JENNER&BLOCK

Recent Developments in Bankruptcy Law, October 2020

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2.1.a **LBO fraudulent transferee was not a "customer" of a financial institution.** As part of a complex series of related transactions, the debtor entered into a note purchase agreement with an investment bank. The agreement specifically disclaimed that the bank was acting as the debtor's agent or owed the debtor any fiduciary duty. The note proceeds were to be used to pay the debtor's shareholders to purchase their shares. The investment bank paid the proceeds directly to the shareholders. The trustee sought to avoid the payment as a fraudulent transfer. Section 546(e) prohibits the trustee from avoiding a transfer that is a settlement payment or a transfer in connection with a securities contract "made by or to (or for the benefit of) a … financial institution" except under section 548(a)(1)(A) as an intentional fraudulent transfer. Under *Merit Mgmt Group, LP v. FTI Consulting, Inc.*, 138 S. Ct. 883 (2018), section 546(e)'s focus is on the transfer to be avoided, without regard to any component parts of the transfer. Here, the trustee sought to avoid the transfer to the shareholders, without regard to the transfer by the bank as a component part of the transfer. However, a financial institution includes not only a bank but also, when the bank "is acting as agent or custodian for a customer … in connection with a securities contract … such customer." An agency relationship requires that the principal vest in the agent authority to act on the principal's behalf, subject to the principal's control, and the agent consents to act. The relationship requires more than an agreement to effect a transaction as an intermediary. Otherwise, any service provider would qualify as an agent. Here, the note purchase agreement expressly disclaims the bank's role as an agent. None of the other agreements in the related transactions expressed an agency relationship. The Code defines "custodian" in terms of one acting to enforce claims. Because the Code contains a definition of custodian, the court may not look to other sources to determine whether the bank qualified as the shareholder's (or debtor's) custodian. The transactions did not involve debt collection, and none of the prongs of the custodian definition applied. Therefore, the court denies the defendants' motion for summary judgment on section 546(e) grounds. *Buchwald Cap. Advs., LLC v. Papas (In re Greektown Holdings, LLC)*, ___ B.R. ___, 2020 Bankr. LEXIS 2938 (Bankr. E.D. Mich. Oct. 19, 2020).

2.1.b **Holder of joint bank account with fraudulent debtor is not liable as a fraudulent transferee.** The debtor opened a joint bank account as an accommodation to a friend, who funded the account. The debtor agreed the account would contain only the friend's money, and, though they both had signatory authority, the debtor would not use the account. Without telling the friend, the debtor later transferred $1 million into the account and simultaneously wrote a check from the account to a company he owned. After bankruptcy, the trustee sued the friend to avoid and recover the fraudulent transfer into the account. A recipient of funds is not necessarily a "transferee" for purposes of section 550(a). Having dominion and control is necessary but not sufficient to find the recipient to be a transferee, rather than a conduit. Here, none of the requirements were met. Because the debtor simultaneously wrote a check draining the account, the friend was completely unaware of the deposit, and the friend did not authorize or participate in the debtor's use of the account, the friend did not have effective dominion or control over the deposit. Nor did the debtor intend to transfer the funds to the friend. He intended to transfer only to his other company, with the joint account acting only as a waystation in the scheme. Therefore, the friend was not a transferee and is not liable to the trustee. *Jalbert v. Gryaznova (In re Bicom NY, LLC)*, ___ B.R. ___, 2020 Bankr. LEXIS 2458 (Bankr. S.D.N.Y. Sept. 21, 2020).

2.1.c **Court extends section 546(a) two-year statute of limitations under Rule 9006(b).** The trustee investigated the debtor's extensive fraud scheme but encountered resistance from many fraud participants and record keepers. The trustee moved for an extension of the section 546(a) statute of limitations for bankruptcy causes of action. Rule 9006(b) authorizes the court to enlarge the time specified in any rule or order of court (with some exceptions) for taking any action. The Rule applies equally to statutory deadlines. Therefore, the court has authority to extend the statute of limitation and, based on the record in this case, concludes that it should. *In re Campbellton-Graceville Hosp. Corp.*, 616 B.R. 177 (Bankr. N.D. Fla. 2020).

2.2 Preferences

2.2.a **New lenders' direct payment to creditor is not a preference.** The debtor owed a law firm money. The debtor's mother agreed to loan the debtor sufficient sums to pay his debt to the law firm on the condition that the funds be used only for that purpose. The debtor executed a promissory note to his mother, who wrote a check to the law firm and delivered it directly to the law firm. A few days later, the debtor filed his bankruptcy petition. A preference is a transfer of an interest of the debtor in property that enables a creditor to recover more than other similarly situated creditors. The debtor has an interest in property if the debtor has dominion or control over the property or if the transfer of the property would diminish property that would have become property of the estate if it had not been transferred. Under these facts, the debtor did not exercise dominion or control over the loan proceeds: his mother controlled them at all times, and he had no ability to direct their distribution. And the loan proceeds did not diminish the estate, because the mother transferred the funds directly to the law firm, the funds never passed through the debtor's hands, and the debtor had no interest in the funds. Therefore, the payment was not a transfer of an interest of the debtor in property. *Walters v. Stevens, Littman, Biddison, Tharp & Weinberg, LLC (In re Wagenknecht)*, 971 F.3d 1209 (10th Cir. 2020).

