Alert

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COZEN O'CONNOR

SCOTUS Goes to Mall of America: Court Recognizes Jurisdiction Over Appeals of Bankruptcy Sale Orders

In August 1992, the largest indoor shopping mall in the continental United States opened to great fanfare in suburban Minneapolis. Dubbed the Mall of America (MOA), this sprawling retail center enjoyed 330 stores, anchored by retail tenants at the height of their reputations: Macy's, Bloomingdale's, Nordstrom, and Sears Roebuck and Co. (Sears). MOA even included the indoor amusement park Camp Snoopy, complete with a roller coaster and log chute ride.[1] At 5.6 million square feet, it remains the largest indoor shopping complex in the continental United States and the second largest in North America.

Some 30 years later, MOA and the now-defunct Sears are making news again. In a recent decision involving the assignment of Sears' long-term lease at MOA, the U.S. Supreme Court overruled lower court orders barring a landlord from contesting the validity of its bankrupt tenant's lease assignment. The Sears lease is novel. Executed in 1991, the lease could run for 99 years and included base rent of only $10 per year. Yes, you read this correctly – $10 per year with more than 60 years of potential lease term to be exploited.

The decision arises out of the 2018 bankruptcy of Sears. Within the bankruptcy case, Sears sought to assign its lease to a third party, Transform Holdco LLC.[2] The U.S. Bankruptcy Court approved the assignment over MOA's objection. After initially vacating the order approving the assignment on substantive grounds,[3] on appeal, the District Court determined that it lacked jurisdiction to consider the matter. The Second Circuit Court of Appeals affirmed that determination. MOA sought review in the U.S. Supreme Court, which granted certiorari.

The jurisdictional dispute is based on application of Section 363(m), which provides, in relevant part:

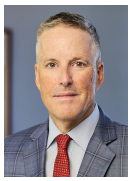
> The reversal or modification on appeal of an [order approving a sale of assets of the bankruptcy estate] … does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

The Second Circuit is among the courts that view Section 363(m) as jurisdictional, and, in the absence of a stay, an appeal of a sale order was limited to the question of good faith. Other courts, including the Third Circuit Court of Appeals, hold that the statute is not jurisdictional but only limited the relief that might be available through the successful appeal of an unstayed order.

The Supreme Court resolved the circuit split in a unanimous opinion, holding that Section 363(m) is *not* jurisdictional. See *MOAC Mall Holdings LLC v. Transform Holdco LLC*, 143 S. Ct. 927 (2023). According to the Supreme Court, federal statutes should only be interpreted as limiting courts' jurisdiction when there is a "clear statement" that Congress intended such an interpretation, and the language of Section 363(m) does not meet that standard.

Nothing in *MOAC Mall Holdings* would in any way limit the protection afforded good faith purchasers under Section 363(m), and the Supreme Court specifically avoided discussing what sort of relief MOA might ultimately realize through the appeal. Perhaps the most significant takeaway from this decision is that parties to any appeal of a sale order must assert their rights under Section 363(m) at the outset of the appeal, or those rights may be waived.

The issue on remand will be whether the assignee is able to provide "adequate assurance of future performance" under the lease. In the case of leases of property in shopping centers, adequate



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assurance of future performance includes a number of specific elements, including adequate assurance:

> of the source of rent and other consideration due under such lease, and in the case of an assignment, that the financial condition and operating performance of the proposed assignee and its guarantors, if any, shall be similar to the financial condition and operating performance of the debtor and its guarantors, if any, as of the time the debtor became the lessee under the lease …

This statutory requirement is significantly more onerous than the relevant terms of the Sears lease, however. Rather than having to show that a proposed assignee is in a similar financial condition to that of Sears in 1991, when the lease was executed, outside of bankruptcy, the lease would be freely assignable to any entity with a net worth or shareholder equity of at least $50 million. The Bankruptcy Court held that the contractual terms superseded the statutory requirement for adequate assurance and found that the proposed assignee had satisfied the net worth requirement. In its first (and subsequently vacated) opinion, the District Court reversed the Bankruptcy Court, holding that the statutory financial condition requirement was not supplanted by the contract terms.

On remand, therefore, it appears that Transform Holdco LLC, as the proposed assignee, will have the heavy burden of establishing that its financial condition is similar to that of Sears circa 1991. This is a tall order and would appear to be all but impossible,[4] but, absent a consensual resolution, further appeals are likely inevitable.

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[1] After failing to come to terms on the royalties to be paid for use of the Peanuts® characters, MOA did not renew the Camp Snoopy lease agreement in 2006. On March 15, 2008, the park became a Nickelodeon-themed park called *Nickelodeon Universe®*.

[2] Formed to acquire some of the assets of Sears, the company is the brainchild of Sears' one-time CEO, Eddie Lampert.

[3] MOA's objection involved certain provisions of the Bankruptcy Code that are particular to assignments of leases in shopping centers. The entire procedural history and details of the dispute are beyond the scope of this Alert and involved material facts that are unlikely to recur, owing to the very unusual terms of what the District Court described as an "extraordinary lease." *In re Sears Holdings Corp.*, 613 B.R. 51, 79 (S.D.N.Y.), *order vacated on reh'g*, 616 B.R. 615 (S.D.N.Y. 2020).

[4] According to its annual report, Sears reported total shareholder equity in excess of $14 billion in 1991.