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8th Circ. Says Court Hastily Invoked Ch. 11 'Mootness' Rule

By **Jeff Montgomery**

Law360 (August 5, 2021, 9:26 PM EDT) -- The Eighth Circuit on Thursday reversed a Northern District of Iowa dismissal of a stockholder challenge to a fish farm's bankruptcy plan in 2019, rejecting the lower court's reliance on an often criticized "equitable mootness" doctrine to toss the appeal.

The appellate decision, which ordered further lower-court proceedings, concluded that the district court failed to justify findings that the appeal should be tossed as equitably moot, under a doctrine that supports dismissal if scuttling or unscrambling a plan would do more harm than good.

The three-judge panel's decision, written by Circuit Judge James P. Loken, found that the lower court should have fully examined the merits of stockholder FishDish LLP's claims that controlling creditors of VeroBlue Farms acted unfairly and in bad faith in the company's \$100 million Chapter 11, tilting its terms in their favor and then selling the business afterward.

Absent from the dismissal, the circuit ruling said, was a "sufficiently rigorous test" to determine if "bankruptcy equities and pragmatics" justified forgoing a full review of the appeal from VeroBlue Farms' Chapter 11 confirmation order in May 2019.

Kept alive with the Eighth Circuit decision were allegations by FishDish that the plan for VeroBlue — a central Iowa seafood farm that opened a \$100 million Chapter 11 proceeding in November 2018 — unfairly favored plan sponsor and stockholder Alder Aqua Ltd. and senior creditor Broadmoor Financial LP at the expense of other claims and creditors.

Alder Aqua subsequently sold the Webster City, Iowa, operation to NaturalShrimp Inc. under an agreement announced last year.

U.S. District Court Judge C.J. Williams' dismissal of the Chapter 11 appeal in October 2019 found in part that "there is an interest in finality. That interest outweighs the interest in a party's right to appeal an adverse decision. This court finds the policy of finality to be more important than the public policy of permitting an appeal in this case."

Unexamined, the Eighth Circuit found, were FishDish's claims that the plan unfairly discriminated between members of the same shareholder class, violated the Bankruptcy Code's absolute priority rule, was proposed in bad faith and was financially infeasible. In addition, FishDish argued, the bankruptcy proceedings failed to investigate and value claims.

"An Article III appellate court has a 'virtually unflagging obligation' to exercise its subject matter jurisdiction," the Circuit Court opinion noted, quoting a 2013 decision in the *In re Semcrude* bankruptcy in the District of Delaware.

Courts have relied on equitable mootness as a purportedly commonsense means of preventing harm to multiple parties when a plan has been substantially consummated and unwinding creates a risk of wide harm, the Eighth Circuit decision noted.

But the practice has been "thoughtfully criticized by many circuit judges" and has aroused suspicions that some bankruptcy plans are structured and rushed through confirmation with equitable mootness in mind, in order to support claims that dismantling them would prove unjustifiably harmful,

according to the opinion.

In VeroBlue's case, out of the \$13.5 million that the plan sponsor committed to the case, half went to the senior creditor, with the sponsor assuming management of the reorganized business. Proposals to inject new capital into the business, meanwhile, did not materialize.

"If that did not take place because the reorganized debtors were preparing for a quick asset sale instead of resuming operations," the case takes on the look of a Chapter 11 plan in need of review by an appellate review in District Court, the Circuit judges found. "We do not assume how these factual inquiries may be resolved. We decide only that the inquiry must be made."

"If the confirmed plan must be set aside on the merits, the district court may be able to fashion effective relief for those whose rights were impaired by the plan," the appellate decision found, "even if the business assets have been sold to a third-party purchaser relying on the confirmed plan, such as disgorgement."

Although FishDish won a remand on the equitable mootness claim, the court overturned a lower court decision that rejected senior creditor Broadmoor's claim that FishDish missed a 14-day deadline for challenging Broadmoor's claims.

The opinion also cautioned that if equitable mootness, "becomes the rule of appellate bankruptcy jurisprudence" rather than an exception to appellate review, "we predict the Supreme Court, having up to now denied petitions for certiorari to review the doctrine, will step in and severely curtail — perhaps even abolish — its use."

Judge L. Steven Grasz and Judge Jonathan A. Kobes joined in the decision.

FishDish LLP is represented by Nathan E. Delman, Stavros S. Giannoulas, John W. Guzzardo and Aaron Hammer of Horwood & Marcus and Jordan Michael Talsma and John R. Walker Jr. of Beecher & Feld.

VeroBlue Farms USA Inc. is represented by Dan Childers of Elderkin & Pirnie and Robert H. Lang of Thompson & Coburn.

Broadmoor Financial L.P. is represented by Kelsey Nicole Frobisher and Shannon D. Wead of Foulston & Siefkin and Jeffrey P. Taylor of Klinger & Robinson.

Alder Aqua Ltd. is represented by Abram V. Carls and Eric W. Lam of Simmons & Perrine and Eric J. Langston of Moye & White.

The case is FishDish LLP v. VeroBlue Farms USA Inc., et al., case number 19-3413 and 19-3487 in the United States Court of Appeals for the Eighth Circuit.

--Editing by Peter Rozovsky.