction. Characterizing I-4 as having "attacked a central provision of the Plan and Confirmation Order," the bankruptcy court held that it had jurisdiction to adjudicate this dispute.[6] However, the bankruptcy court did not directly address I-4's contention that its ruling would be an impermissible advisory opinion. The court further held that the debtors' assumption of the lease constituted an assumption of all its terms, including the purchase option, and that § 365(f)(3) rendered the anti-assignment language in § 13.1 unenforceable. The bankruptcy court made the following conclusion: "To be clear *and to provide guidance to any other court asked to decide any issued [sic] involving the Lease or the Purchase Option*, the Lease is to be read without Section 13.1, which is invalid."[7]

District Court Reverses

On appeal to the district court, I-4 found a receptive audience for its challenge to the bankruptcy court's ruling as an improper advisory opinion. The district court initially discounted the bankruptcy court's reliance on the need to interpret the confirmation order as justification for exercising jurisdiction over the dispute. Although accepting in the abstract that it is proper for a bankruptcy court to interpret its own orders, the district court emphasized that the plan was a pre-pack and that the confirmation order had been written by the litigants.[8]

The district court then held that the case before it failed to satisfy the Article III case or controversy requirement. Relying principally on the Third Circuit's decision in *In re Martin's Aquarium*,[9] the district court held that the bankruptcy court had abused its discretion by reopening the cases for the sole purpose of granting relief that would be used in the parties' state court litigation. In so ruling, the district court emphasized that "it is crystal clear that the reorganized debtors went to the Bankruptcy Court to get an opinion that could be submitted to the Florida courts."[10]

Third Circuit Reaffirms Bankruptcy Court's Ability to Enforce Its Own Orders

An appeal to the Third Circuit followed. The court of appeals reversed the district court's ruling that the bankruptcy court's decree was an advisory opinion and determined that the bankruptcy court properly exercised its subject-matter jurisdiction. The Third Circuit affirmed the bankruptcy court's holding that § 365(f)(3) invalidated the anti-assignment language of § 13.1 of the lease.

In considering whether the bankruptcy court's decree was an advisory opinion, the Third Circuit, quoting recent Supreme Court precedent, described the prohibition against advisory opinions as precluding federal courts from "decid[ing] questions that cannot affect the rights of litigants in the case before them or give opinions advising what the law would be upon a hypothetical state of facts."[11] The bank-

5 *In re Lazy Days' RV Center Inc., et al.*, Case No. 09-13911 (KG), D.I. 153, ¶ 12 n.7 (Bankr. D. Del. June 7, 2011).

6 *In re Lazy Days' RV Center Inc.*, Case No. 09-13911 (KG), D.I. 166, Mem. Op. at 4 (Bankr. D. Del. June 16, 2011) ("*Lazy Days' I*").

7 *Id.* at 5 (emphasis added).

8 *In re Lazy Days' RV Center Inc.*, 2012 WL 4364257, at *2 n.2 (D. Del. Sept. 24, 2012) ("*Lazy Days' II*").

9 98 F. App'x 911 (3d Cir. 2004). As an unreported opinion, *Martin's Aquarium* was technically not binding precedent. *See* 3d Cir. I.O.P. 5.7 (stating that opinions designated not precedential "are not regarded as precedents that bind the court").

10 *Lazy Days' II*, 2012 WL 4364257, at *2.

11 *Lazy Days' III*, 724 F.3d at 421 (quoting *Chafin v. Chafin*, --- U.S. ----, 133 S. Ct. 1017, 1023 (2013)) (internal quotations omitted).

continued on page 97

from page 37

ruptcy court's decree was not an advisory opinion because its "decree actually invalidated the anti-assignment clause and ordered the parties to do something," directives that "affected the rights of [the] litigants."[12]

The Third Circuit rejected the district court's emphasis on how the bankruptcy court's decree would be used in the state court litigation, stating that "its opinion was not advisory, regardless of whether the Reorganized Debtors sought to impact the state proceedings."[13] What made the bankruptcy court's opinion *not* an advisory opinion was that it "had the *legal effect* of voiding the anti-assignment clause."[14]

Martin's Aquarium, the Third Circuit explained, was not in conflict because in that case, the bankruptcy court's order had no impact on the parties' state court litigation. The underlying dispute involved whether two Pennsylvania courts had properly entered judgments based on a bankruptcy court order approving a stipulation settling certain fraudulent transfer litigation. In the Pennsylvania courts, one of the parties had moved to strike the judgments as fraudulently entered. The other party then returned to the bankruptcy court with requests to reopen the bankruptcy case and declare that the bankruptcy court's stipulation and order was a "judgment" within the meaning of Fed. R. Civ. P. 54(a). The bankruptcy court complied, but the Third Circuit reversed.

