SEPTEMBER 17, 2021

District Court Affirms Exide Confirmation Order Finding Third-Party Releases Appropriate and That Plan Satisfies *Midlantic* Standard for Abandonment of Contaminated Property

On July 26, 2021, the United States District Court for the District of Delaware (the "District Court") affirmed the Delaware bankruptcy court's order (the "Confirmation Order") confirming the chapter 11 liquidation plan (the "Plan") of Exide Holdings, Inc. and its debtor affiliates (the "Debtors," and together with their non-Debtor affiliates, "Exide").[1] The District Court rejected the California Department of Toxic Substances Control's (the "DTSC") appeal of the Confirmation Order, finding that while the appeal met the criteria for equitable mootness, it could readily be resolved on the merits against the appealing party. The opinion is notable for its conclusion that the Debtors satisfied the standard for abandoning a heavily contaminated industrial site under section 554 of the Bankruptcy Code because the Plan provided adequate funding for remediation and other procedures that together ensured that the site posed no imminent threat to public safety. The District Court also held that the Plan's releases – including non-consensual third-party releases in favor of supporting

[1] *In re Exide Holdings, Inc., et al*., No. 20-11157-CSS, 2021 WL 3145612 (D. Del. July 26, 2021). The docket of the Debtors' chapter 11 cases is cited herein as "B.D.I. _." Transcripts of the confirmation hearing held before the Bankruptcy Court on October 15, 2020 and October 16, 2020 are cited herein as "10/15/20 Tr._" and "10/16/20 Tr._," respectively.

noteholders (the "Releases") – were the *sine qua non* for the affected creditors to voluntarily contribute funds to consummate the Plan, and were therefore appropriate in scope. Importantly, the District Court rejected a *per se* rule that third-party releases were not allowed in liquidating chapter 11 plans.

Background

Exide was a global leader in stored electrical energy solutions and one of the world's largest producers and recyclers of lead-acid and lithium-ion batteries.[2] It operated in more than 20 countries through four global business groups – Transportation Americas, Transportation Europe and Rest of World, Industrial Energy Americas, and Industrial Energy Europe and Rest of World.[3] By early 2020, Exide faced mounting environmental remediation expenses, rising costs and operational inefficiencies, which were exacerbated by the COVID-19 pandemic.[4] On May 19, 2020, the Debtors commenced chapter 11 cases in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court"), Exide's second chapter 11 case since 2013 and the third in its history.[5]

Over the course of their chapter 11 cases, the Debtors (a) accepted a stalking horse credit bid submitted by an ad hoc group of their secured noteholders (the "Consenting Creditors") for their Europe and Rest of World ("Europe/ROW") business and (b) consummated a sale of substantially all of their Americas assets to a third-party buyer.[6] On a parallel track, to reduce the risk that the various contaminated sites would be abandoned during the course of the bankruptcy, the Debtors engaged in mediation with various environmental agencies to transition or abandon their so-called non-performing properties (the "NPPs").[7] Exide faced significant environmental remediation liabilities from approximately 16 NPPs across the United States, including a battery recycling facility in Vernon, California (the "Vernon Site").[8] The Vernon Site ceased operating in 2015, but remained highly contaminated and required constant monitoring and containment to assure that hazardous substances would not be released into the environment.[9]

Having sold substantially all of their assets, the Debtors would no longer be in business at the end of the chapter 11 cases, and accordingly could no longer retain and support remediation of the NPPs.[10] The Debtors ultimately reached agreement on the preliminary terms of a global settlement of their environmental liabilities with the DOJ, EPA and numerous state and local environmental agencies, including the DTSC. The global settlement provided, among other things, for the creation of an environmental remediation trust (the "ERT") that would be funded by a $10 million contribution from the Europe/ROW business (which was funded through $36 million in bridge financing extended to the Europe/ROW business by the Consenting Creditors) – with $2.6m of that amount allocated to the Vernon Site.[11] However, with two weeks left before the start of the Debtors' confirmation hearing, the California Governor's office rejected the global settlement. In response, the Debtors amended the settlement and the Plan to provide, among other things, that: (a) the DTSC would receive a $2.6m contribution if the Bankruptcy Court approved the Releases, (b) the Vernon Site would be transferred to an environmental remediation trust (the "Vernon ERT") if the DTSC entered into an agreement with the environmental trustee providing covenants not to sue and (c) if the DTSC

2 B.D.I. 14, ¶ 7.
3 *Id*.
4 *Exide*, 2021 WL 3145612, at *1.
5 *See In re Exide Technologies*, Case No. 13-11482 (MFW) (Bankr. D. Del. June 10, 2013); *In re Exide Technologies*, Case No. 02-11125 (KJC) (Bankr. D. Del. April 15, 2002).
6 *Exide*, 2021 WL 3145612, at *1.
7 *Id*. at *2.
8 B.D.I. 14, ¶ 73.
9 *Exide*, 2021 WL 3145612, at *1.
10 *Id.*
11 B.D.I. 942, ¶ 19.

