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From Opioids to Opt-Outs: Nonconsensual Third-Party Releases and the Aftermath of Purdue

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On June 27, 2024, the U.S. Supreme Court released its 5-4 opinion in connection with the bankruptcy case of Purdue Pharma L.P. ("Purdue"). Over a vigorous dissent authored by Justice Kavanaugh, a narrow majority of the Supreme Court held that the Bankruptcy Code does not permit chapter 11 plans of reorganization to provide for non-consensual releases of non-debtors outside of the asbestos context. As such, Purdue's bankruptcy plan—which contained extremely controversial third-party releases of the Sackler family for claims arising from the marketing of opioids—was held to be unconfirmable and the case was remanded to the bankruptcy court. The Supreme Court's opinion resolves a circuit split on the hotly disputed issue of third-party releases, but also leaves plenty of space for future litigation as to the legitimacy of consensual ("opt-in" or "opt out") third-party releases, full-satisfaction releases, and the exculpation of parties and professionals in bankruptcy cases.

The Conflict over Non-Consensual Third-Party Releases

Traditionally, bankruptcy only operates to eliminate claims held by creditors against the debtor. Corporate debtors have increased the number of parties who benefit from the elimination of claims by including non-consensual third-party releases of claims against non-debtors in chapter 11 plans of reorganization, particularly in the mass-tort context. These third-party releases, when approved by the bankruptcy court, operate to preclude creditors of the debtor from pursuing claims against non-debtor third parties, including shareholders, officers, and directors. Such releases are often justified by the contributions the third parties have made to the reorganization efforts. Despite increasing prevalence in chapter 11 restructurings, however, third-party releases have remained controversial and the subject of heated debates, both inside and outside the courtroom.

Purdue's Bankruptcy

The debates regarding non-consensual third-party releases led to a split of authority, which culminated in the Supreme Court's decision to address the issue in the chapter 11 bankruptcy case of Purdue. Purdue, a pharmaceutical company with most of its revenue stemming from the sale of the prescription opioid OxyContin, found itself faced with what the bankruptcy court referred to as a "veritable tsunami of litigation" arising from the marketing and sale of OxyContin. As a result, Purdue filed for bankruptcy protection in September 2019. After two years of litigation and extensive negotiation, Purdue obtained confirmation of a reorganization plan which, among other things, contained third-party releases eliminating claims held by creditors of Purdue against Purdue's private owners (the Sackler family) and other non-debtor entities, including claims arising from alleged willful misconduct and fraud. In return, the Sacklers agreed to contribute approximately $4.5 billion to fund charities and certain recoveries under the plan. While the plan was supported by an overwhelming majority of creditors, several states and other creditors objected to, among other things, the plan's release of the Sacklers, and appealed the plan following confirmation.

On appeal, the United States District Court for the Southern District of New York vacated the order confirming Purdue's chapter 11 plan, holding that non-consensual third-party releases were not permitted by the Bankruptcy Code. Following that reversal, the Sacklers entered into further negotiations and agreed to contribute an additional $1.5 billion in exchange for the non-consensual releases. This additional money persuaded certain objectors to drop their objections, but other parties, including the U.S. Trustee, continued to oppose the plan on the basis that more money does not cure the impermissibility of third-party releases. The issue went up to the Second Circuit which reversed the district court and held that non-consensual third-party releases were permitted by the Bankruptcy Code. The case was further appealed to the Supreme Court.

The Supreme Court Decision

In a 5-4 decision, the Supreme Court reversed again, holding the Bankruptcy Code does not permit non-consensual third-party releases. The Supreme Court's analysis was simple and focused tightly on the text of the applicable sections of the Bankruptcy Code. The Supreme Court held that Congress had not drafted the Bankruptcy Code to permit non-consensual releases of non-debtors to be included in a bankruptcy plan except in cases involving claims relating to asbestos. Because it held that there was no statutory authority for the non-consensual releases, the Supreme Court did not need to reach issues concerning the constitutionality of non-consensual third-party releases, which had been raised by several parties.

The Court noted that the only statutory hook the parties had identified to support the inclusion of non-consensual third-party releases in a bankruptcy plan was Bankruptcy Code § 1123(b)(6). Bankruptcy Code § 1123 governs the "contents" of a chapter 11 plan of reorganization. Bankruptcy Code § 1123(a) provides various provisions that a plan "shall" include. Bankruptcy Code § 1123(b) contains various provisions that a plan "may" include, including provisions that "impair or leave unimpaired any class of claims" (§ 1123(b)(1)), provide for the assumption, rejection or assignment of executory contracts (§ 1123(b)(2)), settle or otherwise resolve claims held by the debtor against non-debtors (§ 1123(b)(3)), sell the debtor's property (§ 1123(b)(4)), and modify the rights of holders of secured claims against the debtor (§ 1123(b)(5)). Critically for the Purdue case, the list of provisions that "may" be included in a bankruptcy plan includes a "catchall" final subsection: a plan "may" include "any other appropriate provision not inconsistent with the applicable provisions of this title." 11 U.S.C. § 1123(b)(6).

