JENNER&BLOCK

Recent Developments in Bankruptcy Law, July 2019

(Covering cases reported through 600 B.R.471 and 922 F.3d 1320)

RICHARD LEVIN
Partner
+1 (212) 891-1601
rlevin@jenner.com

TABLE OF CONTENTS

1. AUTOMATIC STAY

1.1 Covered Activities

1.1.a **Automatic stay requires city to return impounded car to debtor.** After the debtor incurred multiple parking and traffic fines, the city impounded the debtor's car. A city ordinance gave the city a possessory lien on the car to secure payment of the fines. The debtor filed a chapter 13 case with a plan to repay the city over time and demanded the city return the car immediately. The automatic stay prohibits any act to exercise control over property of the estate. The debtor has an interest in the car, which becomes property of the estate. Retaining possession exercises control. A creditor is entitled to adequate protection of an interest in property of the estate. The city's possessory lien is such an interest. The creditor has the burden of seeking adequate protection. Requiring the debtor to provide adequate protection before obtaining return of the car would improperly shift that burden to the debtor. An automatic stay exception permits a creditor to take certain actions to perfect a lien. The exception does not apply to possessory liens, which remain perfected despite turnover required by court order or, in this case, the automatic stay, which functions like a court order. Therefore, the automatic stay requires the city to return the car to the debtor. *In re Fulton*, ___ F. 3d ___, 2019 U.S. App. LEXIS 18393 (7th Cir. June 19, 2019).

1.1.b **Automatic stay does not apply to removal to the home bankruptcy court.** Before bankruptcy, the debtor was sued in a class action in state court. After it filed its chapter 7 petition, the debtor removed the class action to the bankruptcy court. Section 1452(a) of title 28 permits a party to a nonbankruptcy action to remove the action to the bankruptcy court if the bankruptcy court has jurisdiction. Section 362(a) stays all actions against the debtor that were or could have been commenced before bankruptcy. The stay's purpose, among others, is to give the debtor a breathing spell and to centralize the administration of all claims against the debtor. A court must interpret a statute so as not to prevent a result that is absurd or demonstrably at odds with the drafters' intentions. If read literally, the automatic stay would enjoin any action against the debtor in the home bankruptcy court, including filing a proof of claim, objecting to an exemption or to discharge or dischargeability, or even to a request for stay relief. Such a literal reading would be absurd and demonstrably at odds with the drafters' intentions. The same applies to removal of nonbankruptcy litigation against the debtor that is removed to the home bankruptcy court. Therefore, the removal does not violate the automatic stay. *In re Cashco, Inc.* 598 B.R. 9 (Bankr. D.N.M. 2019).

1.2 Effect of Stay

1.3 Remedies

2. AVOIDING POWERS

2.1 Fraudulent Transfers

2.1.a **The financial contracts safe harbor protects a transaction with a financial institution's "customer."** The debtor engaged a bank to act as depository and as exchange agent for the purchase of its shares in an LBO. When the debtor later failed and filed bankruptcy, the court authorized the creditors' committee to pursue fraudulent transfer claims against the selling shareholders under section 548(a)(1)(B) (intentional fraudulent transfers). Upon the Supreme Court's decision in *Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 138 S. Ct. 883 (2018), reversing previously controlling precedent based on the section 546(e) financial contracts safe harbor that prevented the committee from pursuing claims under section 548(a)(1)(B) (constructive fraudulent transfer), the committee sought leave to amend its complaint to add claims under the latter section. The court may not permit an amendment that would be futile. If the safe harbor still applied, the amendment would be futile. The safe harbor shields transfers made "by a financial institution." A "financial institution" is "an entity that is a commercial or savings bank, … and, when any such … entity is acting as agent or custodian for a customer (whether or not a 'customer', as defined in section 741) in connection with a securities contract … such customer." Because the definition excludes the "customer" definition in section 741, the court must give "customer" its ordinary meaning. The debtor purchased services from the bank and therefore was the bank's customer. The services were in connection with the purchase of the debtor's shares under a contract to purchase the shares. Therefore, the debtor falls within the definition of "financial institution." The transfer to the selling shareholders was by the debtor as a financial institution in connection with a securities contract and therefore is protected by section 546(e). *In re Tribune Fraudulent Conveyance Litigation*, ___ B.R. ___, 2019 U.S. Dist. LEXIS 69081 (S.D.N.Y. Apr. 23, 2019).

