JENNER&BLOCK

Recent Developments in Bankruptcy Law, July 2024

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TABLE OF CONTENTS

1. AUTOMATIC STAY

1.1 Covered Activities

1.1.a **Postpetition action to enjoin unlawful conduct does not violate the automatic stay.** After a Catholic archdiocese filed its chapter 11 case, a group of parents of disabled children sued the archdiocese in state court to enjoin the archdiocese from violating state civil rights laws in its school admission policies. The automatic stay prohibits the commencement or continuation of any action that could have been brought prepetition to recover a claim against the debtor that arose before the commencement of the case or any act to exercise control over property of the estate. The stay does not apply to postpetition events or proceedings addressing postpetition conduct. Section 1108's authorization of the operation of the debtor's business implies operation in conformity with nonbankruptcy law. Moreover, the stay is not implicated by reason of the possible need to expend estate resources to comply with applicable law. This action does not involve the automatic stay's core purpose of preventing a race to the courthouse among creditors or the preservation of property of the estate for use in the reorganization. *Minor Children v. Roman Catholic Church of the Archdiocese of New Orleans (In re Roman Catholic Church of the Archdiocese of New Orleans)*, ___ F. 4th ___, Case No. 23-30565 (5th Cir. July 17, 2024).

1.1.b ***Taggart* civil contempt standard applies to stay violation; whether false competitive advertising violates the stay is subject to a fair ground of doubt.** The debtor provided internet service to retail customers. When it filed its chapter 11 case, a competitor sent advertisements to many of the debtor's customers, falsely claiming that the debtor's business was in jeopardy and urging customers to switch carriers. Many did. In addition, to keep its customers, the debtor launched its own corrective advertising campaign and gave substantial discounts to many customers, causing the debtor substantial losses. Section 362(a)(3) stays any act to obtain possession of property of the estate or to exercise control over the debtor's property. Under *Taggart v. Lorenzen*, 587 U.S. 554 (2019), a court may hold a creditor in civil contempt for violating the discharge injunction only if there is no fair ground for doubt as to whether the discharge injunction barred the creditor's conduct. Although the purpose of the automatic stay and the discharge injunction differ, the contempt standard for each should be the same. The debtor's contract rights are property of the estate. Goodwill is also property of the estate that is protected by the automatic stay. However, the competitor did not take possession or exercise control by launching its advertising campaign, because the campaign did not interfere with the debtor's customer contracts. It only informed the public about the debtor's financial condition and its ability to remain in business. Because there is a fair ground of doubt that the advertising violated the stay, the bankruptcy court may not cite the creditor for contempt. *Windstream Holdings, Inc. v. Charter Comm'ns Op., LLC (In re Windstream Holdings, Inc.)*, 105 F. 4th 488 (2d Cir. 2024).

1.1.c **Section 105(a) injunction against state police power action is not warranted where the action is not irreversible if the debtor prevails.** The debtor in possession brought an adversary proceeding against several states under section 105(a) seeking a preliminary (but not permanent) injunction against their prosecution of litigation challenging the debtor's business practices as unfair or deceptive until the resolution of those cases by a final order no longer subject to appeal. The litigation sought to enjoin the debtor's business practices and to void the contracts the debtor had obtained using those practices. Section 362(b)(4) excepts from the automatic stay a governmental unit's action or proceeding to enforce its police and regulatory power. Despite the exception, a court may enjoin prosecution of a covered action or proceeding only when there is a serious conflict between the police or regulatory power and bankruptcy policy. Here, because the requested relief would amount to an unwarranted complete stay pending appeal in the state actions and because debtor success in the state actions could restore the debtor's interests in

property that the state actions challenged, an injunction was not warranted. *MV Realty PBC, LLC v. Office of the AG (In re MV Realty PBC, LLC)*, 658 B.R. 194 (Bankr. S.D. Fla. 2024).

1.2 Effect of Stay

1.3 Remedies

2. AVOIDING POWERS

2.1 Fraudulent Transfers

2.2 Preferences

2.2.a **Insurance proceeds were not earmarked for a remediation service provider.** The debtor suffered an insured casualty loss. The carrier paid the debtor for remediation services, specifying that the funds could be used only for such services but permitted the debtor to determine which service providers to pay. The debtor paid one of the service providers within 90 days before its bankruptcy. A preference is a transfer of an interest of the debtor in property to or for the benefit of a creditor for or account of an antecedent that enables the creditor to receive more than it would in a chapter 7 case. The earmarking doctrine shields from preference liability a payment from a new lender that is earmarked for the old creditor, even if the funds pass through the debtor's accounts, as long as the earmarking is clear and binding. Here, the service provider does not get the benefit of the earmarking defense, because the insurer was not a new lender and the insurer did not require that the funds be used to pay this particular creditor but gave the debtor discretion to pay any remediation service provider. *Offshore Marine Contractors v. Sommers (In re Magellan E&P Holdings, Inc.*, 654 B.R. 98 (S.D. Tex. 2024).

2.3 Postpetition Transfers

2.4 Setoff

2.5 Statutory Liens

2.6 Strong-arm Power

2.6.a **Trustee may sell section 544 claims and may obtain an extension of the statute of limitations.** The trustee was unable to find counsel to pursue avoiding power claims against the debtor's principal, who (the trustee alleged) had transferred assets away from the debtor and hidden the transactions. The debtor's principal secured lender formed a new company to purchase the avoiding power claims for $150,000. The trustee sought approval of the sale and an extension of the statutes of limitations to pursue the claims. Under section 363, the trustee may use, sell, or lease property of the estate. Section 541(a) includes as property of the estate all of the debtor's interests in property as of the commencement of the case. The court interprets section 541(a) to include avoiding power claims. However, claims under sections 547 and 549 are created by the Code, while claims under section 544(b) are pre-existing claims that the trustee may, in reliance on a triggering creditor, pursue. Based on that distinction, the court permits the trustee to sell the section 544(b) claims but not the section 547 or 549 claims. Citing Rule 9006 (which does not by its terms apply to deadlines fixed by statute), and relying in part on the principal's fraudulent conduct, the court approves the extension of the statute of limitation (without specifying which statute—section 546 or the applicable state law statute). *Teras Breakbulk Ocean Navigation Enters., LLC v. Angueira (In re Teras Breakbulk Ocean Navigation Enters., LLC)*, 658 B.R. 611 (S.D. Fla. 2024).