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2.7.a **Transfer to bank account to support a loan is not a transfer to the bank.** While insolvent, the debtor transferred money from its account at the bank to affiliates' accounts at the bank without consideration as collateral to secure bank loans to the affiliates. The trustee may avoid a transfer for less than reasonably equivalent value made while the debtor was insolvent. A transfer into a bank account is not a transfer to the bank unless the bank has sufficient dominion and control over the account. A security interest in the account does not amount to sufficient dominion and control to permit the bank to withdraw the funds for its own use. However, if the affiliate overdrew the account and the bank finally honored the overdraft, the bank would be a subsequent transferee of a transfer by the debtor into the affiliate's account to replenish the balance. *Scott v. Sun Trust Bank, N.A. (In re Runnymeade Cap. Mgmt.)*, 616 B.R. 67 (Bankr. W.D. Va. 2020).

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5.1.a **Court approves confidential critical vendor payments.** The debtor in possession filed a motion for authority to pay up to $80 million for critical vendors, out of a total of about $400 million in accounts payable, based on 10 questions about each vendor, which were directed at determining whether the vendor was critical and payment was necessary to maintaining the relationship with the vendor. The motion contemplated that the DIP would provide the full list of critical vendors and, each week, a list of actual payments, to the committee and the US Trustee. The lists were not filed with the court, and the court had no role (absent an objection from the committee or the US Trustee) in determining whether a vendor was critical or should be paid. Ultimately, the DIP paid only $6.7 million in critical vendors. Section 363(b) authorizes a trustee to use property of the estate, including to pay prepetition claims, based on sound business judgment. Relying on the DIP's representations that the 10 questions were accurately answered for each payment was appropriate, considering the time and resources that would have been required for the court to hear each one, and was not an improper delegation of decision-making authority, especially in light of the oversight by the committee and the US Trustee. Section 107 requires that all papers filed in the case must be public, unless, among other things, the paper contains confidential commercial information. However, the lists here were not filed with the court, so section 107 did not apply. Even if the lists had been filed, redacting the vendors' names would have been an appropriate protection of confidential commercial information. Therefore, the court approves the procedures and the payments. *GLM DFW, Inc. v. Windstream Holding Inc. (In re Windstream Holdings Inc.)*, 614 B.R. 441 (S.D.N.Y. 2020).

5.1.b **Court dismisses chapter 11 case upon election to proceed under subchapter V.** The small business debtor filed its chapter 11 case in June 2019. After litigation and settlements, it was prepared to proceed with a plan in April 2020, although one of the settlements imposed a large administrative expense claim that would have had to be paid in full at plan confirmation. During that 10-month period, the Small Business Reorganization Act added subchapter V to chapter 11, and the COVID-19 pandemic hit, requiring the debtor to close its business. Shortly after reopening in June 2020, the debtor amended its petition to elect to proceed under subchapter V. Subchapter V requires a status conference within 60 days after the order for relief and that the debtor file a plan within 90 days. The court may extend the deadline based on circumstances for which the debtor should not justly be held accountable. Section 1112(b)(4)(J) requires dismissal of a chapter 11 case if the debtor does not file a plan within the time fixed by the Code. Although Bankruptcy Rule 1009 permits a debtor to amend its petition at any time, thereby permitting it to elect application of subchapter V, the Rule does not waive the statutory deadlines in subchapter V. In this case, the debtor did not meet those deadlines, and the circumstances causing noncompliance were the debtor's own activities in its chapter 11 case and therefore did not support an extension. Because the debtor's election to proceed under subchapter V was effective and the debtor did not meet the deadlines, the court dismisses the case. *In re Seven Stars on the Hudson Corp.*, 618 B.R. 333 (Bankr. S.D. Fla. 2020).

