Supreme Court Pokes a Hole in the Ironclad Nature of Bankruptcy 363 Sales

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MOAC Mall Holdings LLC v. Transform Holdco LLC, 143 S. Ct. 927 (April 19, 2023)

Purchasers often relish the prospect of buying distressed assets in a bankruptcy proceeding. Under section 363 of the Bankruptcy Code, a buyer may obtain ownership of bankruptcy estate assets "free and clear of any interest" (assuming certain conditions are met), and also be reasonably confident that the sale will not be reversed on appeal. But the U.S. Supreme Court may have now tempered that confidence. In its unanimous opinion, *MOAC Mall Holdings LLC v. Transform Holdco LLC*, authored by Justice Ketanji Brown Jackson, the Supreme Court held that one of section 363's protections for these sales on appeal is not "jurisdictional" and therefore may render section 363 sales less immune to appeal.

The *MOAC Mall* case concerned a sale that took place in the Sears, Roebuck and Co. bankruptcy. Sears filed chapter 11 in 2018, and in 2019 it sold substantially all of its assets to Transform Holdco LLC ("Transform") pursuant to section 363 of the Bankruptcy Code. Transform was given the right to designate an assignee for any Sears lease that was transferred as part of the transaction. One such lease was Sears' lease at the Minnesota Mall of America, owned by MOAC Mall Holdings LLC ("MOAC"). Transform designated the Mall of America lease for assignment to Transform's wholly-owned subsidiary, but MOAC objected on the basis that Transform could not provide adequate assurance of future performance, as required by subsection 365(b)(3), which relates specifically to shopping center leases. The bankruptcy court overruled that objection and approved the assignment.

MOAC appealed the bankruptcy court's approval of the assignment and also sought a stay of the assignment order. In seeking a stay, MOAC was concerned about subsection 363(m) of the Bankruptcy

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Code, which states:

> The reversal or modification on appeal of an authorization under [§363(b) or §363(c)] 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.

In other words, MOAC feared that without a stay pending appeal, any substantive appeal of the assignment would be futile. The bankruptcy court denied the request for a stay pending appeal, in part because Transform made a representation that it would not invoke subsection 363(m) against MOAC.

On appeal, the district court initially ruled in MOAC's favor, holding that Transform did not provide the requisite adequate assurance and vacating the assignment. Transform then sought rehearing and—notwithstanding its earlier representation that it would not invoke subsection 363(m)—expressly argued that subsection 363(m) "deprived the District Court of jurisdiction to grant MOAC's requested relief." Though "'appalled'" at Transform's "gambit," the district court reluctantly agreed that subsection 363(m) is jurisdictional—and therefore non-waivable—and dismissed MOAC's appeal. The Second Circuit affirmed.

The Supreme Court granted MOAC's petition for certiorari to reconcile a circuit split on the question of whether subsection 363(m) is "jurisdictional." The Third, Sixth, Seventh, Ninth, Tenth, and Eleventh Circuits have held that subsection 363(m) is not jurisdictional, while the Fifth and, with *MOAC Mall*, Second Circuits have held that subsection 363(m) is jurisdictional.

The Supreme Court concluded that subsection 363(m) is not jurisdictional because Congress did not "clearly" designate it as jurisdictional. As Justice Jackson explained, the stakes of this textual analysis were high. If subsection 363(m) is jurisdictional, "a party may invoke [it] at any time—without fear of waiver, forfeiture, or similar doctrines interposing." This matters because not even "egregious conduct by a litigant"—such as Transform's going back

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on its promise not to invoke subsection 363(m)—"could permit the application" of another such doctrine, like judicial estoppel, "as against a jurisdictional rule."

The district court and Second Circuit had both concluded that subsection 363(m) was jurisdictional. Even though they expressed a clear distaste for Transform's conduct, the lower courts viewed their hands as tied and applied subsection 363(m) anyway.

Given these stakes, Justice Jackson noted that the Supreme Court has in recent years "endeavored 'to bring some discipline'" to whether statutory provisions are jurisdictional. The Court's guiding principle is to "only treat a provision as jurisdictional if Congress 'clearly states' as much."

The Supreme Court held that Congress had not "clearly state[d]" that subsection 363(m) is jurisdictional. This conclusion was based on the text of section 363 itself. As Justice Jackson noted, "§363(m) plainly contemplates that appellate courts might 'revers[e] or modif[y]' *any* covered authorization, with a proviso: Sometimes, the court's exercise of power may not accomplish all the appellant wishes, because the reversal or modification of a covered authorization may not 'affect the validity of a sale or lease under such authorization' to a good faith purchaser or lessee under certain prescribed conditions." Justice Jackson also noted the statutory context: subsection 363(m) is separated from the Bankruptcy Code provisions that recognize federal courts' bankruptcy jurisdiction. As a result, the Court concluded that subsection 363(m) is not jurisdictional.

The Supreme Court also rejected Transform's alternative argument that the dispute was moot under Article III of the United States Constitution.

Key Takeaways

- The Supreme Court's determination that subsection 363(m) is not jurisdictional likely weakens, to one degree or another, the position of purchasers in bankruptcy sales.
- Purchasers in a section 363 sale will need to keep in mind *MOAC Mall*'s holding that subsection 363(m)'s protections

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might be waived or remain subject to other avenues of attack.

- Tread carefully and avoid taking any inadvertent action (in writing or otherwise) that could be construed as a waiver of subsection 363(m) rights.
- Purchasers should also consider including language in sale documents and/or the order by the bankruptcy court approving the sale.

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