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### § 363 Sale Order Protects New GM from Most Ignition Switch Claims

The purchaser of the assets of the former General Motors Company (Old GM), through a § 363 sale in its chapter 11 case, will not be liable to car owners for injuries occurring before the sale or later economic losses caused by defective ignition switches, a United States bankruptcy judge decided. In a 134-page decision, Bankruptcy Judge Robert E. Gerber found that presale injury and death creditors, and economic loss creditors holding claims estimated between \$7 and \$10 billion, could not assert successor liability claims against the so-called “New GM.” The decision, which is likely to be appealed directly to the Second Circuit, illustrates the risks that fast-paced bankruptcy sales generate and offers some comfort to purchasers that they will not be held accountable for the prior actions of a bankrupt seller.

Old GM descended into bankruptcy at the height of the financial crisis. A condition of its government-backed rescue package was that its assets be sold within 40 days to stem its alarming cash burn rate. To meet that deadline, the massive asset sale under § 363 of the bankruptcy code was quickly arranged. At the time of the sale, however, Old GM had sold an estimated 27 million cars with ignition switch defects. These defects are alleged to have caused at least 84 deaths, and millions of car owners were driving defective cars without knowing the potential risks. What is more, at least 24 Old GM engineers, attorneys, and other employees were aware of the problem—some as early as 2003.

In June 2009, Old GM filed a motion (Sale Motion) for authorization to sell its assets free and clear of all liens, claims, encumbrances, and other interests, “including specifically all successor liability claims.” Old GM mailed notice of the proposed sale to all parties who had already asserted claims against Old GM (whether through litigation or otherwise). However, for car owners yet to assert claims stemming from the ignition switch defect, and who were likely unaware of the defect, notice of the Sale Motion was only provided by publication in a variety of newspapers. In granting the Sale Motion, the bankruptcy court entered an order (Sale Order) declaring that Old GM’s assets were being sold free and clear of all claims (including successor liability claims) and enjoining all persons from asserting successor liability claims against New GM. Two months later, in September 2009, the bankruptcy court ordered that all creditors of Old GM file proofs of claim on or before November 30, 2009. Notice of this claims bar date was given in the same manner as notice of the Sale Motion. Nonetheless, claims, including those resulting from ignition switch problems, continued to trickle in for years after the bar date.

In spring 2014, New GM publicly announced the existence of the ignition switch defect for the first time, and millions of recall notices were sent to owners of defective vehicles. For some of those owners, this was the first time they had learned of the ignition switch defect and the potential economic cost of that defect to them, such as reduced resale value of their vehicles, missed work necessitated by bringing recalled vehicles in for repair, and similar costs. These owners, along with owners of defective vehicles involved in accidents prior to the § 363 sale and owners of nondefective GM vehicles who claimed losses due to resale value reductions (together, Claimants), sought to enforce their claims against New GM under various successor liability theories. To stop these claims, New GM filed motions to enforce the free and clear provisions of the Sale Order.

The Claimants argued that they had been denied the notice required by due process under the Constitution. Specifically, they argued that Old GM failed to give actual mailed notice of the Sale Motion and the claims bar date despite Old GM's actual knowledge of the existence of the ignition switch defect and the location of many owners of defective cars (who later received recall notices by mail).

In its decision, the bankruptcy court agreed that Old GM's notices did not satisfy the requirement of due process. Despite this constitutional defect, the court essentially found that this failure of notice was a wrong without a remedy. The bankruptcy court rejected two potential avenues to afford relief to the Claimants. First, the court denied the Claimants' attempt to pursue New GM for the alleged wrongs of Old GM. In so doing, the court explained that many of the 850 filed objections considered at the hearing on the Sale Motion had ably argued against the bar to successor liability contained in the Sale Order, and these issues had been fully considered and rejected. The court determined that the outcome would not have been different even if additional Claimants had presented those same objections.

The court also denied the Claimants the right to participate in distributions from the trust established to pay allowed claims against Old GM. The court explained that the bulk of the trust had already been distributed to Old GM's creditors and that the remaining funds were reserved for those creditors in the process of resolving or litigating disputes with respect to their claims. Distribution to the Claimants from these reserves would result in an inequitable distribution of assets to the holders of disputed but timely claims against Old GM to the extent those disputed claims are eventually allowed. Ultimately, the only relief the bankruptcy court was willing to afford to the Claimants was to confirm that they could pursue New GM for any claims that arise solely on account of any wrongful conduct by New GM.

The decision offers valuable lessons for buyers and their lenders in § 363 sales. Asset purchasers and their financiers should have renewed confidence that liabilities of a bankrupt seller will not follow the assets sold if appropriate provisions are included in the sale order; however, some level of diligence concerning a debtor's liabilities and the adequacy of the sale procedures is undoubtedly worthwhile, given the potential challenges which may arise post-sale. Even if the sale order includes appropriate free and clear provisions, asset purchasers will want to promptly address dangers to the public when risks not disclosed by the seller come to light. The failure to do so may allow creditors to walk through the only door left open in the GM decision: pursuit of claims against the buyer due to its own culpable conduct.

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