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5.5 Confirmation, Absolute Priority

5.5.a **Court may confirm cramdown plan without enforcing a subordination agreement.** The plan classified senior unsecured claims that benefitted from a subordination agreement in one class and other general unsecured claims in another class. The general class included some claims that also benefitted from the subordination agreement. The plan provided for the same 33.6% recovery for claims in both classes. Without the benefit of subordination, claims in both classes would have recovered 21.9% of their claims, and with full enforcement of the subordination provision as to the senior class and the senior creditor in the general class, the senior class claims would have recovered 34.5%, the senior claim in the general class would have recovered 36.9%, and the general claims would have recovered 21.9%. The general class accepted the plan; the senior class did not. Section 1129(b) permits nonconsensual plan confirmation if, "Notwithstanding section 510(a)," the plan "does not discriminate unfairly" and is fair and equitable with respect to the nonaccepting class. Section 510(a) requires the court to enforce subordination agreements. "Notwithstanding" means "in spite of" or "without obstruction or prevention by." Therefore, section 1129(b) permits nonconsensual plan confirmation despite the non-enforcement of a subordination agreement. The senior creditors' protections are found in the fair and equitable rule and the unfair discrimination provision. Therefore, the failure to enforce the subordination agreement strictly does not prevent plan confirmation. *In re Tribune Co.*, 972 F.3d 228 (3d Cir. 2020).

5.5.b **Third Circuit explains "unfair discrimination."** The plan classified senior unsecured claims that benefitted from a subordination agreement in one class and other general unsecured claims in another class. The general class included some claims that also benefitted from the subordination agreement. The plan provided for the same 33.6% recovery for claims in both classes. Without the benefit of subordination, claims in both classes would have recovered 21.9% of their claims, and with full enforcement of the subordination provision as to the senior class and the senior creditor in the general class, the senior class claims would have recovered 34.5%, the senior claim in the general class would have recovered 36.9%, and the general claims would have recovered 21.9%. The general class accepted the plan; the senior class did not. Section 1129(b) permits nonconsensual plan confirmation if, "Notwithstanding section 510(a)," the plan "does not discriminate unfairly" and is fair and equitable with respect to the nonaccepting class. A plan may discriminate against a nonaccepting class, but not so much as to be unfair from the perspective of the nonaccepting class. Testing for unfairness requires analysis of the net present value of recoveries, based on a full pro rata recovery to all similarly situated creditors. A plan discriminates unfairly if there is a materially lower percentage recovery to the nonaccepting class. In this case, a difference in recovery of 0.9% is not material. The court properly confirmed the plan. *In re Tribune Co.*, 972 F.3d 228 (3d Cir. Aug. 26, 2020).

5.5.c **DIP financing provision that commits debtor to issue plan equity at a discount does not violate absolute priority but is an impermissible *sub rosa* plan.** The debtor in possession arranged multi-tranche DIP financing. Only major shareholders subscribed to tranche C. The tranche C agreement permitted the debtor to repay it in cash or in stock, at a 20% discount to plan value, through a rights offering that would be made available to non-lender shareholders, though not at a discount. The debtor marketed the facility but found no takers on better terms. The absolute priority rule applies to confirmation of a nonconsensual plan but not necessarily at other stages of a case. However, because approval of the DIP agreement would foreclose later challenge to applying the loan terms to a plan, the court considers whether the agreement violates the absolute priority rule. The rule prohibits shareholders from receiving or retaining any property under the plan if creditors receive less than full compensation and have not accepted the plan. Here, the shareholders would be receiving property—reorganized company stock—and are being given the opportunity to participate in the tranche C loan because they are shareholders. Therefore, they are receiving property on account of their existing shares. The new value exception to the absolute priority rule permits receipt of property under the plan on account of money of equivalent value invested in the debtor that is necessary for a successful reorganization. Determining whether the plan distribution is equivalent in value to the new money requires a market test. The marketing of the tranche C loan satisfied that test, so the provision satisfies the new value exception to the absolute priority rule. However, a debtor may not enter into a transaction that would circumvent chapter 11's plan confirmation requirements by dictating some of the plan terms in advance. Because the provision fixes some of the terms of a plan that has not yet been filed, it crosses the line as a *sub rosa* plan and may not be approved. *In re LATAM Airlines Group S.A.*, ___ B.R. ___, 2020 Bankr. LEXIS 2405 (Bankr. S.D.N.Y. Sept. 10, 2020).

5.5.d **Any form of collateral sale disqualifies a section 1111(b) election.** A creditor's claim was secured by specified equipment that was part of a larger business operation. The claim was undersecured. The debtor proposed a plan that provided for a sale of the operation. Because the sale procedures order permitted sales only for the entire operation, the secured creditor was not able to credit bid its claim for its collateral. The winning bid was made by a combination of the debtor's other secured creditors and a newly formed entity that included some of the debtor's equity holders. After the selection of the winning bid, the creditor elected to have its entire claims treated as secured under section 1111(b). Section 1111(b) permits an undersecured creditor to have its entire claim treated as secured, despite section 506(a), unless its collateral is sold under section 363 or under a plan. Section 1111(b) does not limit the kind of sale or plan, such as a sale that looks like an internal reorganization, to which the exception applies. Therefore, the court disqualifies the election. *In re Murray Metallurgical Coal Holdings, LLC*, 618 B.R. 825 (Bankr. S.D. Ohio 2020).