2.7 Recovery

3. BANKRUPTCY RULES

4. CASE COMMENCEMENT AND ELIGIBILITY

4.1 Eligibility

4.1.a **Trustee's challenges in administering possible marijuana assets is not grounds to deny chapter 7 relief to individual debtor.** The chapter 7 individual debtor owned 100% of an LLC that owned and operated a marijuana dispensary and 40% of another LLC that did the same, as well as several domain names that were suggestive of marijuana businesses. He also claimed a right to a profit distribution from the 40%-owned LLC, but the record was unclear whether there were any profits. The schedules listed no tangible assets connected with marijuana. He also listed prepetition income from his ownership of the 100%-owned LLC. The federal Controlled Substances Act (CSA) prohibits using interstate commerce for engaging in, deriving substantial income, resources, or profits from, or leasing, maintaining, or occupying space used for a marijuana business. In this chapter 7 case, the debtor's entire interests in the LLCs vested in the trustee on the petition date. The CSA does not prohibit the trustee from selling the domain names or the LLC interests nor collecting amounts that the 40%-owned LLC might have owed to the debtor. And any postpetition income from the marijuana businesses of the individual debtor is not property of the estate. In addition, if the trustee is concerned about possibly violating the CSA, he may resign or may abandon the assets. As the court says, "There is no clear basis to disqualify a debtor from the benefits of chapter 7 because of perceived but unanalyzed difficulties the chapter 7 trustee might face when administering the bankruptcy estate." The court denies motions to dismiss the case. *In re Callaway*, 2024 Bankr. LEXIS 1515 (Bankr. N.D. Cal. June 26, 2024).

4.2 Involuntary Petitions

4.2.a **Court may set a deadline to join an involuntary petition.** One creditor filed an involuntary petition. The debtor moved to dismiss on the ground that it had more than 12 creditors. The court set a deadline for other creditors to join. None did so before the deadline. However, several weeks later, and before the court's ruling on the petition, a creditor filed a motion to join. Section 303(a) permits an involuntary petition against a debtor that has 12 or more creditors holding unsecured claims only by three creditors holding unsecured claims. Section 303(c) permits a creditor to join a petition before the case is dismissed or relief is ordered. Rule 1003(b) requires the court to provide creditors a reasonable time to join a petition. Rule 1013(a) requires that the court determine the issues on a contested petition "at the earliest practicable time." Rule 1003(b) should be read in conjunction with Rule 1013(a) so that the court may set a short deadline for joinder. Here, the court properly did so, and the late-joining creditor's motion was denied. *PCC Rokita S.A. v. HH Tech. Corp. (In re HH Tech. Corp.)*, 659 B.R. 788 (1st Cir. B.A.P. 2024).

4.2.b **Petitioning creditor has burden of proof on existence of 12 or more creditors holding unsecured claims.** One creditor filed an involuntary petition. The debtor moved to dismiss on the ground that it had 12 or more creditors, excluding those who had received avoidable preferences. The creditor alleged that some creditors had received avoidable preferences and that creditors who had not received avoidable preferences numbered fewer than 12. The debtor responded that the creditors who had received payment within 90 days before the petition date had affirmative defenses to avoidability. Section 303(a) permits an involuntary petition against a debtor that has 12 or more creditors holding unsecured claims, excluding insiders and creditors who have received avoidable preferences, only by three creditors holding unsecured claims. Section 547(b) makes payments within 90 days before the petition date for or on account of an antecedent debt that enables a creditor to more than it would in a chapter 7 case an avoidable preference, but section 547(c) provides several affirmative defenses to avoidability. A single petitioning creditor has the burden to plead and prove that a debtor has fewer than 12 creditors holding unsecured claims. But unlike in preference litigation, where the burden of proof on affirmative defenses rests with the preferred creditor, here, the petitioning creditor has the burden to show that 90-day payments are avoidable, and that includes the showing that affirmative defenses are not available. *PCC Rokita S.A. v. HH Tech. Corp. (In re HH Tech. Corp.)*, 659 B.R. 788 (1st Cir. B.A.P. 2024).

4.3 Dismissal

5. CHAPTER 11

5.1 Officers and Administration

5.1.a **Court grants preliminary injunction to protect debtor's principals pending reorganization.** Several creditors sued the debtor's principals, who intended to fund the debtor's plan, to collect debts the debtor owed. A court may grant a preliminary injunction against such litigation when the litigation impairs the court's jurisdiction over the case, the debtor establishes a likelihood of success on the merits, and the injunction would not harm the public interest. Impairment of the court's jurisdiction occurs where the principals are a source of funds for the reorganization. "Success on the merits" means a successful reorganization. Here, the principals were responsible for all the debtor's management, accounting, and operations and intended to fund the plan. Therefore, the requirements for a preliminary injunction are met. *Harrington v. Purdue Pharma L.P.*, 144 S. Ct. 2071 (2024), prohibits a plan that grants nonconsensual third-party releases. However, a temporary stay does not amount to a release. *Coast to Coast Leasing, LLC, v. M&T Equip. Fin. Corp. (In re Coast to Coast Leasing, LLC,)*, 2024 Bankr. LEXIS 1662 (Bankr. N. D. Ill. July 17, 2024).

