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Second Circuit Affirms Bankruptcy Court's Exercise of Jurisdiction over Post-Confirmation Contractual Dispute.

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Hughes Hubbard & Reed LLP • A New York Limited Liability Partnership
One Battery Park Plaza • New York, New York 10004-1482 • +1 (212) 837-6000

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July 30, 2018 - The United States Court of Appeals for the Second Circuit affirmed a Bankruptcy Court's exercise of jurisdiction over a post-confirmation contractual dispute between Relativity Media, LLC and Netflix, Inc. as a core proceeding.[1]

The dispute between Relativity and Netflix centered around Netflix's assertion that it had the right under a licensing agreement, as amended, to stream two of Relativity's films, *Masterminds* and *The Disappointments Room*, before they were scheduled to be released in the theatres. Netflix's proposed actions would have completely undercut Relativity's recently confirmed chapter 11 plan of reorganization, the feasibility of which was premised on the significant proceeds that Relativity expected to receive from first theatrically releasing the films and then Netflix distributing them under the licensing agreement.

Finding that Netflix did not have the contractual right to do so, the Bankruptcy Court granted Relativity's motion under section 1142(b) of the Bankruptcy Code to enforce the plan and enjoined Netflix from streaming the films before they were released in the theaters.[2] Netflix appealed, arguing that the Bankruptcy Court did not have jurisdiction over the post-confirmation dispute. Both the District Court and the Second Circuit affirmed.

Following its decisions in *In re U.S. Lines*[3] and *In re Petrie Retail, Inc.*,[4] which found core bankruptcy court jurisdiction over post-confirmation disputes concerning the parties' rights to the proceeds of major insurance contracts and the interpretation of a lease assigned under a Bankruptcy Court-approved sale order, the Second Circuit reasoned that the dispute between Netflix and Relativity was a core proceeding because of the impact that Netflix's threatened distribution of the films would have on Relativity's confirmed plan of reorganization.

As recounted by the Second Circuit, during the confirmation proceedings, Netflix objected to Relativity's proposed plan of reorganization, questioning whether Relativity could actually theatrically release the films on the schedule proposed in the plan, and arguing that theatrical release of the films before distribution by Netflix was a material requirement to the licensing agreement. Relativity's confirmed plan of reorganization incorporated Netflix's understanding of the importance of the film's being theatrically released before being streamed on Netflix. Testimony from the hearing on Relativity's motion established that Netflix's pre-release streaming of the films would have eviscerated the revenue streams anticipated by Relativity's plan. The Second Circuit thus concluded that Netflix's change of position would significantly impact the administration of the estate and "undercut the creditor relief provided by the Plan," thus rendering the dispute a core proceeding over which the Bankruptcy Court properly exercised jurisdiction.[5]

Footnotes

[1]. *Netflix, Inc. v. Relativity Media, LLC (In re Relativity Fashion, LLC)*, 696 Fed. App'x 26 (2d Cir. 2017).

[2]. The Bankruptcy Court also found that the doctrines of judicial estoppel and res judicata barred Netflix from asserting it had the right to stream the unreleased films because of the order confirming Relativity's plan of reorganization and the related proceedings before the Bankruptcy Court.

[3]. 197 F.3d 631 (2d Cir. 1999).

[4]. 304 F.3d 223 (2d Cir. 2002).

[5]. Indeed, the Bankruptcy Court did not believe that Netflix's change in position was made in good faith. The Bankruptcy Court believed that Netflix had recently negotiated more advantageous licensing agreements and speculated that "Netflix waited until very late in the process to spring this new issue on the Debtors in the hopes that it could gain leverage to force a contract change or maybe even a contract cancellation." *In re Relativity Fashion, LLC*, No. 15-11989 (MEW), 2016 WL 3212493, at *12 (Bankr. S.D.N.Y. Jun. 1, 2016).

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