5.5.e **Shareholder's option to purchase stock given to unsecured creditors is subject to absolute priority rule.** The debtor proposed a plan that the general unsecured creditors did not accept. The plan provided that if the creditors did not accept, they would receive 100% of the reorganized debtor's stock, but the stock would be subject to an irrevocable option in the debtor's sole prepetition stockholder to purchase the stock from the creditors. Under the absolute priority rule, the court may not confirm a plan that a class of creditors has not accepted unless it provides for no distribution on account of prepetition equity. The option is consideration to the shareholder and therefore is subject to the absolute priority rule. *In re Green Pharms., Inc.*, 617 B.R. 131 (Bankr. C.D. Cal. 2020).

6. CLAIMS AND PRIORITIES

6.1 Claims

6.1.a **Strict foreclosure under an indenture does not extinguish dissenting bondholders' payment rights.** The debtor issued bonds under an indenture. The debtor's parent guaranteed the notes and secured the guarantee with the debtor's stock under a collateral trust agreement. The indenture provided that the parties to the indenture, including the bondholders, agreed to the collateral trust agreement. Although the indenture was not qualified under the Trust Indenture Act, it incorporated TIA section 316(b) prohibiting modification of any bondholder's right to payment of principal or interest without the bondholder's consent. Both the indenture and the collateral trust agreement authorized a majority of bondholders to direct the indenture trustee in "the time, method, and place of conducting any proceeding for exercising any remedy available to the Trustee." After default, the majority bondholders directed the trustee to conduct a strict foreclosure under sections 9–620 and 9–622 of the UCC (accepting the collateral in satisfaction of the debt). The trustee did so, taking the debtor's stock in the foreclosure and distributing it to all noteholders pro rata. The minority bondholders objected. They sued the debtor to collect the amounts due to them on the bonds. The authority in the indenture for the majority bondholders to direct the exercise of remedies remains constrained by the provision protecting the minority's right to payment. The collateral trust agreement provision that authorizes majority action to direct the exercise of remedies is similarly constrained. Therefore, even though the strict foreclosure purported to result in full satisfaction of the amounts owing under the indenture, it did not extinguish the minority's right to pursue full payment. The court remands for a determination of damages, that is, the amount remaining to be paid on the bonds. *CNH Diversified Opps. Master Acct., L.P. v. Cleveland Unltd., Inc.* ___ N.Y. ___, 2020 N.Y. LEXIS 2514 (Oct. 22, 2020).

6.1.b **Secured creditor has burden of proof on collateral value.** The debtor granted a lender a security interest in general intangibles, including non-tort claims. After a major accident that destroyed the debtor's business and most of a small town and led to the debtor's bankruptcy, the trustee sued for recovery of both tort and non-tort damages. The defendant settled. The creditor claimed a portion of the settlement proceeds were for non-tort claims in which it had a security interest. The trustee and the creditor stipulated that the debtor's non-tort claims were at least $25 million and that the net economic value of the claims, after attorneys' fees and costs, were at least $10 million. Section 506(a)(1) requires the bankruptcy court to determine the value of a secured creditor's collateral. The creditor has the burden of proof on value. "The settlement value of a claim is the amount the claimant would recover if he prevails in litigating the claim multiplied by the probability of recovery," which depends on the strength of the evidence and defenses, the defendant's ability to pay, the cost of litigation, the parties' staying power and their bargaining leverage, among other factors. The "net economic value" of the claim does not address any of those factors and therefore provided insufficient evidence of the value of the claim. *Wheeling & Lake Erie Ry. Co. v. Keach (In re Montreal, Me. & Atl. Ry.)*, 956 F.3d 1 (1st Cir. 2020).

6.1.c **Law firm trust account retainer is free and clear of lenders' security interest.** The lenders lent the debtor money that the debtor used to lend to borrowers, who gave the debtor notes for the loans. The debtor granted the lenders a security interest in current and after-acquired cash, cash investments, general intangibles, accounts, chattel paper, instruments, contracts, contract rights, and all other tangible and intangible property of Borrower. The lenders filed a UCC-1, listing, among other things, contract rights or rights to payment of money, General Intangibles, documents, instruments (including any promissory notes), chattel paper, cash, receivables, deposit accounts, and financial assets. The borrowers' repayments went to the debtor's bank account. The debtor withdrew funds from the bank account to pay his lawyer. The lawyer placed the funds in a client trust account and withdrew from the account as the lawyer incurred fees. The borrower notes are instruments, as defined by UCC § 9-102(a)(47), in which the lenders had a perfected security interest. The borrowers' payments on the notes were deposited in a bank account, which is a deposit account under UCC § 9-102(a)(29). The debtor did not grant a security interest in deposit accounts, but the lenders had a security interest in the deposit accounts as proceeds of the notes, under UCC § 9-315(a). The wire transfers from the deposit account to the law firm trust accounts was a transfer of identifiable cash proceeds, in which the lenders still retained a perfected security interest under UCC 9-315(d)(2). The money in the law firm's trust accounts still belong to the debtor but can be accessed only by the law firm, so the debtor's asset is a general intangible but is still identifiable proceeds of the borrowers' notes. The lenders retained a perfected interest in the general intangible, because of the granting clause in the security agreement and UCC 9-315(d)(3). Under UCC 9-322(b), a transferee of collateral in the ordinary course of business takes free of the security interest in a deposit account unless the transferee acted in collusion with the debtor in violating the secured party's rights. Here, the debtor's transfer of the funds from its deposit account to the trust account (a general intangible) was a transfer for purposes of section 9-322. The law firm had a possessory security interest in the trust account which, absent collusion, had priority over the lenders because of section 9-322. *Walters v. Lynch (In re 3P4PL, LLC)*, ___ B.R. ___, 2020 Bankr. LEXIS 2092 (Bankr. D. Colo. June 22, 2020).