5.1.b **Court denies preliminary injunction to protect debtor's former executives from state court litigation.** Before bankruptcy, a former executive of the debtor sued the debtor and other former officers in state court. After the debtor filed its chapter 11 case, it sought to extend the stay to protect the former officer defendants in the action. A court may extend the stay to protect a nondebtor based on the standard for issuing a preliminary injunction, including likelihood of success on the merits and risk of irreparable injury. In a chapter 11 case, the "merits" is usually interpreted to mean a successful reorganization or plan confirmation and that the injunction is necessary to facilitate that goal or to prevent interference with the reorganization, for example by preventing the distraction that nonbankruptcy litigation may impose on the debtor while trying to reorganize the business and negotiate a plan or by providing a respite that can facilitate negotiations toward a consensual resolution of the claims against the nondebtors. However, after *Harrington v. Purdue Pharma L.P.*, 144 S. Ct. 2071 (2024), which prohibits nonconsensual third-party releases of nondebtors, success on the merits can no longer include the possibility of confirmation of a plan containing such releases. Here, the debtor in possession could not meet the standards for a preliminary injunction. Potential indemnity obligations, which the debtor disputed in the nonbankruptcy litigation, do not establish that the claims against the former officers are, in reality, claims against the debtor; the risk and cost of being subject to ordinary discovery in the action does not establish a risk to the reorganization; and the risk of distraction is minimized since the action is against former, not current, executives. Therefore, the DIP did not establish that the stay was critical to success on the merits or would prevent irreparable injury. *In re Parlement Techs., Inc*, 2024 Bankr. LEXIS 1627 (Bankr. D. Del. July 15, 2024).

5.2 Exclusivity

5.3 Classification

5.4 Disclosure Statement and Voting

5.5 Confirmation, Absolute Priority

5.5.a **Plan modification requires resolicitation, even of rejecting creditors.** The debtor proposed a plan that allocated new equity to existing shareholders based solely on new capital contributions. A day before confirmation, the controlling shareholder moved to modify the plan to eliminate the contributions of the other three shareholders, without notifying them of the motion. The court confirmed the plan, reasoning that the shareholders were to receive or retain nothing under the plan on account of their old equity interests and were therefore deemed to reject the plan. Accordingly, the court concluded that neither a new disclosure statement nor new solicitation was

required. The debtor consummated the plan. The Court of Appeals reversed. On remand, the bankruptcy court determines that even though the dispute was just between competing groups of shareholders, the court had subject matter jurisdiction as a core proceeding, because the dispute centered on plan confirmation. The consummation of the plan did not moot the dispute, because the court could still order a remedy for the violation. A remedy that revises only part of the plan is permissible, because the revision affects only those parties before the court—the shareholder groups—and does not affect creditors, who were paid in full under the plan. The alternative of enforcing the plan's nonseverability provision would require vacating the confirmation order and reinstating the debtor as a debtor in possession, which would be an impractical remedy. Moreover, the Court of Appeals effectively permitted partial invalidation by its opinion. Accordingly, the court orders the parties to unwind the share issuance and to implement the funding and issuance of shares as contemplated by the original plan. *In re America-CV Station Group, Inc.*, 658 B.R. 622 (Bankr. S.D. Fla. 2024).

5.5.b **Subchapter V cram-down plan does not require disposable income true-up to actual income.** The debtor confirmed a subchapter V plan under section 1191(b), which requires that the plan devote the debtor's "projected disposable income" to payments under the plan for the plan period. Based on *Hamilton v. Lanning*, 560 U.S. 505 (2010), projected income is determined by taking into account known or virtually certain information about the debtor's future income and expenses and is decidedly forward-looking, that is, projected, not retrospective or actual. Therefore, by its terms, the Code does not contemplate a true-up, requiring the debtor to pay actual disposable income during the plan term if that income is higher than projected. The lack of any provision in subchapter V for plan modification by anyone other than the debtor reinforces this interpretation. *In re Packet Constr., LLC*, Case No. 23-10860-cgb (Bankr. W.D. Tex. Apr. 30, 2024).

5.5.c **Nonvoting class prevents consensual confirmation in a subchapter V case.** The debtor's subchapter V plan had two classes, comprising one creditor each. One accepted the plan; the other did not. Section 1191(a) permits consensual plan confirmation only if section 1129(a)(8), among others, is satisfied. Section 1129(a)(8) requires "with respect to each class of claims or interests (A) such class has accepted the plan; or (B) such class is not impaired." Section 1126(c) provides that a class has accepted a plan if creditors holding at least two-thirds in dollar amount and a majority in number of claims in the class accept the plan. Therefore, a class whose creditors do not vote at all does not accept the plan. Accordingly, plan confirmation may only be under section 1191(b), which provides for nonconsensual confirmation. *In re M.V.J. Auto World, Inc.*, 2024 Bankr. LEXIS 1487 (Bankr. S.D. Fla. June 21, 2024).

5.5.d **Postconfirmation claim amendment requires compelling circumstances.** The creditor filed a proof of claim, then amended it to $0 based on events during the chapter 11 case, then, after confirmation, reasserted the original amount based on a new theory of recovery. Plan confirmation has the same res judicata effects as a judgment in a civil action. A postconfirmation claim amendment might make the plan infeasible, disrupt the orderly process of adjudication or alter the distributions to other creditors contemplated under the confirmed plan. Therefore, to permit a postconfirmation amendment, the bankruptcy court must find compelling circumstances. *CLO Holdco, Ltd. v. Kirschner (In re Highland Cap. Mgmt. LP)*, 102 F. 4th 286 (5th Cir. 2024).