2.2 Preferences

2.2.a **Creation of a joint check agreement among a contractor, the debtor, and the debtor's subcontractor is a transfer of an interest of the debtor in property.** The debtor subcontractor further subcontracted some of its work. Within 90 days before bankruptcy, when the debtor had encountered financial difficulty, the subsubcontractor entered into a joint check agreement among the contractor, the debtor, and the subsubcontractor. Under the agreement, the contractor issued a joint check payable to the debtor and the subsubcontractor for material the subsubcontractor agreed to release to the contractor. The debtor endorsed the check and returned it to the contractor, who forwarded it to the subsubcontractor. The trustee may avoid as a preference a transfer of a debtor's property to or for the benefit of a creditor made within 90 days before the petition date, if certain other conditions are also met. Under a joint check agreement, the debtor is deemed to hold the funds represented by the check in trust for the other payee, so the funds are not property of the debtor. The joint check agreement created the subsubcontractor's interest in the funds otherwise owing to the debtor within the 90-day preference period, resulting in a transfer of an interest of the debtor in property. Therefore, the trustee may avoid the transfer. *Myers Controlled Power, LLC v. Gold (In re the Truland Group, Inc.)*, 2019 U.S. Dist. LEXIS 88127 (E.D. Va. May 24, 2019).

2.3 Postpetition Transfers

2.4 Setoff

2.5 Statutory Liens

2.6 Strong-arm Power

2.7 Recovery

3. BANKRUPTCY RULES

3.1.a **Court denies Rule 2004 examination request by a plaintiff in a nonbankruptcy court action.** A plaintiff in state court litigation against a third party purchased a $650 claim against the chapter 7 debtor and promptly sought production under Rule 2004 of documents from the estate, which would be used in the nonbankruptcy litigation. Rule 2004 is not available once litigation has commenced, even litigation in a nonbankruptcy court. Granting the request might incentivize parties to purchase small claims solely to pursue outside litigation having no relation to the estate and could impose unnecessary costs and expenses on an estate. The court denies the request. *In re Cambridge Analytica LLC*, 600 B.R. 750 (Bankr. S.D.N.Y. 2019).

4. CASE COMMENCEMENT AND ELIGIBILITY

4.1 Eligibility

4.1.a Pension trust is not a "business trust." A nonprofit organization that operated numerous schools established a pension plan for the schools' employees and a pension trust to hold the funds that would be paid as pensions. The plan required each school to contribute to the trust. The trust's sole function was to invest the contributions and pay pensions as employees retired. Declining enrollments led the organization to terminate the pension plan, and the trust soon thereafter stopped paying pensions, though the trust itself was never terminated. Numerous retirees sued the trust for their pensions, but the trust was unable to pay. It filed a chapter 11 petition. Only a "person" is eligible for chapter 11 relief. A corporation is a person; "corporation" includes a business trust. Although the case law on what constitutes a business trust is not completely coherent, generally the courts find a trust is a business trust if it was created for the purpose of transacting business and if the trust has the indicia of a corporate entity, such as the presence of investors expecting a profit from operations and transferability of ownership interests. The court should determine whether a trust meets those criteria as of the petition date. The petitioner has the burden of proof. In this case, the trust lacked the attributes of a corporation—there were no investors who expected to earn a return on their investments, and the retirees do not hold transferable interests in the trust, only in pensions, which the trust prohibits them from transferring. The pension trust was more like a traditional trust formed to effect, preserve, and protect a gift or contribution for the beneficiaries. The court dismisses the case. *In re Catholic School Employees Pension Trust*, 599 B.R. 634 (1st Cir. B.A.P. 2019).

4.2 Involuntary Petitions

4.2.a **Court may not excuse the requirement of three petitioning creditors on equitable grounds.** Two creditors filed an involuntary petition against the debtor. The debtor filed a response showing he had more than 12 creditors. The petitioning creditors disputed the response and claimed the debtor had defrauded his creditors. The bankruptcy court found the debtor had more than 12 creditors as of the petition date. Section 303(b) permits fewer than three creditors to file an involuntary petition only if the debtor has fewer than 12 creditors. Section 105(a), which grants the court authority to issue any order necessary to carry out the provisions of the Bankruptcy Code, does not authorize the court to override specific statutory provisions on equitable grounds. Therefore, the court may not excuse the three-creditor requirement based on the debtor's alleged fraud in dealing with his creditors. *Popular Auto, Inc. v. Reyes-Colon (In re Reyes-Colon)*, 922 F.3d 13 (1st Cir. 2019).

4.2.b **Only the debtor may seek fees and costs under section 303(i).** One of the debtor's two 50% shareholders opposed an involuntary petition. Because of the deadlocked board, the debtor did not oppose the petition or appear. The court dismissed the petition. The shareholder sought fees and costs for the debtor under section 303(i), which permits the court to award fees and costs "in favor of the debtor." This phrase limits standing to seek fees and costs to the debtor and does not permit any other entity to seek damages, even on the debtor's behalf. *Vibe Micro, Inc. v. SIG Cap., LLC (In re 8Speed8, Inc.)*, 921 F.3d 1193 (9th Cir. 2019).

