

First Circuit Court of Appeals Clarifies Previous Guidance in Circuit on Committee Rights

December 7, 2017

On September 22, 2017, the First Circuit Court of Appeals (the “Court” or “First Circuit”) held that an official committee of unsecured creditors has an unconditional right to intervene in an adversary proceeding pursuant to Rule 24(a)(1) of the Federal Rules of Civil Procedure (the “Federal Rules”), thus reversing a decision of the United States District Court for the District of Puerto Rico (the “District Court”).

In *Assured Guaranty Corp. v. The Financial Oversight and Management Board of Puerto Rico*, several of Puerto Rico’s bond insurers initiated an adversary proceeding in the Commonwealth’s debt adjustment under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act (“PROMESA”). The bond insurers alleged primarily that Puerto Rico’s proposed fiscal plan and accompanying implementing statute violated both PROMESA and the United States Constitution, and sought, among other things, an injunction against implementing the fiscal plan. The official committee of unsecured creditors (the “Committee”) appointed in the case moved for leave to intervene in the adversary proceeding pursuant to Federal Rule 24(a)(1), made applicable pursuant to Rule 7024 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”), and section 1109(b) of title 11 of the United States Code (the “Bankruptcy Code”).

Under Federal Rule 24(a)(1), “the court must permit anyone to intervene who . . . is given an unconditional right to intervene by federal statute.” Further, Bankruptcy Code section 1109(b) states, “[a] party in interest, including a . . . creditors’ committee . . . may appear and be heard on any issue” in a chapter 11 case. In its motion, the Committee argued that section 1109(b) conferred the “unconditional right” to intervene in the adversary proceeding as required by Federal Rule 24(a)(1). However, the District Court, relying on a footnote in the First Circuit’s 1992 decision in *Kowal v. Malkemus (In re Thompson)*, which stated that Bankruptcy Code section 1109(b) “does not afford a right to intervene under [Federal] Rule 24(a)(1),” denied the Committee’s motion, and the Committee appealed to the First Circuit.

The First Circuit began by noting that, though appearing to be directly applicable to the instant controversy, *Thompson’s* discussion of Bankruptcy Code section 1109(b) was pure *dicta*, as it was a case under chapter 7 of the Bankruptcy Code and, thus, section 1109 was wholly inapplicable. The Court further noted that “the statutory language is, indeed, quite broad,” as the Committee may appear and be heard “on any issue in a case,” and it was unlikely that Congress would have used such sweeping language if it had not meant the language to be broadly inclusive. As such, reasoned the Court, the Committee had met the requirement of Federal Rule 24(a)(1) and had the “unconditional right” to intervene in the adversary proceeding, as the clear language of section 1109(b) is

absent any conditions whatsoever on a party in interest's right to appear and be heard. The Court cautioned, however, that the unconditional right to intervene did not abrogate a court's right to dictate the scope of participation once the intervention is granted.

In finding this unconditional right to intervene, the First Circuit recognized the circuit split on the issue, noting that the Fifth Circuit Court of Appeals, in *Fuel Oil Supply and Terminaling v. Gulf Oil Corp.*, declined to find that Bankruptcy Code section 1109(b) applied to adversary proceedings based, among other things, on a general hesitation to find unconditional statutory rights of intervention. Though the Fourth and Tenth Circuit Courts of Appeals have suggested agreement with *Fuel Oil's* analysis of the issue, the Second and Third Circuit Courts of Appeals join the First Circuit in its expansive reading of section 1109(b), finding that it provides an unconditional right to intervene under Federal Rule 24(a)(1).

1. 48 U.S.C. §§ 2161 *et seq.*
2. 965 F.2d 1136 (1st Cir. 1992).
3. *Id.* at 1142 n.8.
4. Section 1109(b) allows parties in interest to “appear and be heard on any issue in a case *under this chapter* .” 11 U.S.C. § 1109(b) (emphasis added).
5. 762 F.2d 1283 (5th Cir. 1985).

If you have any questions regarding the representation of unsecured creditors' committees in chapter 11 proceedings or the First Circuit's recent decision, please feel free to contact:

Travis Powers at [973-849-9010](tel:973-849-9010) or via email at tpowers@cullenanddykman.com

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