5.5.e **Res judicata prevents relitigation of settled issues upon confirmation of a plan modification.** The debtor filed a plan that valued and bifurcated the secured creditor's claim and provided for applying property rents to the secured portion of the claim. The debtor later sought plan modification. Section 1327, by making the provisions of a confirmed plan binding on all parties in interest, effectively codifies res judicata for plan confirmation orders. Section 1329 expressly permits plan modification, which is an exception to the binding effect of section 1327 and the res judicata doctrine. However, section 1327 and the doctrine continue to apply to any plan provision that is not proposed to be modified, such that a creditor may not renew a previous plan objection to a plan provision that the debtor does not propose to modify. *In re Smith*, 102 F. 4th 643 (3d Cir. 2024).

5.5.f **Court may not vacate confirmation order after 180 days, even for unnoticed creditor.** As a result of a judgment and lien obtained by a receivables lender, the debtor filed a chapter 11 case and elected to proceed under subchapter V. The debtor and the lender ultimately settled during the case, entered into a settlement agreement, which was incorporated into a plan, and obtained plan confirmation. The debtor failed to give notice of the filing to another secured lender, who made its first appearance in the case 143 days after entry of the confirmation order. After discovery and more than 180 days after plan confirmation, the unnoticed lender moved to vacate the orders confirming the plan and approving the settlement. Section 1144 permits revocation of confirmation only within 180 days after confirmation and if and only if confirmation was obtained by fraud. Bankruptcy Rule 9024, which incorporates Fed. R. Civ. P. 60, permits a court to modify or vacate an order but specifically limits the ability to revoke a confirmation order to the time allowed by section 1144. Therefore, Rule 60 does not permit the relief the unnoticed creditor sought. Vacating a confirmation order is effectively the same as revocation and does not provide a work-around. Because the plan incorporated the settlement agreement, vacating the order approving the agreement would amount to vacating the confirmation order and is equally prohibited. However, since the unnoticed creditor did not receive notice of the case or the plan, none of the court's orders are binding on the creditor, and the creditor may pursue all its claims and rights unaffected by the chapter 11 case. *In re Mine Hill Anesthesia, LLC*, 658 B.R. 214 (Bankr. S.D. Fla. 2024).

6. CLAIMS AND PRIORITIES

6.1 Claims

6.1.a **Right to future royalties is a claim.** Before bankruptcy, the debtor purchased the rights to a drug from the creditor for a fixed sum plus 1% of sales each year in excess of $10 million. Under section 101(5)(A), "claim" is defined as a right to payment, whether liquidated or unliquidated, fixed or contingent, or matured or unmatured. "Unliquidated" means not ascertained in amount. "Contingent" means subject to a future event, not limited to extrinsic events, but including events contemplated by and even those controlled by the debtor or the creditor. Though the future royalties are contingent and unliquidated, they fall within the definition of "claim." Generally, a claim under a contract arises when the contract is agreed. Contingency is determined by when the liability is triggered, not by when the claim arises. Here, at the petition date, the creditor's rights were both unliquidated and contingent, but still a claim. Under the debtor's plan, all claims were discharged. Therefore, the creditor's rights to post-confirmation royalties were discharged. *In re Mallinckrodt PLC*, 2024 U.S. App. LEXIS 10035 (3d Cir. Apr. 25, 2024).

6.1.b **Nonrecourse special revenue bondholders have security interest in future revenues but no unsecured deficiency claim.** The municipal debtor had issued revenue bonds payable solely from and secured by the debtor's net revenues. The U.C.C. permits a debtor to grant a security interest in after-acquired property, but the interest does not attach until the debtor acquires rights in the property. Generally, section 552(a) cuts off a lien on property a debtor acquired postpetition, but section 928(a) provides that section 552(a) does not apply to postpetition "special revenues" that secure revenue bonds. Therefore, the bondholders' security interest extends to future revenues. The security interest secures a claim for the full face amount of the bonds, plus accrued interest. Generally, section 1111(b) permits a nonrecourse secured claim to be allowed as a recourse claim, unless the creditor elects otherwise. However, section 927 makes section 1111(b) inapplicable to special revenue bonds in a chapter 9 case. Therefore, the bondholders may not pursue a general unsecured claim for any amount by which the value of future net revenues is less than the face amount of the bonds. *Fin. Oversight and Mgmt. Bd. v. Cortland Cap. Mkt. Servs. LLC (In re Fin. Oversight and Mgmt. Bd.)*., 104 F. 4th 367 (1st Cir. 2024).

6.2 Priorities

6.2.a **Disappointed bidder is not entitled to "substantial contribution" allowance.** A bidder for the debtor's assets negotiated with the debtor prepetition, during the postpetition "stalking horse" stage, and at the auction for the debtor's assets. It was unsuccessful and did not even bid at the auction. It sought fees for making a substantial contribution by providing competition to other bidders, resulting in an increased sale price. Section 503(b)(3)(D) permits the court to allow compensation and reimbursement of expenses incurred by "a creditor, an indenture trustee, an equity security holder, or a committee … in making a substantial contribution" in a chapter 11 case. A bidder who is not a creditor or other party listed in section 503(b)(3)(D) is not eligible. Moreover, in this case, this bidder did not contribute to any increased bid proposal from others. Therefore, the court denies the request. *In re NVN Liquidation, Inc.*, 2024 Bankr. LEXIS 952 (Bankr. D. Del. Apr. 8, 2024).

