St. John's University School of Law
St. John's Law Scholarship Repository

Bankruptcy Research Library | Center for Bankruptcy Studies

2017

Bankruptcy Courts May Alter Final Sale Orders and Findings of Good Faith Purchasers

Louis Calabro

Follow this and additional works at: https://scholarship.law.stjohns.edu/bankruptcy_research_library

 Part of the Bankruptcy Law Commons

This Research Memorandum is brought to you for free and open access by the Center for Bankruptcy Studies at St. John's Law Scholarship Repository. It has been accepted for inclusion in Bankruptcy Research Library by an authorized administrator of St. John's Law Scholarship Repository. For more information, please contact selbyc@stjohns.edu.

ST. JOHN'S UNIVERSITY
SCHOOL OF LAW

Bankruptcy Courts May Alter Final Sale Orders and Findings of Good Faith Purchasers

2017 Volume IX No. 4

Bankruptcy Courts May Alter Final Sale Orders and Findings of Good Faith Purchasers

Louis Calabro, J.D. Candidate 2018

Cite as: *Bankruptcy Courts May Alter Final Sale Orders and Findings of Good Faith Purchasers,* 9 ST. JOHN'S BANKR. RESEARCH LIBR. NO. 4 (2017).

Introduction:

For many years, a policy of finality has existed in the legal sphere to protect purchasers after a sale has been completed.[1] This policy serves to create stability and predictability for investors and incentivizes activity in the marketplace.[2] In bankruptcy cases, issues of finality are implicated when a debtor engages in an asset sale, and the court grants a final sale order.[3] The purchasing party wants the sale to be final, so courts have promoted the policy of finality to enhance the efficiency and effectiveness of bankruptcy plans.[4] Sometimes, however, an adverse party claims to have an interest in assets that the debtor sold and wants to challenge the approved sale.[5] In such event, the adverse party can make a Rule 59 motion to compel the court to amend a judgment and attempt to reverse the sale.[6] Alternatively, the adverse party can make a Rule 60

---

[1] *In re CADA Invest., Inc.,* 664 F.2d 1158, 1162 (9th Cir. 1981).
[2] *Id.*
[3] *See In re Agriprocessors, Inc.*, 465 B.R. 822 (N.D. Iowa 2012).
[4] *See id.*
[5] *See id.*; *In re Global Energies, LLC*, 763 F.3d 1341 (11th Cir. 2014).
[6] Fed. R. Civ. P. § 59; *Pacific Ins. Co. v. American Nat. Fire Ins. Co.*, 148 F.3d 396 (4th Cir. 1998).

motion and obtain relief from a final order if certain criteria are satisfied.[7] However, to preserve the policy of finality, courts must narrowly assess the facts of each case and may only vacate a sale order in very limited circumstances.[8]

In many asset sales, the purchasing party is afforded an additional protection as a good faith purchaser.[9] Usually, sales made to good faith purchasers are final even if another party appeals them.[10] However, bankruptcy courts may revisit and revoke a finding that one was a good faith purchaser, eliminating the additional protections and making it easier to alter final sales.[11] If the policy of finality does exist, and courts can revisit and revoke final sale orders and affirmative good faith purchaser judgments, an important question arises: when does the court's discretionary power outweigh the policy of finality?

This memorandum will assess the aforementioned question in three sections. Section I will examine when a court may revoke final sale orders under the Federal Rules of Civil Procedure § 60 ("Rule 60"). Section II will examine when a court may revoke a judgment that granted a good faith purchaser status to a party under the Federal Rules of Civil Procedure § 59 ("Rule 59"). Section III will conclude by examining both rules and their impact on the policy of finality and chapter 11 assets sales.

I. Courts May Revoke Final Sale Orders Where a Rule 60 Motion Is Timely, Meritorious, and Not Unfairly Prejudicial

[7] Fed. R. Civ. P. § 60; *Nat'l Credit Union Admin Bd. v. Gray,* 1 F.3d 262, 264 (4th Cir. 1993).
[8] *In re Chung King, Inc.*, 752 F.2d 547 (7th Cir. 1985).
[9] Section 363(m) of the United States Bankruptcy Code (the "Bankruptcy Code") provides:
> The reversal or modification on appeal of an authorization under subsection (b) or (c) of this section 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. 11 U.S.C. § 363 (m).