6.1.d **Court disallows surety's claim under a surety bond.** Before bankruptcy, the debtor obtained surety bonds to secure performance obligations under various agreements. If the debtor defaulted under any of the agreements and the surety were required to pay the counterparty, the debtor agreed to indemnify the surety. At the petition date, the debtor had not defaulted under the agreements. The surety filed a proof of claim for a contingent unliquidated amount. Section 502(e)(1)(B) disallows "any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that … such claim …is contingent as of the time of allowance of disallowance of such claim." The provision prevents the co-obligor from competing with the principal creditor for the debtor's scarce assets. Because the surety was liable with the debtor to the counterparties and as of the time of allowance, the debtor had not yet defaulted, the surety's reimbursement claim was contingent, the court disallows the claim. *In re Falcon V, L.L.C.*, ___ B.R. ___, 2020 Bankr. LEXIS 2490 (M.D. La. Sept. 22, 2020).

6.2 Priorities

7. CRIMES

8. DISCHARGE

8.1 General

8.2 Third-Party Releases

8.3 Environmental and Mass Tort Liabilities

9. EXECUTORY CONTRACTS

9.1.a **Lehman flip clauses are safe harbored and enforceable.** The debtor entered into several transactions involving a credit default swap between the debtor and synthetic collateralized debt obligation SPVs (issuers), which issued notes under an indenture. The notes' proceeds were held as collateral for the issuers' obligations under both the notes and the swaps. The swaps provided that payments under were subject to the priority provisions of the indentures. The indentures contained a waterfall specifying which party would receive collateral proceeds based on the event that triggered the collateral liquidation and distribution. Because the debtor defaulted by its bankruptcy, the priority favored the noteholders, whereas it would have favored the debtor if the noteholders had defaulted. After the debtor filed bankruptcy, indenture trustees for some of the note issues sent a notice of default and termination under the swaps. After termination, the indenture trustees liquidated the collateral and distributed the proceeds to the noteholders. An executory contract is a contract under which the obligations of the debtor and the counterparty are so far unperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other. The swaps' outstanding payment obligations make them executory contracts. Section 365(e) prohibits the enforcement after the commencement of the debtor's case of a contractual provision that modifies or terminates a debtor's rights under an executory contract based on "the commencement of a case under this title." However, section 560 exempts swap agreements from the prohibition of section 365(e) and permits "termination, liquidation, or acceleration" of a swap agreement. A swap agreement includes terms and conditions incorporated by reference. Because the swap incorporated the indenture's priority provisions by reference, they were protected by the section 560 safe harbor. "Liquidation" is not limited to determining the amount of the claims under the swap (liquidating the claim amount), but rather includes liquidating any collateral and distributing proceeds. Otherwise, the safe harbor would be of little benefit to swap counterparties. *Lehman Bros. Special Financing Inc. v. Branch Banking & Tr. Co. (In re Lehman Bros. Holdings Inc.)*, 970 F.3d 91 (2d Cir. 2020).

9.1.b **Surety bond is not an executory contract.** Before bankruptcy, the debtor obtained surety bonds to secure performance obligations under various agreements. At the petition date, the debtor had not defaulted under the agreements. The surety filed a proof of claim for a contingent unliquidated amount. The plan did not list the surety bond agreements as rejected but provided that all executory contracts that were not rejected were assumed. After the plan effective date, the reorganized debtor missed payments on some of the bonds. The surety demanded additional collateral. The debtor refused. An executory contract is one for which performance remains due to some extent on both sides and if at the petition date, the failure of either party to complete performance would constitute a material breach excusing the other party's performance. A surety bond is a tripartite agreement among the debtor, the surety, and the debtor's contract counterparty. The surety agrees to pay the counterparty if the debtor defaults but owes no further performance to the debtor. Therefore, the surety bond is not an executory contract. *In re Falcon V, L.L.C.*, ___ B.R. ___, 2020 Bankr. LEXIS 2490 (M.D. La. Sept. 22, 2020).