4.3 Dismissal

5. CHAPTER 11

5.1 Officers and Administration

5.1.a **Revolver payments are disbursements for U.S. Trustee fee purposes.** The debtor had a revolving line of credit with a bank. In its chapter 11 case, the bank increased the borrowing limit for the debtor in possession and required a roll-over, which the bankruptcy court approved. Under the roll-over, the debtor's customers sent payments to the bank, who credited the debtor's prepetition loan and then re-advanced the same amount to the DIP as a postpetition loan. The total indebtedness remained the same, but it was converted from prepetition to administrative expense. 28 U.S.C. 1930(a)(6) requires a trustee or debtor in possession to pay U.S. Trustee fees as a percentage of "disbursements." "Disbursements is a broad term, encompassing any money paid out. Because customer payments were the debtor's receivables, paying them to the bank constituted a disbursement. The bank's re-advance of the funds to the estate did not make them less so. Therefore, the U.S. Trustee fee calculation includes the customer payments that reduced the bank's claim. *In re Cranberry Growers Coop.*, ___ F.3d ___, 2019 U.S. App. LEXIS 21121 (7th Cir. July 17, 2019).

5.1.b **U.S. Trustee fee increase is unconstitutional as non-uniform.** The debtor confirmed a plan in 2010. The plan provided for payment of U.S. Trustee fees under 28 U.S.C. 1930(a) until the case was closed. Congress increased U.S. Trustee fees substantially, effective January 1, 2018. The increase did not apply to the six judicial districts in Alabama and North Carolina that do not have U.S. Trustees, but the Judicial Conference provided for the increase in those districts effective October 1, 2018, but only for cases filed on or after that date. The U.S. Trustee fee is like a tax. As such, it applies in pending cases, regardless of when they were filed or when a plan was confirmed. The Constitution requires that taxes and bankruptcy law be uniform geographically. The U.S. Trustee fee is not uniform as to cases filed before October 1, 2018, because different rates apply in the six non-U.S. Trustee districts. Therefore, it may not be charged in this cases. *In re Circuit City Stores, Inc.* ___ B.R. ___, 2019 Bankr. LEXIS 2121 (Bankr. E.D. Va. July 15, 2019).

5.1.c **Court denies request for waiver of section 345 bonding requirement.** The debtors in possession operated a complex mortgage origination and servicing business with hundreds of bank accounts and average daily balances of nearly $100 million. Section 345 requires a depository institution that holds estate funds to post a bond in favor of the United States to ensure proper accounting for all funds or to deposit securities with a federal reserve ban to collateralize the deposit obligations, unless the court orders otherwise. In this case, the bank had refused to deposit securities to collateralize the account unless the DIP offset the $80,000 per month cost. Section 345 is designed to ensure moneys of estates will be available for distribution to creditors or for reorganization. A court should permit a waiver of its requirements based on the totality of the circumstances, including the size and sophistication of the business and the complexity of the case, the soundness of the depository and the risk to the estate, and the potential effect on the reorganization if a depository failed. In this case, although the DIP's circumstances might have warranted a waiver, the depository's willingness to collateralize the account, albeit at a cost to the estate, undercut the need for a waiver, which the court denied. *In re Ditech Holding Corp.*, ___ B.R. ___, 2019 Bankr. LEXIS 1892 (Bankr. S.D.N.Y. June 24, 2019).

5.2 Exclusivity

5.3 Classification

5.4 Disclosure Statement and Voting

5.5 Confirmation, Absolute Priority

5.5.a **Section 1129(a)(3) applies only to the means by which the plan is proposed, not the plan's substantive provisions.** The debtor leased property to a marijuana establishment, which operated in compliance with state law but not federal law. The debtor proposed a plan that paid all creditors in full. The plan contemplated retention of the lease and the use of rent paid under the lease as part of the plan. The U.S. trustee objected to confirmation on the ground that the property's use violated federal law. Section 1129(a)(3) requires as a condition to confirmation that the plan "be proposed in good faith and not by any means forbidden by law." By its express terms, the provision addresses only the means by which the plan is proposed, not the substantive terms of the plan or of the debtor's postconfirmation activities. Therefore, the court overrules the objection. *Garvin v. Cook Invs. NY, SPNWY, LLC*, 922 F.3d 2013 (9th Cir. 2019).

6. CLAIMS AND PRIORITIES

6.1 Claims

6.1.a **Court allows default interest rate as liquidated damages.** The debtor's loan agreement provided a default interest rate of 5% over the nondefault rate. The debtor and the bank did not negotiate over the default rate, and the bank made no effort when it issued the loan to determine what its damages, such as administrative or funding costs or loss in the loan's value, might be if the debtor defaulted or whether the default interest rate bore any relation at all to anticipated damages resulting from a default. After bankruptcy, the debtor in possession objected to the allowance of default interest as an unenforceable penalty rather than liquidated damages arising from the debtor's breach of the loan agreement. Applicable nonbankruptcy law renders a liquidated damages provision unenforceable unless the provision was unreasonable under the circumstances existing when the contract was made. It does not require that the parties actually have negotiated the amount. The issue is a question of law. Courts have regularly treated a default interest rate as permissible and not as an unenforceable penalty. Moreover, in addition to the administrative costs and increased risk to the lender, the value of a loan to the lender decreases after default. A higher interest rate can compensate the lender for that loss. Therefore, the court allows the default interest rate. *East West Bank v. Altadena Lincoln Crossing, LLC*, 598 B.R. 633 (C.D. Cal. 2019).