[10] *Id.*
[11] Fed. R. Civ. P. §59(e); *In re Gunboat Int'l. Ltd.*, 557 B.R. 410, 423 (Bankr. E.D.N.C. 2016).

Rule 60 allows a district court to relieve a party from a final judgment, effectively changing a prior ruling. Fed. R. Civ. P. § 60. Additionally, Rule 60 has been incorporated by the Federal Rules of Bankruptcy Procedure to apply to bankruptcy courts as Rule 9024. Fed. R. Bankr. P. § 9024. Rule 60(c) provides that a Rule 60 motion must be made "within a reasonable time – and . . . no more than a year after the entry of the . . . order or the date of the proceeding." Fed. R. Civ. P. § 60(c)(1). Moreover, a Rule 60 motion must present a meritorious defense to the action and show that the opposing party would not be unfairly prejudiced by setting the order aside. *In re Gunboat Int'l. Ltd.*, 557 B.R. 410*; Nat'l Credit Union Admin. Bd. v. Gray,* 1 F.3d 262, 264 (4th Cir.1993). If a party successfully meets this criteria, it must then satisfy one of the six grounds for relief listed in Rule 60(b).[12]

In determining whether a Rule 60 motion is timely, the court must assess whether the moving party brought the motion within a reasonable time.[13] This factor lacks a bright-line rule and is left up to the court's discretion.[14] Moreover, a Rule 60 motion may be timely even if it is brought after the final sale order has already been issued.[15] Thus, the discretionary test for

---

[12] *Nat'l Credit Union Admin. Bd. v. Gray,* 1 F.3d at 266; Fed. R. Civ. P. Rule 60 (b) provides as follows:
(b) Grounds for Relief from a Final Judgment, Order, or Proceeding. On motion and just terms, the court may relieve a party or its legal representative from a final judgment, order, or proceeding for the following reasons:
(1) mistake, inadvertence, surprise, or excusable neglect;
(2) newly discovered evidence that, with reasonable diligence, could not have been discovered in time to move for a new trial under Rule 59(b);
(3) fraud (whether previously called intrinsic or extrinsic), misrepresentation, or misconduct by an opposing party;
(4) the judgment is void;
(5) the judgment has been satisfied, released or discharged; it is based on an earlier judgment that has been reversed or vacated; or applying it prospectively is no longer equitable; or
(6) any other reason that justifies relief.

[13] Fed. R. Civ. P. Rule 60(c)(1).

[14] *See In re Gunboat Int'l. Ltd.*, 557 B.R. 410 (finding the motion was timely even though the adverse party never responded to debtor's email notifying him of the sale).

[15] *Id.* (finding the motion was timely when it was brought 19 days after a court issued a final sale order).

timeliness is broad, and Rule 60 motions may be approved weeks after a final sale order has been entered.[16]

Whether a Rule 60 motion presents a meritorious defense depends upon the facts of each case and what the parties argue; however, district courts have broad discretion in their assessment, and abuse of discretion only occurs if the district court relies on "clearly erroneous factual findings or if its decision relies on erroneous legal conclusions."[17] Moreover, an adverse party can meet the meritorious defense requirement by questioning the purchaser's good faith status.[18] This incentivizes adverse parties to question the purchaser's good faith status whenever applicable, to satisfy Rule 60's meritorious defense burden.[19] Moreover, even where there has not been sufficient evidence of a meritorious defense on appeal, federal courts have declined to reverse bankruptcy courts' decisions based upon bankruptcy courts' broad equitable powers.[20]

Whether a Rule 60 motion will not unfairly prejudice the debtor and purchasing parties depends upon the length of time passed from the final sale order's issuance, the procedural formalities of the sale, and whether a party has received rights in reliance on the final order.[21] If the Rule 60 motion is brought before all funds and assets have been properly transferred, or if the court has not yet seen a bill of sale or closing statement, it will not unfairly prejudice the debtor or the purchaser.[22] Furthermore, the unfair prejudice factor is "of lesser importance" than the other factors, and there may be situations where a final order is vacated even though it creates

[16] *See id.*
[17] *In re Agriprocessors, Inc.*, 465 B.R. at 828.
[18] *In re Gunboat Int'l. Ltd.*, 557 B.R. at 424.
[19] *Id.*
[20] *See In re CADA Invest., Inc.,* 664 F.2d 1158, 1161 (9th Cir. 1981).
[21] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 425; *In re Phillips,* 553 B.R. 536 (E.D. North Carolina 2016); *In re Lenox*, 902 F.2d 737 (9th Cir. 1990).
[22] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 425.