The parties defending the plan relied on this catchall provision to justify the Sacklers' releases, arguing the non-consensual release of liability was an "appropriate" provision—in the context of the Purdue bankruptcy—that was not barred by any other "applicable provision" of the Bankruptcy Code. The Supreme Court rejected that argument. It held §1123(b)(6) was "a catchall phrase tacked on at the end of a long and detailed list of specific directions," and that, under ordinary principles of statutory construction, such a "catchall provision" should not be afforded the "broadest possible construction" but rather should be read only to "embrace only objects similar in nature to the specific examples preceding it." Slip. Op. at 10 (internal quotations and citations omitted). In connection with § 1123(b), the Supreme Court held that there was an "obvious link" between the preceding five subsections in the list: all "concern the *debtor*—its rights and responsibilities, and its relationship with its creditors." Slip. Op. at 11. As such, the Supreme Court held that § 1123(b)(6) must be similarly limited—it could not be "fairly read to endow a bankruptcy court with the radically different power to discharge the debts of a nondebtor without the consent of affected nondebtor claimants." *Id.*

The fact—focused on by the dissent—that § 1123(b)(3) permitted the resolution of claims of the debtor's estate against non-debtors, including the resolution of claims that other parties may be granted "derivative" standing to pursue in place of the debtor, did not change the analysis. Slip. Op. at 12. Such "derivative" claims "belong to the debtor's estate." *Id.* That a bankruptcy plan could resolve and release them thus did not justify the position that a bankruptcy court could release *direct* claims of non-debtor creditors against other non-debtors.

To further support its holding, the Supreme Court considered and rejected arguments that broad "policy" considerations should be used to expand the meaning of § 1123(b)(6) beyond the bounds suggested by the statutory wording (Slip. Op. at 13). It also noted other provisions in the Bankruptcy Code, including § 524(e), that were inconsistent with the view that the Bankruptcy Code granted broad powers to discharge non-debtors (Slip. Op. at 14–16), and that prior to the Bankruptcy Code's enactment in 1978 no courts granted non-consensual third-party releases. Thus, had Congress intended to radically expand bankruptcy court's power in that respect, one could expect it to have done so clearly, not simply by a reference to "appropriate" provisions. *Id.* at 16–17. The Supreme Court also expressed concern at the abuse of such releases. The Supreme Court noted the Sacklers were receiving what amounted to a discharge of all Purdue-related claims against them, without the Sacklers delivering all of their assets to a bankruptcy court for equitable distribution, and in derogation of Bankruptcy Code provisions that—in a Sackler bankruptcy—would have prohibited them from being discharged of claims arising from "fraud" or "willful misconduct." In other words, the Supreme Court concluded "the Sacklers seek greater relief than a bankruptcy discharge normally affords, for they hope to extinguish even claims for wrongful death and fraud, and they seek to do so without putting anything close to all their assets on the table." Slip Op. 16. Such expansive relief, the Court held, was not permissible.

The Supreme Court finished its decision by emphasizing what it was *not* deciding. The Supreme Court made clear that it was not seeking to cast doubt on the legitimacy of *consensual* third-party releases or what constituted "consent" for such purposes, the inclusion of "full satisfaction" third-party releases in a bankruptcy plan (releases upon full satisfaction of the subject creditors' claims), or whether equitable mootness could apply to a plan that had been consummated including third-party releases. Slip. Op. at 19–20.

Dissent

Justice Kavanaugh authored a dissent, which was joined by Chief Justice Roberts and Justices Sotomayor and Kagan. The dissent, which was phrased in forceful terms, focused largely on policy considerations, arguing the non-consensual third-party releases were the opioid victims' best hope of receiving a recovery on account of their claims and were necessary to deal with "collective action" issues in mass tort cases. The dissent would have taken a much more expansive view of § 1123(b)(6), taking the view that it permits a bankruptcy court to include any provision that it considers "appropriate" to facilitate the Bankruptcy Code's purposes, including non-consensual releases of non-debtors. The dissent further expressed concern that the majority's reasoning would, even if unintentionally, cast doubt on the inclusion in a bankruptcy plan of consensual third-party releases, full-satisfaction releases, or the exculpation of parties and professionals for actions taken during a bankruptcy case, because, on the majority's reading, there was no clear basis to include such provisions in a bankruptcy plan, under Bankruptcy Code § 1123(b)(6) or otherwise.

Immediate Aftermath, Takeaways, and Considerations

The Supreme Court's opinion seeks to resolve one of the most controversial matters facing bankruptcy courts in recent years—the permissibility of non-consensual third-party releases—and firmly rejects them in all circumstances outside asbestos cases. The dissent's and debtors' fears that creditors would get nothing absent the releases has not yet materialized—once the decision was rendered, all parties headed back into mediation to resolve the dispute on the new legal landscape almost immediately. However, it remains to be seen how quickly the parties can come to a consensual resolution, if at all. Moreover, the decision leaves various other issues unresolved, which will likely result in further litigation.