In holding that the bankruptcy court had made an impermissible advisory ruling, the *Martin's Aquarium* court commented critically that the movants "sought ... to enlist the aid of the Bankruptcy Court to aid their arguments in the state litigation"[15] — precisely what the reorganized debtors in *Lazy Days'* were attempting to do. Nevertheless, the Third Circuit correctly distinguished *Martin's Aquarium* on the basis that the bankruptcy court's ruling "did nothing to resolve whether the Pennsylvania courts would be required to abide by it under Pennsylvania procedural rules."[16] The bankruptcy court's decision merely declared that the order approving the stipulation was a "judgment" under Fed. R. Civ. P. 54(a) but did not address whether that judgment had been procured by fraud. Moreover, because state law rather than federal law controlled whether the Pennsylvania courts would treat the bankruptcy order as a judgment, the bankruptcy court's ruling had no impact on the dispute.[17]

The *Lazy Days'* court next considered whether the bankruptcy court otherwise had subject-matter jurisdiction under § 350(b) of the Bankruptcy Code to reopen the cases and grant the requested relief. The appeals court reaffirmed the bankruptcy court's jurisdiction to reopen a bankruptcy case to interpret or enforce its own orders, concluding that "the Bankruptcy Court ... was 'well suited to provide the best interpretation of its own order.'"[18]

Although "[t]he precise analytical contours of what constitutes an advisory opinion" still remain less than clear in bankruptcy proceedings, the Third Circuit's decision in *Lazy Days'* does illuminate how to approach the question.... *Lazy Days'* instead frames the question as whether a bankruptcy court's decree will have any legal effect on the rights or obligations of the parties.

The Third Circuit's decision in *Lazy Days'* was undoubtedly the right outcome based on the facts before it. The question of whether LDRV retained the purchase option could not be answered without first examining the settlement agreement and order that been incorporated into the plan, assumed with the lease and approved pursuant to the confirmation order. Because the Third Circuit concluded that the settlement had not waived the protections of § 365(f)(3) of the Bankruptcy Code, it necessarily had to consider the effect of § 365(f)(3) on the lease's anti-assignment provision.

Lazy Days' Reframes the "Advisory Opinion" Inquiry

Although "[t]he precise analytical contours of what constitutes an advisory opinion"[19] still remain less than clear in bankruptcy proceedings, the Third Circuit's decision in *Lazy Days'* does illuminate how to approach the question. It is not the mere fact that relief from a bankruptcy court is being sought for use in connection with litigation pending elsewhere that will cause a bankruptcy court's decree to run afoul of the prohibition against advisory opinions. *Lazy Days'* instead frames the question as whether a bankruptcy court's decree will have any legal effect on the rights or obligations of the parties. If "yes," then at least this first hurdle to invoking bankruptcy court jurisdiction will have been satisfied. abi

12 *Id.* (quoting *Chafin*, 133 S. Ct. at 1023).
13 *Id.* at 422.
14 *Id.* at 422 (emphasis added).
15 *Martin's Aquarium*, 98 Fed. App'x at 913.
16 *Lazy Days' III*, 724 F.3d at 422 (citing *Martin's Aquarium*, 98 F.3d. App'x at 912).
17 *Martin's Aquarium*, 98 Fed. App'x at 913 n.1.
18 *Lazy Days' III*, 724 F.3d at 423. The Third Circuit also disposed of challenges based on *Stern v. Marshall*, 131 S. Ct. 2594 (2011), and the argument that the bankruptcy court was required to abstain under 28 U.S.C. § 1334(c)(2).
19 *In re McDonald*, 205 F.3d at 608.5 *In re Lazy Days' RV Center Inc., et al.*, Case No. 09-13911 (KG), D.I. 153, ¶ 12 n.7 (Bankr. D. Del. June 7, 2011).