unfair prejudice.[23] Thus, where a party moves quickly, it might be able to compel bankruptcy courts to affirm Rule 60 motions and vacate final sale orders.[24]

II. Alternative Source for Relief: Courts May Alter a Judgment to Account for New Law, Evidence, and Prevent Manifest Injustice

Rule 59(e) grants district courts the power to alter and amend judgments after their entry, as long as a party files the motion no later than 28 days after the entry of the judgment.[25] The Federal Rules of Bankruptcy Procedure have also incorporated Rule 59 motions to proceedings in bankruptcy courts, as Rule 9023.[26] While the rule itself does not provide a standard for which motions shall be granted, case law provides three instances where a Rule 59(e) motion should be granted: "(1) to accommodate an intervening change in controlling law; (2) to account for new evidence not available at trial; or (3) to correct a clear error of law or prevent manifest injustice."[27] These motions are extraordinary remedies, and may only be granted when new information allows a party to make new arguments that they could not have made prior to the judgment.[28]

However, when a dealing with an assets sale to a good faith purchaser, a party can make a Rule 59(e) motion to question the purchaser's good faith status if any new evidence regarding the transaction gives rise to an argument against it.[29] This is particularly effective where a third party had an interest in property in an asset sale, and can provide new or previously unavailable

---

[23] *Nat'l Credit Union Admin Bd. v. Gray,* 1 F.3d 262, 265 (4th Cir. 1993).
[24] *In re Gunboat Int'l. Ltd.*, 557 B.R. at 426.
[25] Fed. R. Civ. P. § 59(e); Fed. R. Civ. P. Rule 59(e) advisory comm. nn. ("This subdivision has been added to care for a situation such as that arising in *Boaz v. Mutual Life Ins. Co. of New York,* C.C.A.8, 1944, 146 F.2d 321, and makes clear that the district court possesses the power asserted in that case to alter or amend a judgment after its entry. The subdivision deals only with alteration or amendment of the original judgment in a case and does not relate to a judgment upon motion as provided in Rule 50(b)").
[26] Fed. R. Bankr. P. Rule 9023.
[27] *Pacific Ins. Co. v. American Nat. Fire Ins. Co.*, 148 F.3d 396 (4th Cir. 1998).
[28] *Id.*; *Federal Practice and Procedure* § 2810.1, at 127–28 (2d ed. 1995).
[29] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 421 (granting Rule 59(e) motion where new testimony described information not available to the court at the hearing on the sale motion).

evidence about the nature of its interest.[30] However, the moving party must still give a legitimate explanation for why the new evidence was not provided at earlier proceedings.[31]

Where new evidence or controlling law does not emerge, a party can still satisfy the requirements of Rule 59(e) by showing that a judgment should be reversed to prevent a clear error or manifest injustice.[32] Clear error exists where a court entered judgment inconsistent with controlling law or statute.[33] Manifest injustice is measured within the discretion of the court, but can be shown where a judgment was supported by fraud or foul play.[34]

When a Rule 59(e) motion is made to amend a prior judgment of a good faith purchaser, the courts must assess whether the purchaser bought the asset (1) for value and (2) in good faith.[35] To determine whether one purchased for value, the court must be able to ascertain the overall value of the debtor's estate, and then must determine whether the purchasing price was the highest bid or a comparable bid to a more reliable purchaser.[36] Additionally, to determine whether one purchased in good faith, the court must assess whether the purchaser had knowledge or notice of any adverse claims on the assets.[37] Yet this knowledge does not have to be definitive; it may be sufficient to show that the purchaser *may* have known of other claims on the assets if enough evidence supports the speculation.[38] Since this process also functions through

---

[30] *See id.* (granting Rule 59(e) motion where the new information described settlement agreement negotiations, and the moving party believed that the assets it was negotiating for would be excluded from the asset sale).
[31] *Pacific Ins. Co. v. American Nat. Fire Ins. Co.*, 148 F.3d at 403.
[32] Fed. R. Civ. P. § 59(e); *Pacific Ins. Co. v. American Nat. Fire Ins. Co.*, 148 F.3d at 403.
[33] *Id.* at 404 (granting a Rule 59(e) motion to reverse a prior Rule 59(e) motion ruling that allowed a party to use new evidence that *was* previously available to amend a judgment).
[34] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 423.
[35] *Id.*; *In re Agriprocessors, Inc.*, 465 B.R. 822.
[36] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 421-22.
[37] *Id.* at 422-23.
[38] *Id.* at 423 (finding sufficient evidence to grant Rule 59(e) motion based upon speculations that the good faith purchaser acted in bad faith prior to the bid).

