UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

In re Delta Air Lines, Inc.

608 F.3d 139 (2d Cir. 2010) · No. 08-5002-bk, 08-5230-bk, 08-5236-bk, 08-5239-bk · Decided July 13, 2010

SUMMARY

Claimants who were owner participants in leveraged aircraft leases appealed the disallowance of their tax indemnification claims against Delta Air Lines in bankruptcy. The Second Circuit held that the contractual exclusion provisions did not bar the claims merely because Delta's obligations were discharged in bankruptcy or because payment of stipulated loss value was demanded or partially made. The court vacated the district court's judgment and remanded with instructions to overrule Delta's objections.

CASE DETAILS

COURT	United States Court of Appeals for the Second Circuit
WRITING FOR THE COURT	Pierre N. Leval; Robert A. Katzmann; Debra Ann Livingston
JURISDICTION	Federal
DECIDED	July 13, 2010
DOCKET	08-5002-bk, 08-5230-bk, 08-5236-bk, 08-5239-bk
DISPOSITION	vacated
PROCEDURAL POSTURE	Claimants in Delta's Chapter 11 bankruptcy appealed from a Southern District of New York decision affirming Bankruptcy Court orders that sustained Delta's objections to approximately $1 billion in tax-indemnification claims arising under leveraged-aircraft-lease agreements.
STANDARD OF REVIEW	De novo review of contract-interpretation issues.
PRECEDENTIAL VALUE	published and precedential
PARTIES	The Northwestern Mutual Life Insurance Company, DFO Partnership, AT&T Credit Holdings, Inc. v. Delta Air Lines, Inc., Bank of New York, as Indenture Trustee and Pass Through Trustee, Bank of America, N.A., Strategic Value Partners, LLC

TOPICS

contract interpretation · proof of claim · chapter 11 · bankruptcy · appellate procedure

PRACTICE AREAS

bankruptcy contracts tax appellate procedure

QUESTIONS PRESENTED

1. Whether the tax-indemnification agreements' references to Delta having paid stipulated loss value included the bankruptcy discharge of Delta's obligations.
2. Whether the phrase requiring Delta to be required to pay stipulated loss value was satisfied merely by a demand for payment, without payment being made.
3. Whether payment of a percentage of stipulated loss value or lease-rejection damages calculated by reference to stipulated loss value discharged Delta's tax-indemnification obligations.
4. Whether the Owner Participants' tax-indemnification claims were barred because allowing them would create duplicative recovery for a single loss or violate bankruptcy equality-of-distribution principles.

HOLDINGS

1. The contractual reference to Delta having paid stipulated loss value was not satisfied by the discharge in bankruptcy of Delta's obligation to pay stipulated loss value. The bankruptcy court's interpretation was unreasonable because it nullified the tax-indemnification obligation in the very insolvency circumstances for which the agreements were designed to provide protection.
2. A demand by an Indenture Trustee that Delta pay stipulated loss value did not, without more, establish that Delta was required to pay stipulated loss value so as to trigger the DFO tax-indemnity exclusion. In any event, the record showed that the DFO Indenture Trustee filed claims for stipulated lease-rejection damages rather than stipulated loss value.
3. Payment of a percentage of stipulated loss value, or of lease-rejection damages calculated by starting with stipulated loss value, did not satisfy the Northwestern exclusion provision. The court did not definitively resolve every possible meaning of the phrase, but held that the parties could not have intended any partial payment, however small, to discharge the tax-indemnity obligation.
4. The Owner Participants' tax-indemnity claims were not barred merely because the Indenture Trustees also held stipulated-loss-value or lease-related claims. Separate obligations owed under separate contracts to different parties could coexist, particularly where the Owner Participants had suffered an uncompensated actual loss.

KEY QUOTATIONS

> *"Adoption of the bankruptcy court's construction of "pay" nullified Delta's obligation to pay the Owner Participant under the TIA upon the occurrence most likely to call its provisions into play – Delta's insolvency."* (608 F.3d at 145)

> *"By ruling that partial payment of the Lease claims, in however small an amount, satisfied the exclusion, the bankruptcy court effectively nullified the TIAs by stripping them of their ability to protect the Owner Participant in the event of Delta's default."* (608 F.3d at 148)

> *"If Delta has contracted to pay duplicative claims, then it must pay both—it cannot repudiate its duty to party A under contract A by asserting that it contracted to pay the same amount to party B under contract B."* (608 F.3d at 150)

FACTUAL BACKGROUND

Delta entered into leveraged aircraft leases in which Owner Participants contributed equity and claimed accelerated depreciation deductions, while lenders financed the remainder of the aircraft purchases. The tax indemnification agreements required Delta to compensate the Owner Participants for tax losses caused by depreciation recapture, while the leases separately required stipulated-loss-value payments to the Indenture Trustees upon default. After Delta's bankruptcy, aircraft foreclosures and lease restructurings caused the Owner Participants to incur depreciation-recapture losses, and they filed tax-indemnification claims that Delta opposed on the ground that the contractual exclusion provisions had been triggered by payment, discharge, or partial payment of stipulated loss value.

PROCEDURAL HISTORY

Delta filed for Chapter 11 bankruptcy on September 14, 2005. After the bankruptcy court confirmed Delta's plan of reorganization, the bankruptcy court designated objections to selected tax-indemnification claims as test cases and disallowed the claims of Northwestern, DFO, and AT&T. The United States District Court for the Southern District of New York affirmed, and the Second Circuit vacated the district court's judgment and remanded with instructions to overrule Delta's objections.

DISPOSITION

vacated

REMAND INSTRUCTIONS

Remand to the district court with instructions that Delta's objections to the Appellants' tax-indemnification claims be overruled.

CASES CITED

- Fin. One Pub. Co. v. Lehman Bros. Special Fin., Inc., 414 F.3d 325, 339 (2d Cir. 2005)
- Butner v. United States, 440 U.S. 48 (1979)
- Greenfield v. Philles Records, Inc., 780 N.E.2d 166, 170 (N.Y. 2002)
- Aron v. Gillman, 128 N.E.2d 284, 288 (N.Y. 1955)
- Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co., 549 U.S. 443, 448 (2007)
- Musso v. Ostashko, 468 F.3d 99, 104 (2d Cir. 2006)
- In re Delta Air Lines, Inc., 381 B.R. 57, 68-69, 71, 82 (Bankr. S.D.N.Y. 2008)
- In re Delta Air Lines, Inc., 370 B.R. 552, 557, 559, 562 (Bankr. S.D.N.Y. 2007)