10. INDIVIDUAL DEBTORS

10.1 Chapter 13

10.2 Dischargeability

10.3 Exemptions

10.4 Reaffirmations and Redemption

11. JURISDICTION AND POWERS OF THE COURT

11.1 Jurisdiction

11.1.a **Bankruptcy court has exclusive jurisdiction to determine what constitutes property of the estate.** Long after a bankruptcy case concluded, some creditors sued the debtor and others in state court, alleging that the debtor had hidden assets from the bankruptcy trustee and had transferred his assets to the other defendants. Under section 554, property of the estate remains property of the estate unless abandoned or otherwise administered. Undisclosed property is not automatically abandoned under section 554. Under sections 544, 548, and 550, the trustee may avoid and recover fraudulently transferred property. Whether the creditors had standing to bring the state court action depended on whether the property they sought to recover was property of the estate. Section 1334(e)(1) of title 28 gives the district court (and, by reference, the bankruptcy court) exclusive jurisdiction over all property of the debtor as of the commencement of the case and of the estate. Therefore, the bankruptcy court had exclusive jurisdiction to determine whether the undisclosed assets and the fraudulent transfer claims the creditors asserted were property of the estate and could not leave to the state court the determination of the creditors' standing. *Hafen v. Adams (In re Hafen)*, 616 B.R. 570 (10th Cir. B.A.P. 2020).

11.1.b **Court has related to, but not arising in, jurisdiction to enjoin actions against nondebtor.** The debtor pharmaceutical manufacturer was accused by numerous individuals and governmental units of causing the opioid epidemic in the United States and was a defendant in over 2500 actions around the country, for which attorneys' fees were running about $100 million per year. The debtor's owner and former CEO was named as a defendant in most of those actions. The debtor had negotiated a tentative but somewhat incomplete deal, which included a material contribution from the former CEO, with a steering committee of plaintiffs and was continuing to work toward a final agreement. The debtor filed a chapter 11 petition to focus the negotiations and develop a chapter 11 plan based on the tentative agreement. It sought an injunction against continued prosecution of the actions against the former CEO, who had not filed a bankruptcy case. Section 105(a) allows a bankruptcy court to enjoin actions against nondebtors where the injunction would play an important part in the reorganization or the action to be enjoined would have an immediate adverse economic consequence for the estate. A bankruptcy court has "related to" jurisdiction over any proceeding whose outcome could conceivably affect the estate, including altering rights, liabilities, options, or freedom of action or affecting the administration of the estate. The proceeding need not involve claims that are derivative of the debtor's rights or liabilities, as long as there is a strong interconnection between the third-party action and the bankruptcy case. Thus, the bankruptcy court has jurisdiction over any action against a debtor and an accused co-tortfeasor. The actions against the former CEO is subject to "related to" jurisdiction because a finding of liability is likely to affect the debtor's defenses and because the former CEO likely had indemnification and contribution claims against the debtor for any liability, which would be allowable in the bankruptcy case. However, the bankruptcy court does not have "arising in" jurisdiction, which cannot be based on a "boot-strap" argument arising from the court's exercise of its discretion under section 105(a). Here, the actions met the standard for an injunction: there was a reasonable likelihood of a successful reorganization, the actions would cause imminent irreparable harm to the estate, the balance of harms favor the debtor and its reorganization, and the public interest supports the injunction. Accordingly, the court enjoins the litigation. *Dunaway v. Purdue Pharmaceuticals L.P. (In re Purdue Pharmaceuticals L.P.)*, ___ B.R. ___, 2020 U.S. Dis. LEXIS 143799 (S.D.N.Y. Aug. 11, 2020).

11.2 Sanctions

11.3 Appeals

11.4 Sovereign Immunity

11.4.a **Trustee may sue to recover fraudulent transfer tax payments to the United States.** More than two years before bankruptcy, the debtor paid its two shareholders' federal tax obligations. Relying on the rights of a creditor with an allowable claim, the trustee sued the United States under section 544(b) to avoid and recover the payments. Section 544(b) permits the trustee to avoid any transfer that would be avoidable by a creditor holding an allowable claim. Any such action is subject to any defenses the transferee would have in an action by that creditor, including a sovereign immunity defense. Section 106(a) abrogates the sovereign immunity of the United States with respect to specified Code sections, including section 544. Because the provision contains no exceptions, limitations, or conditions, it abrogates sovereign immunity for purposes of the trustee's pursuit of the creditor's claim. The Internal Revenue Code is a comprehensive federal statute that preempts state law covering the same field. However, an action to recover a tax payment that is a fraudulent transfer is not an action to collect a tax and is therefore not preempted. *Miller v. U.S. (In re All Resorts Grp., Inc.)*, 617 B.R. 375 (Bankr. D. Utah 2020).