7. CRIMES

8. DISCHARGE

8.1 General

8.2 Third-Party Releases

8.2.a **Bankruptcy Code does not authorize nonconsensual third-party releases under a chapter 11 plan.** The debtors manufactured opioids. Their products resulted in an opioid epidemic, exposing the debtor to substantial mass tort liability. Their shareholders/directors/officers were potentially exposed for both direct and derivative claims of the victims and were indemnified by the debtors for all such claims and defense costs. The debtors proposed a plan under which the shareholders contributed at least $5.5 billion to various funds against which claims of individuals and governments, among others, were channeled. In exchange, the shareholders received non-consensual third-party releases of both derivative and direct claims relating to the debtors "as to which any conduct, omission or liability of any Debtor or any Estate is the legal cause or is otherwise a legally relevant factor." Over 90% of creditors accepted the plan. Section 1123(b) specifies what a plan may include; paragraph (6) permits "any other appropriate provision not inconsistent with the applicable provisions" of the Code. The provision's scope is limited by the preceding paragraphs of section 1123(b), all of which relate to the debtor, its rights and responsibilities, and its relationship with creditors. Despite the indemnification provisions, the releases here do not concern the debtor. Moreover, only the debtor may gain a discharge, which requires the debtor to make all its assets available for its creditors. The only exception is for asbestos bankruptcies, under section 524(g), which suggests it is not available in other cases. Therefore, the plan may not include nonconsensual third-party releases. The opinion does not address what would be necessary to evidence "consent." *Harrington v. Purdue Pharma L.P.*, 603 U.S. ___, 144 S. Ct. 2071 (2024).

8.2.b **Court denies exculpation of insiders granted in exchange for remaining with the debtor.** The debtor in possession engaged in a liquidation of its assets. Several officers and employees threatened to leave before sales were complete if they did not receive releases of any claims against them by the DIP. The DIP agreed and provided for the exculpation in the plan. Section 503(c) prohibits a "transfer made to or an obligation incurred for the benefit of an insider for the purpose of inducing such person to remain with the debtor's business" unless certain conditions are met. The prohibition is not limited to the payment of administrative claims but includes all postpetition transfers and obligations. Here, the releases transfer property of the estate—potential claims against the officers. Section 1123(b)(3) permits the plan to release claims the estate owns, and Rule 9019 permits settlement of the estate's claims. However, section 1129(a)(1) requires that a plan comply with all applicable Code provisions, which includes section 503(c). Therefore, the court denies approval of the releases for the benefit of the insiders. *In re Mercon Coffee Corp.*, Case No. 23-11945 (MEW) (Bankr. S.D.N.Y. Juny 19, 2024).

8.3 Environmental and Mass Tort Liabilities

9. EXECUTORY CONTRACTS

9.1.a **Section 365(d)(4) time limit applies only to a "true lease."** The debtor leased shopping center real property for a 100-year term for a nominal payment, plus payment of common area charges and taxes. Within the 120-day deadline of section 365(d)(4), the DIP moved to assume and assign the lease, which the court approved, but the approval was reversed on appeal. While the matter was still on appeal, the debtor confirmed a plan, which vested some estate assets (including the lease) in a liquidating trust. Section 365(d)(4) provides that if the trustee does not assume a lease within 120 days (as extended) after the order for relief, the lease is deemed rejected, and the property must be surrendered to the lessor. Filing a motion to assume stops the clock. However, the ultimate denial of the motion on appeal after the assumption deadline left matters in limbo, with no case law instructing what the parties' rights would be. But Second Circuit case law provides that the deadline applies only to a true lease. The economics of this lease suggested it was not a true lease but rather more akin to a transfer of ownership. As such, the deadline did not apply, the deemed rejection did not operate, and the lease remained in the bankruptcy estate and then vested in the trust. *MOAC Mall Holdings LLC v. Transform Holdco LLC (In re Sears Holdings Corp.)*, 2024 U.S. Dist. LEXIS 81227 (S.D.N.Y. May 3, 2024).

9.1.b **District court gives a master class in applying the section 502(b)(6) lessor claim damages cap.** The debtor guaranteed its subsidiary's long-term lease and secured the guarantee with a letter of credit. Days after the debtor filed bankruptcy, the subsidiary vacated the premises and delivered the keys to the lessor, but the lessor refused to accept those acts as a termination of the lease. The lessor drew the full amount of the letter of credit; the issuer's reimbursement claim was satisfied from estate assets. The lessor filed a claim in the debtor's case for the full rent remaining under the lease plus clean-up costs incurred when the subsidiary vacated the premises. Section 502(b)(6) caps "the claim of a lessor for damages resulting from the termination of a lease of real property" to an amount equal to "the rent reserved by such lease, without acceleration, for the greater of one year, or 15 percent, not to exceed three years, of the remaining term of such lease." The provision does not limit its application to a lease by the debtor and so applies equally to a guarantee by the debtor of another's lease. The provision does not define "termination." Under applicable nonbankruptcy law, termination would ordinarily require the lessor's agreement. However, such a requirement would defeat the provision's purpose, because the lessor could refuse to agree and therefore prevent the limitation measurement period from beginning. Therefore, in this case, the tenant's surrender of the keys and abandonment of the premises constitutes "termination" for purposes of section 502(b)(6). The limitation amount is based on the rent reserved for the specified time period—the "Time Approach"—rather than on a percentage of the remaining rent under the lease—the "Rent Approach," because the language specifically applies the percentage measurement to the remaining term of the lease, not the remaining rent under the lease. Because the estate satisfied the bank's reimbursement claim under the letter of credit, the letter of credit amount should be applied to the lessor's damage claim *after* calculation of the damages cap. Otherwise, the lessor would be able to end-run the cap. Finally, whether clean-up costs are subject to the cap depends on whether the costs resulted from termination, that is, whether the lessor would have had the same claim if the tenant assumed the lease. In this case, the lessor had the clean-up costs claim only because the tenant terminated the lease. Therefore, they are subject to the cap. *Lincoln Triangle Commer. Holding Co. LLC v. Halperin (In re Cortlandt Liquidating LLC)*. 658 B.R. 244 (S.D.N.Y. 2024).