First, and even though the Supreme Court expressly noted it was not deciding this issue, its reasoning casts some doubt on the inclusion of both consensual third-party releases and full-satisfaction releases in bankruptcy plans, as the dissent recognized. If § 1123(b)(6) must relate solely to the *debtor* and its "rights and responsibilities," as the Supreme Court held, then on what basis can even consensual *non-debtor* releases be included in a bankruptcy plan? It may be possible to justify the inclusion of consensual non-debtor releases in a plan as, essentially, the use of the plan as a mechanism to establish a contract for non-debtors to release claims against other non-debtors. The consensual nature of such relief largely eliminates the concern that the Bankruptcy Code is being abused to benefit private parties who have not satisfied all the criteria for a bankruptcy discharge. As to "full-satisfaction" third-party releases, however, which are non-consensual, it may be challenging to justify including them in a bankruptcy plan following *Purdue*. There is no apparent basis under § 1123(b)(6) to include such releases of non-debtors, and the plan is not being used as a vehicle to offer a contract. It may be possible to argue that they are justified under some other provision of the Bankruptcy Code, or general law providing for the extinguishment of liability upon full satisfaction, but this reasoning may not work if the full-satisfaction release purports to modify the claimant's rights against the third party in any respect not permitted under generally-applicable law. We can expect such arguments to be made in the future, and counter-arguments to be raised by dissatisfied creditors.

Second, and assuming the continued permissibility of consensual third-party releases, the Supreme Court did not decide what constitutes consent. That issue has already been litigated in various cases, with some courts holding that a *failure to object* amounts to consent, and others taking a view of consent as requiring some *express indication of assent*. This issue has already surfaced in the post-*Purdue* confirmation decision in the bankruptcy of Red Lobster Management LLC, Case No. 6:24-bk-02486-GER, in which the bankruptcy court granted approval of the debtor's disclosure statement only on the condition that "opt-out" third-party releases (binding parties to such release unless they affirmatively opt out) be removed from the plan, in favor of "opt-in" third-party releases (rendering releases only effective as to parties who affirmatively opt in). On the other hand, Judge Lopez in the Bankruptcy Court of the Southern District of Texas has recently approved a plan containing opt-out third-party releases, holding that such opt-out releases were consensual and not barred by *Purdue*. *See In re Robertshaw US Holding Corp.*, 2024 Bankr. LEXIS 1958, at *49–54 (Bankr. S.D. Tex. Aug. 16, 2024). The issue of consent will now take on an outsized importance. If the more expansive view of consent is widely adopted, then, as a practical matter, the *Purdue* decision may not result in a radical change in results in mass-tort cases.

Third, parties will likely raise the *Purdue* case to argue exculpations of parties for their actions during bankruptcy cases are no longer permitted, as suggested by the dissent. That argument is unlikely to prevail. Courts have long been recognized as having an inherent authority to control and limit claims that can be asserted against parties in a case before it, including in the seminal decision of *Barton v. Barbour*, 104 U.S. 126 (1881). Moreover, exculpations only apply to actions taken in connection with a debtor's bankruptcy case, to advance that bankruptcy case. As such, they arguably contain a more direct nexus to the debtor's reorganization efforts than the releases in *Purdue*. As a result, it is unlikely that *Purdue* should be construed to cast doubt on properly tailored exculpations.

Fourth, issues concerning the constitutionality of non-consensual third-party releases have not been resolved. We can expect such issues to be raised and litigated in the future, including in asbestos cases, where non-consensual third-party releases are explicitly authorized under Bankruptcy Code § 524(g).

Finally, although the availability of non-consensual third-party releases has led to successful debt restructurings with enhanced recoveries for creditors stemming from contributions of such parties to pay for such releases, the *Purdue* decision does not eliminate the benefit of third-party settlements to help fund chapter 11 plans. Although *Purdue* eliminates non-consensual releases of *direct* claims of creditors against settling third parties, plans may still settle the *debtor's* claims, and thus claims derivative of the debtor's claims, and such settlements would in most cases still be highly valuable and worth substantial contributions by third parties. Although such parties have historically insisted on full non-consensual releases because case law allowed them, such parties may accept the releases that survive *Purdue* in exchange for a similar level of currency they would have paid for non-consensual releases pre-*Purdue*. Indeed, all parties in the Purdue Pharma case have since returned to mediation to reach a new deal, though the results of that mediation remain to be seen.

Moreover, bankruptcy courts acknowledge the availability of litigation stays under Bankruptcy Code § 105 remain appropriate and permissible in certain circumstances to protect third parties while settlements are negotiated. *In re Parlement Techs., Inc.*, 2024 Bankr. LEXIS 1627, at *11 (Bankr. D. Del. Jul. 15, 2024). Other creative solutions may exist to work around, or within the parameters of, the Purdue decision. For example, the Long Island Roman Catholic diocese, which has been in bankruptcy as a result of alleged sexual abuse claims for approximately 4 years, recently announced a settlement of all claims against it and its parishes. To provide releases to those parishes, which did not file for bankruptcy with the diocese, the diocese plans to file extremely short chapter 11 cases for the parishes for the sole purpose of effectuating the diocese's settlement with alleged sexual abuse victims and obtaining discharges from tort liability. As a result of these clarifications and work arounds, the long-term impact of the *Purdue* decision may well be significantly less than its perceived significance today.

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