12. PROPERTY OF THE ESTATE

12.1 Property of the Estate

12.1.a **Trustee may abandon estate causes of action to a creditor.** Before bankruptcy, the debtor conspired with its law firm and a creditor to transfer assets so that a major creditor could not reach them. The major creditor sued all three. The major creditor sued the law firm and the other creditor to avoid and recover fraudulent transfers and for damages for breach of fiduciary duty and aiding and abetting breach of fiduciary duty and the fraudulent transfers. Two months later, the debtor filed a chapter 7 case. The trustee settled with the two creditors, releasing the estate's claims against the first creditor and agreeing not to interfere with the major creditor's claims against the first creditor or others. The trustee abandoned other claims of the kind that the major creditor brought. Constitutional standing requires injury in fact fairly traceable to the defendant's conduct that a favorable decision would likely redress. It differs from statutory authority to pursue a claim, which is not constitutional standing but relates only to which entity a statute authorizes to assert a claim. Here, the major creditor had constitutional standing to bring the claims, but the bankruptcy deprived it of authority to bring them, vesting them in the estate, because they assert a generalized injury to all creditors, not a personal, particularized injury just to the major creditor. The trustee may abandon estate causes of action, causing them to revert back to the prior holder. Since the major creditor owned the claims before bankruptcy, the trustee's abandonment of the claims revested them in that creditor, who then had statutory authority to continue to assert them. *Artesanias Hacienda Real S.A. de C.V. v. N. Mill Cap., LLC (In re Wilton Armetale, Inc.)*, 968 F.3d 273 (3d Cir. 2020).

12.1.b **Pennsylvania gaming license is not property of the debtor under PUFTA.** The state granted the debtor a gaming license, for which the debtor paid $50 million. A few years later, the state revoked the license when the debtor did not meet certain maintenance requirements. After the debtor filed a bankruptcy case, the trustee sued the state to recover for the revocation as a fraudulent transfer. The Pennsylvania Gaming Act provides that a gaming license is "a privilege, conditioned upon the proper and continued qualification of the licensee," bars the transfer of the license, and prevents the formation of a property interest by precluding any entitlement to a license. The Pennsylvania UFTA permits a creditor to avoid a transfer of an interest of the debtor in property. It defines property as anything that may be the subject of ownership, including the right to possess a thing. However, because the license is a revocable, conditional, and nontransferable privilege, it cannot be subject to ownership and therefore is not an interest of the debtor in property. Therefore, the trustee could not avoid the revocation of the license as a fraudulent transfer. *Phila. Entertainment and Devel. P'ners v. Commonwealth (In re Phila. Entertainment and Devel. P'ners)*, ___ B.R. ___, 2020 U.S. Dist. LEXIS 180199 (E.D. Pa. September 30, 2020).

12.2 Turnover

12.3 Sales

13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

13.1 Trustees

13.1.a **Language of liquidation trust determines whether dissolution is self-executing.** The chapter 11 plan created a liquidating trust, which provided "the Trust shall be dissolved" upon the occurrence of certain events and "shall be dissolved" no later than three years after the plan effective date unless upon a party in interest's request within three months before the third anniversary, the court determined to extend the trust. None of those events had occurred. The trustee failed to seek an extension within the three-month period, but sought an extension about six months later. The terms of the trust govern its dissolution. The language, "the Trust shall be dissolved," is not self-executing; it requires an action by the trustee or perhaps a party in interest or the court to effect the dissolution. Therefore, although the court refuses to grant the trustee's motion to extend the trust because the motion was untimely, the trust is not dissolved. *In re Black Elk Energy Offshore Operations, LLC*, ___ B.R. ___, 2020 Bankr. LEXIS 2248 (Bankr. S.D. Tex. Aug. 21, 2020).

13.1.b ***Barton* doctrine does not apply after bankruptcy court jurisdiction over the case ceases.** Debtor in possession counsel misrepresented that the bankruptcy court had approved special counsel's employment. It had not. At the conclusion of the case, the court denied special counsel's fees and ordered disgorgement. After the court dismissed the case, special counsel sued DIP counsel in district court for intentional and negligent misrepresentation. The parties agreed that the action would have no conceivable effect on the estate. The *Barton* doctrine requires that before suing a fiduciary for the estate, the plaintiff must obtain leave of the bankruptcy court so as not to usurp the bankruptcy court's control over the estate and its fiduciaries. DIP counsel is such a fiduciary. But when the bankruptcy court no longer has jurisdiction over a matter, *Barton* does not apply, because there are no powers or duties belonging to the bankruptcy court that the other court might usurp. Here, because the action would not have any conceivable effect on the estate, the bankruptcy court did not have even related-to jurisdiction. Therefore, *Barton* did not apply, and leave of court was not required. *Tufts v. Hay*, ___ F.3d ___, 2020 U.S. App. LEXIS 33061 (11th Cir. Oct. 20, 2020).