6.1.b **Section 502(b)(7) caps earned but unmatured compensation.** The debtor's employee's employment contract provided for a bonus, payable over five years. The contract also provided for a severance payment and the acceleration of any unpaid portion of the bonus if the debtor terminated the employment without cause. The employee earned the bonus before the debtor terminated his employment without cause, but the debtor had paid only a portion. The debtor later filed a chapter 11 petition. The employee sought damages for termination of the employment contract plus interest. Section 502(b)(7) limits an employee's claim for damages resulting from termination of an employment contract to "the compensation provided by such contract, without acceleration, for one year following" termination plus "any unpaid compensation due under such contract, without acceleration," on such date. Although the employee had fully earned the bonus before termination, because the contract extended the payments over time but accelerated them upon termination without cause, section 502(b)(7) limits the employee's allowable claim to the amount provided under the contract for the one year following termination. Section 502(b)(7) similarly limits prepetition interest on the claim. Prepetition interest on the claim's capped portion is limited by the cap; prepetition interest on the uncapped portion, that is, the amount that was already owing on the termination date, is not. *In re 21st Century Oncology Holdings, Inc.*, 597 B.R. 217 (Bankr. S.D.N.Y. 2019).

6.1.c **Surety's claim is superior to accounts receivable security interest.** The debtor filed a bankruptcy petition before it completed work on a construction project. The debtor's surety completed the project, and the project owner paid the retainage due under the contract into court. The debtor's lender, who claimed a security interest in the debtor's receivables, and the surety each claimed the payment. The right to a retainage under a contract belongs to the party who completes the contract. As a result, the retainage belonged to the surety and never became property of the estate that was subject to the lender security interest. In addition, a surety's right to payment is based on equitable principles, not on the U.C.C. Therefore, the surety is entitled to the payment. *Kappa Devel. & Gen. Contracting Inc. v. Hanover Ins. Co. (In re Kappa Devel. & Gen. Contracting Inc.)*, ___ B.R. ___, 2019 Bankr. LEXIS 2002 (Bankr. S.D. Miss. July 2, 2019).

6.1.d **Sections 552(b) and 928 do not protect a security interest in the right to receive post-petition revenues that are not fixed prepetition.** The municipal debtor served as a fund to which employers within the government made contributions to fund employees' retirements and from which employee pensions were paid. The amount of payments to the fund were based on a combination of a percentage of the employer's payroll, the then-current number of an employer's retirees, and an actuarial calculation based on the pension funding needs of the debtor and each employer's proportion of employees and contributions. An employer's contribution amount each year could be determined only when the payments were due, based on then-current statistics. The debtor had issued bonds secured by, among other things, employer contributions and the right to receive employer contributions. Section 552 terminates a security interest in property the debtor acquires after the commencement of the case, except property that is the proceeds of prepetition collateral. Because the debtor's right to receive the payment is not fixed and is based on postpetition workforce demographics and postpetition calculations, the right to receive the payments does not exist as of the commencement of the case, the debtor had no right to collect the postpetition payments as of the commencement of the case, and therefore the postpetition payments are not proceeds of prepetition collateral. Section 928(a) excepts "special revenues" from section 552's effect. "Special revenues" include "(A) receipts derived from the ownership, operation, or disposition of projects or systems … that are primarily used … to provide transportation, utility or other services," and "(D) other revenues or receipts derived from particular functions of the debtor." Clause (A) applies only to receipts from physical systems that provide services to third parties. Clause (D) applies only to receipts from providing the "particular function;" it does not cover a debtor's receipts that are not compensation for the function, such as for services. Therefore, the debtor's revenues are not "special revenues." *Fin. Oversight and Mgmt. Bd. v. Andalusian Global Designated Activity Co. (In re Fin. Oversight and Mgmt. Bd.)*, ___ B.R. ___, case no. 3:17-213 (D.P.R. June 27, 2019).