did not sign the agreement with the environmental trustee, or the Releases were not approved by the Bankruptcy Court, the Vernon Site would be abandoned pursuant to Section 554(a) of the Bankruptcy Code.[12]

After a contested hearing, the Bankruptcy Court confirmed the amended Plan.[13] To prevent the abandonment of the Vernon Site, the DTSC executed covenants not to sue and the Vernon Site was transferred to the Vernon ERT. The DTSC nevertheless appealed the Confirmation Order, arguing that the Plan should not have been confirmed because it presented the DTSC with a "Hobson's choice" – either accept the intolerable abandonment of the Vernon Site, or agree to its transfer to an underfunded environmental response trust.[14] The DTSC also challenged the legality of the Plan's releases and injunctive provisions.

The District Court Rules That the Plan Meets the Standards for Equitable Mootness

On appeal to the District Court, Judge Richard G. Andrews affirmed the Confirmation Order and dismissed the DTSC's appeal on the merits, notwithstanding his determination that dismissal was also warranted on equitable mootness grounds. The District Court began by noting that the doctrine of "equitable mootness" is narrow and empowers an appellate court to forbear deciding an appeal if granting the requested relief would undermine the finality and reliability of a consummated chapter 11 plan.[15] The Third Circuit standard for assessing equitable mootness considers (a) whether a confirmed plan has been substantially consummated[16] and (b) if so, whether granting the requested relief will fatally scramble the plan and/or significantly harm third parties who justifiably relied on plan confirmation.[17] In finding that the appeal met the criteria for equitable mootness, the District Court concluded that the Plan had been substantially consummated – in light of the fact that all relevant property had been transferred, the Debtors' successors had assumed management of the businesses and remaining estate property, and Plan distributions had begun.

Turning to the next factor, the District Court then considered whether the DTSC's requested relief – which contemplated narrowing the releases applicable to the DTSC and allocating up to $43 million of additional consideration towards the remediation of the Vernon Site – would result in the collapse of the Plan and harm third parties who acted reasonably in reliance on the finality of confirmation. The District Court found that the Consenting Creditors agreed to contribute settlement payments to remediate the NPPs and fund general unsecured claimant recoveries in exchange for the Releases – without which the global settlement and the Plan would have fallen apart.[18] The District Court likewise rejected the DTSC's request to allocate an additional $43 million to the Vernon Site. It noted that the Consenting Creditors had no obligation to put *any* money into the global settlement, and that the Bankruptcy Court had no power to force third-party creditors to make settlement payments over their objection. The District Court held that doing so "would circumvent the bankruptcy process and give the DTSC by judicial fiat what it could not achieve by consensus within the Chapter 11 proceedings."[19]

Turning to the Merits, the District Court Holds That the Plan Satisfies the *Midlantic* Standard for Abandonment and Approves Third-Party Releases Contained Therein

Under section 554 of the Bankruptcy Code, a court ordinarily can authorize abandonment of property that is burdensome to the estate.[20] In *Midlantic Nat'l Bank* v. *New Jersey Dep't of Envtl. Prot.*, the Supreme Court recognized a "narrow" exception to that power, concluding that a bankruptcy court cannot "authorize an abandonment without formulating conditions that will adequately protect the public's health and safety."[21] Accordingly, courts disallow abandonment if (a) the abandonment itself

12 *See* B.D.I. 871; B.D.I. 944, ¶ 20.
13 10/16/20 Tr. 170:16–19; 181:9–182:1.
14 *Exide*, 2021 WL 3145612, at *4.
15 *Id*. at *5.
16 The Bankruptcy Code defines substantial consummation to mean: (A) transfer of all or substantially all of the property proposed by the plan to be transferred; (B) assumption by the debtor or by the successor to the debtor under the plan of the business or of the management of all or substantially all of the property dealt with by the plan; and (C) commencement of distribution under the plan. *Id*. (citing 11 U.S.C. § 1101(2)).
17 *Id*. at *4 (citing *In re Tribune Media Co.*, 799 F.3d 272, 277 (3d Cir. 2015)).
18 *Id*. at *6 (citing *Tribune,* 799 F.3d at 280).
19 *Id*. (citing *Tribune,* 799 F.3d at 281).
20 *Id*. at *8 (citing 11 U.S.C. § 554).
21 474 U.S. 494, 502, 507 & n.9 (1986).

