

April 21, 2023

Supreme Court Holds That Section 363(m) of the Bankruptcy Code Is Not Jurisdictional

On April 19, 2023, the U.S. Supreme Court unanimously held in *MOAC Mall Holdings LLC v. Transform Holdco LLC* that Section 363(m) of the Bankruptcy Code is not jurisdictional. The decision requires parties timely to invoke that provision, or else risk forfeiting its protections. The decision also continues the Supreme Court's trend of interpreting statutes to be non-jurisdictional (and thus waivable or forfeitable) in the absence of a clear congressional statement to the contrary.

Background

This case involves several provisions of the Bankruptcy Code. First, Section 363(b) permits a debtor or trustee to sell or lease the property of a bankruptcy estate outside of the ordinary course of the entity's business. Second, Section 365(f)(2)(b) prohibits the assignment of an unexpired lease without "adequate assurance of future performance by the assignee." Third, Section 363(m) states that "[t]he reversal or modification on appeal of an authorization under [Section 363(b)] of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal."

Sears, Roebuck and Co. filed for Chapter 11 bankruptcy in 2018. Early the next year, Sears agreed to sell certain assets to respondent Transform Holdco LLC. One of those assets was the right to designate the entity to which a lease between Sears and a landlord should be assigned. The bankruptcy court approved the agreement.

Transform then designated a lease with landlord petitioner MOAC Mall Holdings to its own wholly owned subsidiary. MOAC objected that Sears failed to provide the adequate assurance of future performance required under Section 365(f)(2)(B) of the Bankruptcy Code. The bankruptcy court rejected that argument and approved the assignment. The bankruptcy court also denied MOAC's request for a stay pending appeal, noting that Transform stated it would not invoke Section 363(m). On appeal to the district court, Transform reversed course and invoked Section 363(m). The district court affirmed, considering itself bound by Second Circuit precedent to treat Section 363(m) as jurisdictional (and therefore capable of being raised at any time). The Second Circuit likewise affirmed based on its precedent.

Because the Third and Eleventh Circuits had previously held that Section 363(m) was non-jurisdictional, the Supreme Court granted MOAC's petition for certiorari to resolve the conflict with the Second Circuit.

The Supreme Court's Decision

In a unanimous opinion written by Justice Jackson, the Supreme Court held that Section 363(m) is not jurisdictional and is thus waivable and forfeitable. The Court first reaffirmed its test for distinguishing jurisdictional provisions from non-jurisdictional ones. A provision is jurisdictional only if it "pertain[s] to 'the power of the court rather than to the rights or obligations of the

parties.” To be treated as jurisdictional, a provision must “clearly state[]’ as much.” The consequences, as the Court explained, are significant because a jurisdictional issue can be raised at any time in the litigation, but a non-jurisdictional issue can be waived or forfeited.

Applying that test, the Court concluded that Section 363(m) is not jurisdictional. The Court reasoned that Section 363(m) “takes as a given the exercise of judicial power over any authorization under § 363(b) or § 363(c),” rather than granting such authority. As the Court put it, Section 363(m) is a “caveated constraint on the effect of a reversal or modification.” Rather than being jurisdictional, Section 363(m) “merely cloak[s] certain good-faith purchasers or lessees with a targeted protection of their newly acquired property interest, applicable even when an appellate court properly exercises jurisdiction.” And as the Court further observed, “Congress separated § 363(m) from the Code provisions that recognize federal courts’ jurisdiction over bankruptcy matters” and “does not contain any ‘clear tie’ to the Code’s plainly jurisdictional provisions.”

The Court further rejected Transform’s remaining arguments for treating the provision as jurisdictional. First, the Court determined that Transform’s discussion of traditional principles of *in rem* jurisdiction at most “offer[ed] a reason to think Congress intended Section 363(m) to be jurisdictional” and did not rise to the level of a clear statement. Second, the Court declined to treat the provision as jurisdictional simply because some courts arguably treated its predecessor, former Federal Rule of Bankruptcy Procedure 805, as jurisdictional. The Court emphasized that those decisions “predate[d] this Court’s effort to ‘bring some discipline’ to the use of the term ‘jurisdictional.’”

The Court also rejected Transform’s argument that the case was moot because the bankruptcy court lacked authority to reconstitute the leasehold as property of the estate. The Court did not resolve the merits of the question whether the bankruptcy court had such authority, which the Second Circuit had not addressed. The Court instead concluded that there was a live case or controversy because “MOAC simply seeks ‘typical appellate relief: that the Court of Appeals reverse the District Court and that the District Court undo what it has done.’”

Implications

The most immediate implication of the Court’s decision is that parties must timely obtain the protections of Section 363(m) in bankruptcy court, as is commonly done in Section 363(b) sale orders. If parties forfeit those protections by failing to raise them or waive them by expressly disclaiming reliance on them, the issue may not be raised on appeal.

More broadly, this case is yet another instance of the Court narrowing the range of statutory provisions that are treated as jurisdictional. Older cases often used the term quite loosely. But in recent years, the Court has relied on the clear-statement rule to protect against the risk that one party will sandbag its opponent (and lower courts) by waiting too long to raise issues. Going forward, it is highly likely that the Supreme Court and lower courts will continue to enforce that clear-statement rule.

* * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Paul M. Basta
+1-212-373-3023
pbasta@paulweiss.com

Robert A. Britton
+1-212-373-3615
rbritton@paulweiss.com

Kelley A. Cornish
+1-212-373-3493
kcornish@paulweiss.com

Alice Belisle Eaton
+1-212-373-3125
aeaton@paulweiss.com

Brian S. Hermann
+1 212-373-3545
bhermann@paulweiss.com

Sean A. Mitchell
+1-212-373-3356
smitchell@paulweiss.com

Andrew M. Parlen
+1-212-373-3141
aparlen@paulweiss.com

Kannon K. Shanmugam
+1-202-223-7325
kshanmugam@paulweiss.com

John Weber
+1-212-373-3656
jweber@paulweiss.com

Kenneth S. Ziman
+1-212-373-3733
kziman@paulweiss.com

Associates Brian M. Lipshutz and Yishai Schwartz contributed to this Client Memorandum.