the court's discretionary powers, courts have broad power to revisit good faith findings and revoke them.[39]

III. Bankruptcy Courts' Broad Equitable Powers and the Discretion-Based Tests of Rules 59 and 60 Allow Courts to Override the Policy of Finality

Throughout the years, case law has described Rule 60 and Rule 59(e) motions as drastic measures that should only be used to vacate final sale orders in very limited circumstances.[40] When good faith purchasers are involved in final sale orders, section 363(m) of the Bankruptcy Code grants protections to the sale on appeal. These limitations give weight to the policy of finality; however, the recent case, *In re Gunboat Int'l. Ltd.,* shows why the policy of finality has become more limited as the law has evolved. There the court allowed a party to challenge a final sale order to a good faith purchaser through a collateral attack, stating that the § 363(m) protections only exist on appeal.[41] Furthermore, the court reversed a final sale order nineteen days after it was granted and reversed the prior judgment that the sale was made to a good faith purchaser.[42]

Since Rule 59(e) and 60 involve discretionary tests, and bankruptcy courts have broad equitable powers, any party that wants to dispute an asset sale to a good faith purchaser should make a Rule 59(e) or 60 motion on collateral attack and get around the good faith purchaser protections.[43] Even in instances where the evidence presents a speculative argument against good faith purchaser protections, a court can in its discretion revoke the good faith purchaser title.[44] Moreover, case law has stated that while the policy of finality is important, the equitable

[39] *See id.*; *In re Agriprocessors, Inc.*, 465 B.R. 822.
[40] *In re Chung King, Inc.*, 752 F.2d 547 (7th Cir. 1985).
[41] *In re Gunboat Int'l. Ltd.*, 557 B.R. 410.
[42] *Id.*
[43] *See id.*
[44] *Id.*

concerns of Rule 60(b) outweigh it, further limiting its effect.[45] Thus, bankruptcy courts may reconsider or modify the policy of finality when vacating prior final sale orders or good faith judgments, so long as the moving party satisfies the requirements of Rule 59(e) or 60.

Conclusion

While overcoming the burden of finality is no easy hurdle, recent case law shows that it is possible. The Rule 59(e) and 60 motions allow adverse parties to compel courts to vacate prior orders.[46] Even where good faith purchasers are involved in an asset sale, parties can attempt a collateral attack to get around section 363(m) of the Bankruptcy Code and compel a court to revoke its prior finding of good faith under Rule 59(e) or 60.[47] Moreover, Rule 60 allows a court to revoke a prior order for any reason that justifies relief so long as the motion is made within a reasonable time – which leaves the ultimate decision to the court's discretion. However, equitable concerns heavily limit the application of these motions, since "reconsideration of a judgment after its entry is an extraordinary remedy which should be used sparingly.'"[48] Additionally, the policy of finality will likely compel courts to dismiss Rule 59(e) and 60 motions where final orders confer intervening rights to a party.[49] Still, recent case law shows that overcoming the policy of finality is a possibility, especially where meritorious allegations of bad faith exist.[50] Thus, where an adverse party seeks to vacate a final order, the policy of finality no longer reigns absolute.

---

[45] *Id.* at 424.
[46] *See Id.*; *In re Global Energies, LLC*, 763 F.3d 1341 (11th Cir. 2014).
[47] *In re Global Energies, LLC*, 763 F.3d 1341.
[48] *Pacific Ins. Co. v. American Nat. Fire Ins. Co.*, 148 F.3d 396 (quoting 11 Wright et al., *Federal Practice and Procedure* § 2810.1, at 127–28 (2d ed. 1995)).
[49] *See In re Lenox*, 902 F.2d 737.
[50] *See In re Gunboat Int'l. Ltd.*, 557 B.R. at 421-22; *In re Global Energies, LLC*, 763 F.3d 1341; *In re CADA Invest., Inc.,* 664 F.2d 1158).