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 **"Related to" jurisdiction is determined *ex ante*.** The debtor had a tax dispute with the IRS and sought to litigate it in the bankruptcy court under section 505, which permits the bankruptcy court to determine the amount and legality of any tax. The bankruptcy court's jurisdiction is governed by 28 U.S.C. 1334, which grants the district court jurisdiction over any proceeding arising in or related to a bankruptcy case or arising under title 11. Because the tax dispute arose before bankruptcy and is not governed by any Code provision, only related-to jurisdiction could apply. The courts have construed related-to jurisdiction to apply if the dispute could have any conceivable effect on the estate or its assets or liabilities. Consistent with all other jurisdictional rules, the related-to determination is made at the outset of the dispute, so even though it turns out that the resolution of the dispute would ultimately have no effect on the estate, if it were conceivable when the dispute arose (the court doesn't address whether that would be at the petition date or when the adversary proceeding is commenced), the court has jurisdiction. Section 505 is not a jurisdictional rule. It merely authorizes the bankruptcy court to address a tax dispute if jurisdiction lies under section 1334. Here, because the debtor filed the adversary proceeding before most claims were filed, with the result that the outcome might have affected distributions, even though by the time the dispute was resolved, many claims were filed, and the outcome would not affect distributions, the bankruptcy court had jurisdiction and could hear the tax dispute. *Bush v. United States*, 100 F. 4th 807 (7th Cir. 2024).

11.1.b **Insurer has standing as party in interest in asbestos chapter 11 case.** The debtor proposed a plan in an asbestos chapter 11 case that provided for the debtor's insurance policies to be assigned to the section 524(g) trust. Under the plan, to prevent fraudulent claims, a claimant with an uninsured claim had to provide information to the trust about other asbestos trust claims and provide a certification. A claimant with an insured claim was not required to provide the certification. Under the insurance policy, the debtor was required to assist in the investigation and defense of claims. The insurer claimed that the different treatment of insured and uninsured claims under the plan was not "insurance neutral," that is, that it effected a change in the debtor's or the insurer's obligations under the insurance policies. The bankruptcy court found otherwise, and therefore determined that the insurer was not a party in interest who had standing to object to confirmation. Section 1109(b) permits a "party in interest" to appear and be heard on any issue in a chapter 11 case. "Party in interest" is capacious. Its plain meaning includes anyone whose interests might be directly affected by the chapter 11 case. The section's statutory history and purpose also evidence an intent to broaden standing to prevent insider control. Here, the potential financial harm to the insurer gives it an interest in the case's outcome. Whether the plan is actually insurance neutral does not affect the analysis, because that question conflates standing with the merits. That said, section 1109(b) gives only a voice, not a veto. The Court does not determine insurance neutrality or confirmation but simply reverses and remands for consideration of the insurer's objection to confirmation. *Truck Ins. Exch. v. Kaiser Gypsum Co, Inc.*, 603 U.S. ___, 144 S. Ct. 1414 (2024).

11.1.c **Adversary defendant does not have standing to move to dismiss bankruptcy case.** A debtor's chapter 7 trustee sued defendants who had advanced funds for the benefit of the debtor's parent corporation, which was also a chapter 7 debtor. The defendants did not have claims against the subsidiary debtor. A court may dismiss a chapter 7 case for cause. Only a party in interest has standing to move to dismiss a case. The Code does not define "party in interest," but courts have defined the term to refer to creditors "who have claims against the estate and whose pecuniary interests are directly affected by the bankruptcy." Where a party's interest is solely its status as a defendant, adverse to the estate, it is not a party in interest with

standing to appear and be heard in the case. *In re Richardson Foods, Inc.*, 659 B.R. 154 (Bankr. S.D.N.Y. 2024).

11.2 Sanctions

11.2.a **Compensatory civil contempt sanctions are limited to amounts needed to purge the contempt and may not include litigation over the contemnor's motives.** Without objection, the court prohibited all parties from filing an action against the debtor in possession's CEO except with the permission of the bankruptcy court. Entities related to the former CEO filed an action against the current CEO in the district court. The DIP's CEO obtained an order to show cause why the entities and the former CEO should not be held in contempt and conducted extensive discovery into the reasons for the filing, after which the court held a lengthy hearing on contempt and granted the DIP fees for the OSC, the discovery, and the hearing. A bankruptcy court has authority to issue a civil, but not a criminal, contempt citation. A civil contempt order must be coercive or compensatory and may not be punitive. The contempt in this case was the filing of the action in the district court, regardless of motive. The inquiry into motive and the award of fees for that activity was punitive; compensatory damages would have been limited only to the work required to obtain dismissal of the district court action. *Fund, L.P. v. Highland Cap. Mgmt., L.P. (In re Highland Cap. Mgmt., L.P.)*, 98 F. 4th 170 (5th Cir. 2024).

11.2.b **Bankruptcy court may award fees against the United States as a contempt sanction.** The trustee subpoenaed a retired IRS agent for a deposition. The government moved to quash. The court denied the motion with respect to most proposed questions. The trustee took the deposition. In violation of the court's order, the government and the witness refused to answer numerous approved questions. The trustee moved to hold the government in contempt and for a compensatory award of fees and costs. Under its inherent authority, a court, including a bankruptcy court, may hold any person who willfully disobeys a specific order in contempt and may impose sanctions to compensate the injured party for damages incurred because of the contempt. Section 106(a) abrogates the government's sovereign immunity with respect to the bankruptcy court's authority under section 105, which authorizes the court to issue any order necessary to carry out the provisions of the Code, including the authority to find a litigant in contempt. Therefore, the court may find the government in contempt and award compensatory sanctions. *Marshack v. Eisenhower Carlson, PLLC (In re Eagan Avenatti, LLP)*, 659 B.R. 214 (Bankr. C.D. Cal. 2024).

