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Post-Confirmation Assumption And Rejection

Law360, New York (March 04, 2009) -- While the Bankruptcy Code does not expressly provide for it, most parties in bankruptcy proceedings assume trustees or debtors-in-possession should be allowed a reasonable period of time to decide whether to assume or reject executory contracts.

The courts have tended to agree, stipulating debtors must make this decision by the date of confirmation of a plan of reorganization, and no later.

For example, the court in *In re Dana Corp.*, 350 B.R. 144, 147 (Bankr. S.D.N.Y. 2006) stated “[I]t is clear policy of the Bankruptcy Code to provide the debtor with breathing space following the filing of a bankruptcy petition, continuing until confirmation of the plan, in which to assume or reject an executory contract.”

This is also consistent with prior practice under the Bankruptcy Act, as seen in *In re Grayson-Robinson Stores Inc.*, 227 F. Supp. 609, 613 (S.D.N.Y. 1964), a pre-Bankruptcy Code case where the court refused to permit rejection of executory contract after confirmation.

There is also nothing in the legislative history of the Bankruptcy Code that demonstrates Congress intended to extend the debtor-in-possession’s assumption and rejection powers with respect to executory contracts past the confirmation date.

And, it is well established that courts should not freely interpret the Bankruptcy Code to effect a major change in practice unless it is the subject of at least some discussion in the legislative history. See *Dewsnup v. Timm*, 502 U.S. 410, 419 (1992).

Despite this, however, some courts have improperly interpreted Bankruptcy Code sections 365 and 1123 as providing a statutory basis to extend the time to assume and reject executory contracts beyond the confirmation date of a plan.

For example, in *DJS Properties v. Simplot*, 397 B.R. 493 (D. Idaho 2008), the confirmed plan of reorganization provided that the debtor could assume or reject a certain partnership agreement after confirmation.

On appeal, the non-debtor counterparty to the partnership agreement contended that the debtor could not be allowed to assume or reject the partnership agreement after a plan is confirmed and argued that the debtor must make that decision at or before confirmation.

When deciding the appeal, the district court focused on the statutory language of Bankruptcy Code Sections 365 and 1123. Section 365 provides that “the trustee may assume or reject an executory contract ... at any time before the confirmation of the plan ...” 11 U.S.C. § 365(d)(2).

Section 1123(b)(2) further provides that a Chapter 11 reorganization plan “may ... subject to section 365 ... provide for the assumption, rejection, or assignment of any executory contract ... not previously rejected under such section[.]” 11 U.S.C. § 1123(b)(2).

It affirmed the bankruptcy court, finding Sections 365 and 1123 allow for post-confirmation assumption or rejection of an executory contract. It reasoned that these sections are permissive and do not expressly prohibit a plan from “providing” for assumption or rejection by selecting a post-confirmation date for that action.

The district court also reasoned that allowing for post-confirmation assumption and rejection furthered the Congressional intent to treat executory contracts flexibly in Chapter 11 reorganizations.

However, the district court’s decision in *DJS Properties v. Simplot* collides with well-established law that, following confirmation, the plan proponent is merely a reorganized debtor (rather than a debtor-in-possession) and cannot exercise the powers granted to debtors-in-possession and trustees under the Bankruptcy Code.

See *In re Northwestern Corp.*, Case No. 03-12872, 2005 Bankr. LEXIS 367, * 2 n. 1 (Bankr. D. Del. Mar. 10, 2005) (“[I]n this case, the plan of reorganization has been confirmed, and under section 1141(b), the confirmation of the plan vests all of the property of the estate in the debtor.

Thus, there is no longer a debtor-in-possession, i.e., trustee”). On its face, Bankruptcy Code section 365 provides that the “trustee, subject to the court’s approval, may assume or

reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a) (emphasis added).

Since the bankruptcy estate does not survive post-confirmation and the property of the estate reverts in the reorganized debtor on the effective date of the plan, there is no surviving entity that can exercise the rights of a trustee, including the right to assume and reject executory contracts under Bankruptcy Code section 365.

Likewise, Bankruptcy Code section 1123(b)(2) does not provide statutory authorization for post-confirmation assumption or rejection of executory contracts because its provisions are expressly "subject to [Bankruptcy Code] section 365." 11 U.S.C. § 1123(b)(2).

Allowing for a post-confirmation assumption and rejection also creates a number of potentially problematic confirmation issues. The nondebtor contract counterparty may challenge the plan's feasibility when it is premised on the existence of income or other benefits derived from a critical contract, and there are significant issues regarding the reorganized debtor's ability to assume the contract.

These include whether defaults under the contract may be cured and whether the reorganized debtor would have the financial resources to pay the cure amount.

Another feasibility issue that will need to be addressed at the confirmation hearing is quantifying the possible post-confirmation rejection damages.

Finally, a debtor may disenfranchise creditors from their fundamental rights of voting on the Chapter 11 plan by choosing to postpone the announcement of its decision to reject contracts until after plan confirmation.

Based on this, *DJS Properties v. Simplot* and other cases allowing for post-confirmation assumption or rejection of contracts are wrongly decided as Bankruptcy Code sections 365 and 1123 do not provide statutory authority for assumption and rejection by a reorganized debtor and post-confirmation assumption and rejection is not a viable option because nondebtor parties lose valuable protections provided by the Bankruptcy Code.

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