6.2 Priorities

6.2.a **Subordination agreement prevents subordinated creditor from taking Rule 2004 discovery against senior lender.** The creditors' subordination agreement provided "the Subordinated Lender shall not … foreclose upon, take possession of, or attempt to realize on any Collateral, or proceed in any way to enforce any claims it has or may have … unless and until the Obligations to the Senior Lender have been fully and indefeasibly paid and satisfied in full." In the debtor's chapter 7 case, the subordinated lender sought discovery under Rule 2004 from the Senior Lender, who opposed the request. Section 510(a) requires the court to enforce a subordination agreement to the same extent enforceable outside of bankruptcy. Here, because any discovery would be calculated to enforce claims against the debtor, the subordination agreement language constitutes an express "silent second" provision, which prevents the subordinated lender from using the bankruptcy process to obtain discovery. *In re Argon Credit, LLC*, 596 B.R. 882 (Bankr. N.D. Ill. 2019).

7. CRIMES

8. DISCHARGE

8.1 General

8.1.a **Court may not sanction a party for violating the discharge injunction if the party had an objectively reasonable belief that the conduct was permitted.** Before bankruptcy, creditors sued the debtor and his transferee to recover an LLC interest that the LLC operating agreement required be offered first to the creditors. During the litigation, the debtor filed bankruptcy and received a discharge. The litigation continued against the debtor's attorney, but the debtor participated to a degree in opposing the relief the creditors sought. After the creditors prevailed, they sought attorneys' fees from the transferee and from the debtor. While the discharge injunction prohibits collection on a discharged debt, a creditor may pursue a debtor for post-discharge attorneys' fees if the debtor returns to the fray after discharge. The creditors relied on this exception. While the attorneys' fees petition was pending, the debtor moved in the bankruptcy court to hold the creditors in contempt for violating the discharge injunction. Later, the state court determined that the debtor had returned to the fray and granted the petition against the debtor, but the state appeals court reversed. The bankruptcy court also found the debtor had returned to the fray, but on appeal, the district court reversed, finding the creditors in contempt for violating the discharge injunction. Section 524(a)(2) provides the discharge operates as an injunction, and section 105(a) gives the bankruptcy court power to issue any order or judgment necessary to carry out other Bankruptcy Code provisions. Because these specific provisions are transplanted from the general rules that govern how courts enforce injunctions, they bring with them those rules. Courts enforce injunctions through the power to cite for civil contempt, which a court should not impose “where there is a fair ground of doubt as to the wrongfulness of the defendant’s conduct.” The standard is an objective one, not dependent on the defendant’s subjective belief that its conduct was permitted, although a good faith belief might help to determine an appropriate sanction. These standards apply equally to civil contempt for violation of the discharge injunction. The court remands the case for the court below to determine whether the conduct here met the standard. *Taggart v. Lorenzen*, 587 U.S. ___, 139 S. Ct. 1795 (2019).

8.2 Third-Party Releases

8.2.a **Equity receivership court may issue a bar order against third party claims.** A federal equity receiver asserted claims against insurance brokers arising from an enormous Ponzi scheme in which the brokers played a material role. Numerous scheme investors, most of whom had claims in the receivership estate, sued the brokers in other courts for essentially the same conduct as the receiver alleged in the receivership action. The receiver settled with the brokers, who insisted on a bar order from the receivership court enjoining the investors from pursing their claims against the brokers. A receivership is designed to take control of all a debtor’s assets, including the debtor’s claims against third parties, and to distribute them equitably among the debtor’s creditors. A receivership solves the collective action problem by channeling all assets and claims into a central forum and controlling the race among creditors to recover on their claims ahead of other creditors. That purpose also informs the court’s power to channel claims against third parties, especially where, as here, the claims arise from a singular scheme, not isolated acts, to perpetrate the Ponzi scheme. Because of the finite resources at issue in the litigation, permitting the investors to seek recovery from the defendant brokers for the same conduct for which the receiver seeks recovery would resurrect the collective action problem. The bar order is within the receivership court’s jurisdiction and appropriate because the investors will share in the recoveries through their allowed claims in the receivership. The bar order also does not deprive the investors of their property (their claims against the brokers) without due process. Instead, they participate in the receivership both procedurally and substantively, where their property interests are protected. Therefore, the court affirms the bar order. *Zacarias v. Stanford Int’l Bank, Ltd.*, ___ F.3d ___, 2019 U.S. App. LEXIS 21764 (5th Cir. July 22, 2019).