13.2 Attorneys

13.2.a **Sanction for nondisclosure of fees under section 329 should ordinarily be complete denial of fees.** An attorney for a chapter 7 debtor also represented its affiliates. He prevailed in litigation for the debtor and the affiliates and received a significant contingent fee from the litigation. He did not disclose the fee agreement or the fee at the outset of the case nor when he received the fee. He disclosed them only after the court ordered disclosure following a hearing on approval of a related settlement, in which the litigation results and fees came up. Section 329(a) and Bankruptcy Rule 2016 require an attorney representing a debtor to disclose any compensation or agreement for compensation in or in connection with the case, including any fee sharing agreement. The attorney's disclosure duty is that of a fiduciary, and violations are intolerable, warranting harsh sanctions going beyond compensation for the damage done. Accordingly, absent specific, sound mitigating factors, the sanctions should be total denial of fees. The appellate court remands for the bankruptcy court to determine whether any such factors apply. *SE Prop. Holdings, LLC v. Stewart (In re Stewart)*, 970 F.3d 1255 (10th Cir. 2020).

13.2.b **Prohibition on nunc pro tunc orders does not prevent retroactive approval of employment.** The debtor forgot to schedule a mass tort claim in her filing. Several years after the closing of her no-asset case, the tort claim settled. The court reopened the case and reappointed the trustee, who later sought approval to employ the debtor's tort counsel and pay its contingent fee. Under *Roman Catholic Archdiocese v. Acevedo Feliciano*, 140 S. Ct. 22 696 (2020), the court may not issue a nunc pro tunc order except to correct the record to reflect a fact that existed at the prior date. However, *Acevedo* does not prohibit retroactive relief in appropriate circumstances. It limits the court's authority to issue orders that purport to rewrite history, not a discretionary grant of retroactive relief for something that does not by its terms require prior approval. The circumstances of this case warrant such relief, including approval of the employment and approval of the contingent fee for work performed since the beginning of the debtor's bankruptcy case. *In re Miller*, ___ B.R. ___, 2020 Bankr. LEXIS 2856 (Bankr. E.D. Cal. Oct. 13, 2020).

13.3 Committees

13.4 Other Professionals

13.4.a **A non-creditor party in interest is not entitled to a "substantial contribution" claim under section 503(b)(3).** The debtor in possession settled with an adverse claimant. The county objected on the ground the settlement violated county ordinances; the court ordered mediation of the objection; and the parties reached a revised settlement agreement. The county did not have a claim but sought reimbursement of fees and expenses under section 503(b)(3)(D) for making a substantial contribution to the case. Section 503(b)(3)(D) permits reimbursement of expenses of a creditor, indenture trustee, equity security holder, or ad hoc committee for making a substantial contribution. The provision does not extend to parties in interest generally, only to the listed entities. Accordingly, the county did not have standing to seek reimbursement. *In re Mt. Creek Resort, Inc.*, 616 B.R. 45 (Bankr. D.N.J. 2020).

13.5 United States Trustee

14. TAXES

14.1.a **Erroneous postpetition refund claim and tax on prepetition straddle-year income are not entitled to administrative expense priority.** About two weeks after its return was due, the debtor paid the IRS $15.8 million to apply to its anticipated income tax liability. Two weeks later, it filed bankruptcy. During the case, the trustee filed the debtor's tax return for the year before the petition date. The IRS issued a $15.5 million refund to the trustee. The IRS later disallowed deductions claimed on the return and filed an administrative expense claim to recapture the refund amount. The trustee also filed a return for the year in which the petition date occurred. All the debtor's income in that year was accrued before the petition date. The IRS filed an administrative claim for the taxes owing for that year as well. Section 503(b)(1) grants administrative expense priority to any tax "incurred by the estate," except a tax entitled to priority under section 507(a)(8). Section 507(a)(8) grants priority to "a tax on or measured by income … for a taxable year ending on or before" the petition date. Section 507(c) provides a governmental unit's claim "arising from an erroneous refund or credit of a tax has the same priority as a claim for the tax to which such refund or credit relates." This provision is not limited to erroneous prepetition refunds. Therefore, the claim for the erroneous refund is entitled only to prepetition priority under section 507(a)(8). Federal income taxes are incurred when they accrue, not when payment is due. The debtor's income for the straddle year occurred, and therefore the tax on it was incurred prepetition, and therefore is entitled only to prepetition priority under section 507(a)(8). *Darr v. U.S. (In re TelexFree)*, 615 B.R. 362 (Bankr. D. Mass. 2020).

15. CHAPTER 15—CROSS-BORDER INSOLVENCIES