11.3 Appeals

11.3.a **Only aggrieved creditors have standing to appeal specific issues.** The debtor's plan left the general unsecured claims unimpaired. Creditors whose claims were disputed and in litigation in a nonbankruptcy forum objected to confirmation on feasibility, best interest, good faith, release and exculpation, and appropriateness of settlement grounds. If the creditors prevailed on any of those grounds, their recoveries would not increase, because their claims were unimpaired. The court overruled the objections. In bankruptcy, only a "person aggrieved," that is, a person whose rights are diminished or impaired or whose burdens are increased, by an order of the bankruptcy court has standing to appeal. Whether an appellant is a person aggrieved is determined on an issue-by-issue basis. Because the objecting rights and burdens of the objecting creditors, whose claims were unimpaired, were not affected by the confirmation order, they did not have standing to appeal, except on their feasibility objection. *CMB Exp., LLC v. Tonopah Solar Energy, LLC (In re Tonopah Solar Energy, LLC)*, 657 B.R. 393 (D. Del. 2022).

11.3.b **Order granting recognition under chapter 15 is appealable.** The foreign representatives commenced a chapter 15 case. Over the debtor's objection, the court granted recognition. Only a final order is appealable. In bankruptcy, finality is determined at the "proceeding" level, not at the whole case level. If an order finally determines a discrete procedural sequence, including notice and a hearing, and occurs apart from the main case, the order should be appealable. Here, the entire case rests on the validity of the order, and delaying appeal until the conclusion of the case

would present a significant risk to judicial economy. Therefore, the court has jurisdiction over the appeal. *Zawawi v. Diss (In re Zawawi)*, 97 F. 4th 1244 (11th Cir. 2024).

11.3.c **Contempt for violation of discovery-related order is not final and appealable.** Under Bankruptcy Rule 2004, the bankruptcy court ordered claimants to complete a personal injury questionnaire (PIQ). Some claimants sued in district court in another state to enjoin the enforcement of the order. The bankruptcy court held the claimants and their counsel in contempt for violation of the PIQ order and awarded the debtor attorneys' fees. In ordinary civil litigation, a party may appeal a civil contempt order only at the conclusion of the litigation. In bankruptcy, because there are many proceedings within the main case, the rules on finality and appealability of orders are measured at the proceedings level, rather than at the case level. Here, the contempt order itself was not a separate proceeding but was part of a discovery dispute in connection with determining the total amount of claims and developing a plan, which is part of the main case. Therefore, this contempt order is not immediately appealable and will become appealable only upon conclusion of the case. *Blair v. Bestwall, LLC (In re Bestwall, LLC)*, 2024 U.S. App. LEXIS 10293 (4th Cir. Apr. 29, 2024).

11.3.d **Order denying subchapter V eligibility is final and appealable.** The debtor incurred substantial debts that enabled her to open a business many years before opening the business. At the confirmation hearing, the court was prepared to confirm her plan otherwise, but denied confirmation because she was ineligible to proceed under subchapter V. In bankruptcy, the concept of finality is flexible and pragmatic, based on whether an order resolves and terminates a proceeding that is a distinct procedural unity within the larger bankruptcy case. The bankruptcy court's separate order on eligibility disposed of that issue, even though issued in the context of denying confirmation. Therefore, it was final and appealable. *Reis v. Garvin (In re Reis)*, Case No. 1:23-cv-00279-BLW (D. Ida. June 20, 2024).

11.3.e **Appellee need not include arguments on issues that would arise only if the appellant prevails.** The debtor leased shopping center real property for a 100-year term for a nominal payment, plus payment of common area charges and taxes. Within the 120-day deadline of section 365(d)(4), the DIP moved to assume and assign the lease, which the court approved, but the approval was reversed on appeal. While the matter was still on appeal, the debtor confirmed a plan, which vested some estate assets (including the lease) in a liquidating trust. Section 365(d)(4) provides that if the trustee does not assume a lease within 120 days (as extended) after the order for relief, the lease is deemed rejected, and the property must be surrendered to the lessor. Filing a motion to assume stops the clock. However, the ultimate denial of the motion on appeal after the assumption deadline left matters in limbo, with no case law instructing what the parties' rights would be. But Second Circuit case law provides that the deadline applies only to a true lease. The economics of this lease suggested it was not a true lease but rather more akin to a transfer of ownership. The DIP failed to raise the true lease issue in the bankruptcy court or in the appeal. An appellee need not raise arguments that would apply only if the appellee lost on the appeal. It is required only to respond to the appellant's arguments, "not to invent arguments about the consequences of a hypothetical reversal," because courts do not deal in hypotheticals and need not give advisory opinions if they are reversed. Therefore, the DIP did not waive the true lease argument. *MOAC Mall Holdings LLC v. Transform Holdco LLC (In re Sears Holdings Corp.)*, 2024 U.S. Dist. LEXIS 81227 (S.D.N.Y. May 3, 2024).

11.4 Sovereign Immunity

11.4.a **Section 106 abrogates states' sovereign immunity for injunction action under section 105(a).** The debtor in possession brought an adversary proceeding against several states under section 105(a) to enjoin their prosecution of litigation challenging the debtor's business practices as unfair or deceptive. The litigation sought to enjoin the debtor's business practices and to void the contracts the debtor had obtained using those practices. Section 106(a) abrogates the states' sovereign immunity with respect to matters arising under section 105. As a result, the states are subject to suit on claims pursued to further the bankruptcy laws, including to protect the

bankruptcy court's exclusive *in rem* jurisdiction over property of the estate, the equitable distribution of property, and the debtor's discharge. Here, the DIP's action implicates the first two of those purposes, since the state actions seek to affect the debtor's contracts, which are property of the estate. Moreover, the DIP's proceeding implicates only section 105, as it does not seek any rulings on the states' actions in state courts. Therefore, the states are not immune from suit in this adversary proceeding. *MV Realty PBC, LLC v. Office of the AG (In re MV Realty PBC, LLC)*, 658 B.R. 194 (Bankr. S.D. Fla. 2024).