8.2.b **Equity receivership court *may not* issue a bar order against third party claims.** A federal equity receiver asserted claims against directors and officers arising from an enormous Ponzi scheme and against managers and employees for their role in the scheme and to recover compensation they were paid. The directors, officers, managers, and employees all asserted claims against the debtor’s insurance carriers under various policies. Substantial disputes existed over, among other things, whether the policies covered the employees and the amount of policy limits. The receiver settled with the carriers, who paid an amount that would have resolved the policy limits dispute. The settlement was contingent on a bar order from the district court enjoining the employees, among others, from pursing any coverage claims against the carriers and from pursuing any statutory or tort claims against the carriers that were not based on or limited in amount by the policies, such as claims for bad faith refusal to defend. In addition, the settlement precluded the employees from filing claims against the receivership estate. A receivership estate may include all the debtor’s property, and the district court has exclusive jurisdiction, as well as broad powers and discretion, over the estate. The insurance policies and their proceeds were properly property of the receivership. But the court’s jurisdiction and discretion are limited. Courts look to bankruptcy law principles for guidance on the limits in a receivership, since bankruptcy law was derived from receivership principles. Thus, the receivership’s claims are only those that address injury to the debtor, and the receivership estate does not include third parties’ assets. Because the insurance policies and their proceeds are property of the estate, the district court may enjoin claims against the carriers but must permit claimants to share in the estate. However, because the receivership estate does not include the claims the managers and employees held against the insurers, the district court may not bar their assertion against the carriers. *S.E.C. v. Stanford Int’l Bank, Ltd.*, ___ F.3d ___, 2019 U.S. App. LEXIS 18111 (5th Cir. June 17, 2019).

8.2.c **Court limits nonconsensual third party releases.** The debtor's plan provided for broad consensual and nonconsensual releases, including non-consensual releases of any claim by a creditor or shareholder arising prepetition against the debtor's audit committee members or against the debtor's prepetition and postpetition lender and plan purchaser. The audit committee members navigated a difficult and complex situation in effecting the restructuring, and the lender enabled the successful plan through its purchase of the debtor's assets. A court may approve a nonconsensual third party release only in rare cases when it is an important part of a reorganization plan. A bankruptcy court has in rem jurisdiction over the debtor and its assets, including claims by and against the debtor, and may adjudicate or release any such claims. The claims subject to the proposed releases were neither by or against the debtor but were property of third parties. The bankruptcy court's jurisdiction over civil proceedings related to a title 11 case does not permit the court to grant the releases, since there is no "proceeding" over which it has jurisdiction. Subject matter jurisdiction is insufficient to give the court power over the claims of third parties, who are subject to the court's exercise of personal jurisdiction only upon proper service of process. Mere notice is insufficient. Even if the court had personal jurisdiction over the third parties, it would not have power to order releases, only power to adjudicate the claims. Imposing a third party release takes the third party's property without recognition of any of the third party's procedural or substantive rights. Finally, the proposed releases here of audit committee members for possible securities law violations go beyond the discharge they could obtain in their own personal bankruptcies, since liability for certain securities law violations are excepted from discharge. The work the proposed releasees did to reorganize the debtor might be worthy of a bonus, but from the debtor, not indirectly from the property of the third parties whose claims are being released. Nor does such work support the treatment of this case as the "rare case" where the releases are an important part of the plan. That the released claims might be frivolous or without merit also does not support the releases, especially because the court has no means to assess whether unasserted claims are meritless. Therefore, the court denies the non-consensual third party releases. *In re Aegean Marine Petroleum Network, Inc.*, 599 B.R. 717 (Bankr. S.D.N.Y. 2019).

8.3 Environmental and Mass Tort Liabilities

9. EXECUTORY CONTRACTS

9.1.a **Rejection is a breach, not a rescission.** The debtor gave a distributor a time-limited non-exclusive limited license to use the debtor's trademarks. After bankruptcy, the debtor in possession rejected the agreement with the distributor, who then asserted its rights under section 365(n) to retain licensed intellectual property. Section 365(n) provides that a licensee under a rejected license of intellectual property may retain its rights to the licensed intellectual property. However, rejection is not rescission; under section 365(g), it is only a breach, effective as of immediately before the commencement of the case. After rejection, the same consequences follow as apply under applicable nonbankruptcy law after a breach. A breach does not permit a breaching trademark licensor to rescind a trademark license. Therefore, the licensee retains all rights granted under the contract. *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 587 U.S. ___, 139 S. Ct. 1652 (2019).

9.1.b **FERC does not have concurrent jurisdiction over an electric utility DIP's rejection of an executory power purchase agreement.** As required by applicable state law, the electric utility debtor announced its intention to file a chapter 11 petition 15 days before filing. During that 15-day period, the Federal Energy Regulatory Commission issued an order finding that it had concurrent jurisdiction with the bankruptcy court over whether the debtor in possession may reject any of its power purchase agreements and whether the DIP and the reorganized debtor may be required, despite rejection, to continue to perform as required in the public interest. After the chapter 11 petition, the DIP sought declaratory relief that the bankruptcy court has exclusive jurisdiction to authorize rejection under section 365 and to determine the effect of rejection. Section 365 grants the bankruptcy court authority to authorize rejection. Any concurrent jurisdiction in FERC that permits FERC to order continued performance would effectively undo the effect of rejection by converting the obligation arising from breach of the contract into a obligation treated the same as the obligations under an assumed contract. Therefore, FERC's order violates the Bankruptcy Code and is unenforceable in the chapter 11 case. *PG&E Corp. v. F.E.R.C. (In re PG&E Corp.)*, ___ B.R. ___, case no. 19-30088 (Bankr. N.D. Cal. June 7, 2019).