poses an imminent and identifiable harm to the public health or safety and (b) the debtor is attempting to abandon property in contravention of state or local laws or regulations designed to protect the public.[22]

The District Court found that the Plan satisfied the standard for abandonment established by the Supreme Court in *Midlantic.* Citing the evidence presented at the confirmation hearing, the District Court noted that the Plan provided $26 million in financial assurances and a $2.6 million settlement contribution towards the remediation of the Vernon Site – even more than the $27 million that the DTSC itself had estimated was needed to implement certain initial, "Phase I" remedial actions.[23] The District Court also noted that the Confirmation Order provided for the orderly transfer of responsibility for the site and continuation of protections for the public's health and safety, declining to second-guess the Bankruptcy Court's determination that the Vernon Site did not pose an "imminent threat."[24] Additionally, the District Court rejected the DTSC's position that the Supreme Court's decision in *Midlantic* prohibited abandonment of the Vernon Site simply because it still required additional remediation.[25] The District Court concluded that such an understanding of *Midlantic* would replace the Supreme Court's narrow exception with a requirement that bankrupt parties must assume long-term obligations and eliminate all long-term risks before abandonment.[26]

Finally, the District Court also found that the releases in favor of the Consenting Creditors were proper in light of their substantial contributions towards the implementation of the global settlement – which included, among other things, (a) extending $36 million in bridge financing to the Europe/ROW business, which was used by those Exide Europe entities to fund the Plan's $18.5 million in settlement payments, (b) consenting to the use of cash collateral and debtor-in-possession financing, (c) purchasing the Europe/ROW business, (d) waiving deficiency claims on account of their secured notes and (e) releasing liens on the NPPs.[27] The District Court rejected the DTSC's contention that Exide's bankruptcy case did not present an "extraordinary case" justifying the grant of non-consensual third-party releases – citing testimony from the United States Department of Justice's Environmental Enforcement Section (a party to the settlement negotiations) that the case was "unprecedented" because of "the complex environmental issues and the limited financial resources available for remediation."[28] The District Court accordingly concluded that the unique facts and circumstances of the case supported the Bankruptcy Court's finding that the Releases were "*sine qua non*" for the Consenting Creditors to voluntarily contribute funds necessary to implement the global settlement and consummation of the Plan.[29] In addition, the District Court rejected the DTSC's position that non-consensual third-party releases are unavailable in liquidating cases – noting that (a) the case was not a chapter 7 liquidation and (b) the Plan involved a combination of reorganization transactions (namely, the Europe/ROW sale and the transfers of the NPPs to the two trusts) as well as the liquidation of the Debtors' remaining assets.[30]

Conclusion

The District Court's decision provides useful clarity around the scope of a debtor's abandonment power in bankruptcy. By rejecting the DTSC's position that *Midlantic* requires a debtor to fund long-term environmental liabilities as a condition to abandonment, the opinion provides guidance on the types of measures a debtor can implement that adequately protect the public's health and safety, and accordingly, would permit abandonment pursuant to section 554 of the Bankruptcy Code.

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22 *Exide*, 2021 WL 3145612, at *8 (citing *In re Unidigital, Inc.*, 262 B.R. 283, 286–87 (Bankr. D. Del. 2001)).

23 *Exide*, 2021 WL 3145612 at *8.

24 *Id.* at *10. In so ruling, the District Court noted that although the DTSC's position asked the court to reweigh the record evidence, the court's review on appeal was limited to determining whether the Bankruptcy Court's findings were clearly erroneous. *Id*. at 15.

25 *See Midlantic*, 474 at 507 & n.9.

26 *Exide*, 2021 WL 3145612 at *9.

27 *Id.* at *13.

28 *Id.* at *14.

29 *Id.* In the Third Circuit, courts assess "fairness, necessity to the reorganization, and [must make] specific factual findings to support [such] conclusions" in determining whether to grant non-consensual releases. *In re Cont'l Airlines*, 203 F.3d 203, 214 (3d Cir. 2000). Such considerations might include whether: "(i) the non-consensual release is necessary to the success of the reorganization; (ii) the releasees have provided a critical financial contribution to the debtor's plan; (iii) the releasees' financial contribution is necessary to make the plan feasible; and (iv) the release is fair to the non-consenting creditors, *i.e.* whether the non-consenting creditors received reasonable compensation in exchange for the release." *In re Spansion, Inc.*, 426 B.R. 114, 144 (Bankr. D. Del. 2010).

30 *Id*. at *13.

Together with the District Court's ruling reaffirming the legality of third-party releases, the opinion emphasizes the Bankruptcy Code's power to help debtors with limited funds and substantial liabilities successfully implement a chapter 11 plan. The opinion also proves a useful reminder of the importance of a comprehensive evidentiary record in connection with plan confirmation.

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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:

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