9.1.c **A postpetition tail D&O policy is a continuation of a prepetition insurance policy and subject to section 365**. The debtor purchased a one-year directors' and officers' liability insurance policy before bankruptcy. It expired shortly after the petition date. The debtor in possession renewed the policy for one year and soon thereafter purchased a three-year tail policy, which would cover claims made during the three-year period. Each policy was identical, except for dates of coverage and premium amount, and each contained an endorsement that excluded coverage for acts that resulted in insolvency or bankruptcy. The prepetition policy was an executory contract of the debtor. Under section 365(e), an executory contract provision that modifies or terminated the contract based on the debtor's insolvency, bankruptcy, or financial condition is unenforceable. Section 365(e) does not apply to a postpetition contract. However, here, because the postpetition policy was a mere continuation of the prepetition policy, both policies gave the insured the right to purchase the tail coverage, and the tail coverage was an endorsement to the postpetition policy, the tail coverage was a continuation of the prepetition policy to which section 365 should apply. *CMH Liq. Trust v. Nat'l Union Fire Ins. Co. (In re Community Memorial Hosp.)*, ___ B.R. ___ (E.D. Mich. July 23, 2019).

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 may issue final judgment in fraudulent transfer action.** The chapter 11 plan created a liquidating trust, which sued a non-claimant in the bankruptcy court to avoid and recover a fraudulent transfer. Section 157(b)(2) of title 28 includes a list of "core" proceedings, including an action to avoid and recover a fraudulent transfer. In *Granfinanciera, S.A. v, Nordberg*, 492 U.S. 33 (1989), the Supreme Court applied the Seventh Amendment right to a jury trial to a fraudulent transfer action pending before a bankruptcy judge. Although the Court discussed Article III and the judicial power and found the two issues similar and based on similar antecedents, it decided the "sole issue" of the jury trial right and left "for future decision" whether Article III allows a jury trial to be held before a non-Article III bankruptcy judge. In *Stern v. Marshall*, 564 U.S. 462 (2011), the Court issued a narrow ruling that "Congress, in one isolated respect, exceeded" its Article III power. The "isolated respect" in *Stern* was not a fraudulent transfer action, and in a later case, *Exec. Benefits Ins. Agency v. Arkison*, 573 U.S. 25 (2014), the Court "assume[d], without deciding, that the fraudulent conveyance claims in this case are *Stern* claims." Because the statute designates a fraudulent transfer action as a core proceeding in which a bankruptcy judge may issue a final judgment and the Supreme Court has not directly held otherwise, the bankruptcy court may issue a final judgment. *Paragon Litigation Trust v. Noble Corp. PLC (In re Paragon Offshore PLC)*, 598 B.R. 761 (Bankr. D. Del. 2019).

11.2 Sanctions

11.3 Appeals

11.3.a **Appeals from sale proceeds distribution order is not moot.** Before bankruptcy, the lender mistakenly filed a mortgage satisfaction in the land records office, discovered the error, and filed a revocation of the satisfaction. After bankruptcy, the debtor in possession sold the mortgaged property and claimed the proceeds. The bankruptcy court awarded the proceeds to the mortgagee, and the debtor in possession appealed. Section 363(m) provides that a reversal or modification on appeal from an order approving a sale does not affect the validity of the sale. An appeal is moot only when there is no longer a live dispute between the parties; it deprives the court of jurisdiction. Section 363(m) does not make an appeal moot; rather, it is a substantive rule of decision and therefore does not affect the appellate court's jurisdiction. As a substantive rule of decision, section 363(m) addresses only the validity of the sale, not the distribution of proceeds. So the appeal from the order granting the proceeds to the lender is not moot. *Trinity 83 Devel., LLC v. ColFin Midwest Funding, LLC*, 917 F.3d 599 (7th Cir. 2019).

11.4 Sovereign Immunity

12. PROPERTY OF THE ESTATE

12.1 Property of the Estate

12.2 Turnover

12.3 Sales

12.3.a **Debtor in possession may sell hospital free and clear of state attorney general's restrictions on hospital's operations.** In connection with a restructuring three years before bankruptcy, the debtor non-profit hospital had agreed with the state attorney general to maintain specified levels of emergency, intensive care, cardiac, and other services based on historical experience of the hospital operator. The agreement was binding on "any and all current and future owners" of the hospital. After bankruptcy, the debtor in possession proposed to sell the hospital free and clear of those restrictions. Section 363(f)(1) permits sale of property of the estate free and clear of interests in the property if permitted under applicable nonbankruptcy law. "Interests" include any monetary obligations arising from ownership of the property. The restrictions are interests in the hospital property because they arise from the prior use and operation of the hospital. Therefore, section 363(f)(1) applies. *In re Verity Health Sys. Of Calif., Inc.*, 598 B.R. 283 (Bankr. C.D. Cal. 2018).

13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

13.1 Trustees

13.1.a **Liquidating trust does not have standing to bring breach of fiduciary duty action against a limited partnership debtors' principals.** During the chapter 11 case, the court granted the creditors committee authority to bring claims against the debtor's directors and officers for breach of fiduciary duty. The chapter 11 plan transferred those claims to a creditors trust, which pursued the claim. Section 17-1001 of the Delaware Limited Partnership Act authorizes a limited partner to bring a derivative action on the partnership's behalf; section 17-1002 requires the plaintiff to be "a partner or an assignee of a partnership interest at the time of bringing the action." Because neither the debtor nor the creditors were a partner or an assignee of a partner at the time of bringing the action, the trust did not have standing to bring the action. *Gavin/Solmonese LLC v. Citadel Energy P'ners, LLC (In re Citadel Watford City Disposal P'ners, L.P.)*, ___ B.R. ___, 2019 Bankr. LEXIS 1375 (Bankr. D. Del. May 2, 2019).

13.1.b **A plan may vest section 542 turnover rights in a liquidation trustee.** Before bankruptcy, the debtor's board appointed an audit committee to investigate financial statement irregularities. The committee hired counsel and a forensic accountant to investigate. The chapter 11 plan created a liquidation trust and vested the trustee with all the debtor in possession's causes of action under section 542 through 550 and with all rights, titles, and interests in any privilege or immunity applicable to the documents, records, and information related to the investigation. The liquidation trustee sought turnover under section 542 of the documents from counsel and the accountant, who argued that the attorney-client privilege applied to their work for the audit committee separately from the debtor. Section 542 permits the estate, subject to applicable privilege, to obtain turnover of recorded information relating to the debtor's property or financial affairs. Section 1123(b)(3) permits a plan to provide for the retention and enforcement by a representative of the estate of any claims or interests belonging to the debtor or the estate. The plan properly vested the section 542 right in the liquidating trustee, which may obtain the counsel's and accountant's documents, subject to any applicable privilege. *In re Old BPSUSH Inc.*, ___ B.R. ___, 2019 Bankr. LEXIS 1867 (Bankr. D. Del. June 20, 2019).

13.1.c **Liquidating trustee succeeds to audit committee's attorney-client privilege.** Before bankruptcy, the debtor's board appointed an audit committee to investigate financial statement irregularities. The committee hired counsel and a forensic accountant to investigate. The chapter 11 plan created a liquidation trust and vested the trustee with all the debtor in possession's causes of action under section 542 through 550 and with all rights, titles, and interests in any privilege or immunity applicable to the documents, records, and information related to the investigation. Upon the filing of a bankruptcy petition, the trustee obtains control over a corporation's attorney-client privilege. An audit committee is a committee of the board of directors and thus is a component of the debtor. Therefore, the trustee succeeds to control of the audit committee's attorney-client privilege and may obtain all privileged documents. *In re Old BPSUSH Inc.*, ___ B.R. ___, 2019 Bankr. LEXIS 1867 (Bankr. D. Del. June 20, 2019).

13.2 Attorneys

13.3 Committees

13.4 Other Professionals

13.5 United States Trustee

14. TAXES

15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

15.1.a **Court may recognize a foreign representative appointed after a foreign proceeding has been closed.** A creditor of an Indonesian debtor opened a PKPU proceeding against the debtor in the debtor's COMI in Indonesia to obtain a suspension of payments order and to restructure the debtor's debts. The Indonesian court appointed administrators. The debtor completed a financial restructuring in the proceeding, and the court closed the proceeding, which was then no longer subject to reopening. However, the administrators retained authority to ensure the restructuring plan was carried out. Following the court's approval of the restructuring, an ad hoc bondholders committee pursued litigation in New York to collect on their bonds. After several rulings that were adverse to the debtor, the debtor's board adopted resolutions authorizing a director to act as foreign representative and authorizing him to file a chapter 15 petition in New York for recognition of the PKPU proceeding. A chapter 15 case may be commenced only by a foreign representative, which the Code defines as "a person or body … authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor's assets or affairs or to act as a representative of such foreign proceeding." The definition does not require the appointment to occur while the foreign proceeding remains open. To promote chapter 15's broad purposes, courts should read the requirement broadly and include an appointment that occurs in the context of a foreign proceeding. Therefore, the delay in the appointment does not prevent the foreign representative from qualifying to file a chapter 15 case. *In re PT Bakrie Telecom TBK*, ___ B.R. ___, 2019 Bankr. LEXIS 1496 (Bankr. S.D.N.Y. May 30, 2019).