12. PROPERTY OF THE ESTATE

12.1 Property of the Estate

12.1.a **Demutualization proceeds of prepetition insurance policy are property of the estate.** The debtor insured its physician members through a mutual insurance company but terminated the policies more than two years prepetition. Postpetition, the insurance company began the process of de-mutualization. Under applicable state law, holders of policies within 3 years before demutualization are entitled to the demutualization proceeds. The process was not concluded until after plan confirmation and closing of the case. When concluded, the demutualization resulted in a substantial payment to the debtor. Property of the estate includes "all legal or equitable interests of the debtor in property as of the commencement of the case." Property acquired postpetition becomes property of the estate only if it is derived from property that was part of the estate as of the commencement of the case, that is, only if it is sufficiently rooted in the prebankruptcy past. Because the debtor owned the mutual interest as of the commencement of the case, the demutualization proceeds became property of the estate. *Kim v. NRAD Med. Assocs., P.C. (In re NRAD Med. Assocs., P.C.)*, 658 B.R. 1 (Bankr. E.D.N.Y. 2024).

12.1.b Voluntary "escrow" remains property of the debtor. The debtor and its landlord engaged in state court litigation. During the case, debtor's counsel stated to the court that the debtor was placing monthly rent payments in an escrow account. The account was in the debtor's name and address. After bankruptcy, the debtor transferred the funds to a debtor in possession account. Under applicable state law, a valid escrow requires an agreement on subject matter, a third-party depositary, irrevocable delivery of the escrow property to the third party, subject to agreed terms on disbursement, and relinquishment of the property by the depositor. Property subject to a valid escrow does not become property of the depositor's bankruptcy estate but becomes property of the estate if the escrow does not meet the four requirements. Here, there was no agreement: the money was voluntarily deposited by the debtor into the separate account, without the landlord's agreement. Because the property was held in the debtor's name, there was no third-party depositary, and the debtor never relinquished its interest in the funds. Finally, there were no terms governing disbursement. Therefore, the property was property of the debtor as of the petition date and therefore property of the estate. *In re Odanata Ltd.*, 658 B.R. 62 (Bankr. S.D.N.Y. 2024). n

12.2 Turnover

12.3 Sales

13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

13.1 Trustees

13.1.a **Subchapter V trustee does not have standing to pursue claims on behalf of the estate.** In the subchapter V case, the debtor remained in possession. The subchapter V trustee brought an action against a third party to enjoin the defendant from interfering with the debtor. Section 1184 gives a subchapter V debtor in possession all the rights of a debtor in possession in an ordinary chapter 11 case. Section 1183 specifies a subchapter V trustee's duties. They include objecting to claims, providing information and a final report, facilitating development of a plan, and

participating in hearings on a plan. None of these duties authorize the trustee to pursue claims on the estate's behalf. Therefore, only the subchapter V debtor in possession has authority to pursue such claims. *Singh v. Price (In re Turkey Leg Hut & Co. LLC)*, 659 B.R. 539 (Bankr. S.D. Tex. 2024).

13.2 Attorneys

13.2.a **Counsel for debtor who also represents 43% shareholder without ethical wall is not disinterested.** Counsel for the debtor in possession also represented the debtor's 43% shareholder, who was a $14 million per year (1.4% of revenues) firm client and appointed two of the debtor's 13 directors. Because the individual lawyers working on the case also actively performed services for the shareholder, all of which were unrelated to the debtor, an ethical wall was not feasible. The firm also represented the debtor's officers and directors in shareholder litigation and had received prepetition payments that were potentially avoidable preferences. The DIP consented to the joint representation, and the DIP proposed to retain conflicts counsel as well. Section 327(a) requires counsel for the DIP to be disinterested and not hold or represent an interest adverse to the estate. Disinterestedness requires that counsel does not have an interest materially adverse to the estate's interest or to any class of creditors or shareholders. Disqualification under these provisions must be addressed on a case-by-case basis. Because directors and officers are generally entitled to indemnification from the debtor, the firm's representation of them creates only a potential conflict, which is not disqualifying. The potential preference is not disqualifying, because the court could grant derivative standing to the committee to investigate and pursue the claim if necessary. However, the firm's continued representation of the shareholder renders the firm not disinterested. Employment of conflicts counsel can be useful for portions of a case, such as avoiding power claims, but is not a substitute for general counsel's duties to manage the case and negotiate a plan. Here, the court finds an actual conflict in the firm's representation of the shareholder, who has an interest in the outcome of the case. *In re Enviva Inc.*, 2024 Bankr. LEXIS 1266 (Bankr. E.D. Va. May 30, 2024).

13.2.b **DIP counsel who represents principal secured lender on unrelated matters is not disqualified.** Debtor's counsel also represented, on unrelated matters, the debtor's principal secured lender, who accounted for about $2 million (0.03%) of the firm's annual revenue. The lender held 79% of the debt from a transaction less than a year prepetition. The transaction was a central issue in the case. The lender, the debtor, and the firm had agreed to a broad conflicts waiver. Section 327(a) requires that counsel for the DIP be disinterested and not hold or represent an interest adverse to the estate. Disinterestedness requires that counsel does not have an interest materially adverse to the estate's interest or to any class of creditors or shareholders. "Adverse interest" is any economic interest that would tend to lessen value or create an actual or potential dispute with the estate. These provisions disqualify an attorney with an actual conflict, but disqualification based on a potential conflict is discretionary, and the appearance of a conflict is not grounds for disqualification. Model Rule 1.7 prohibits representation that is directly adverse to another client or that would materially limit the lawyer's responsibilities to another client. An informed waiver may resolve a conflict but may not overcome lack of disinterestedness. Here, the representation of the creditor on small, unrelated matters does not prevent the firm from being disinterested. However, it would violate Rule 1.7 but for the conflicts waiver, which the court finds sufficient. The court approves the employment of the firm as DIP's counsel but requires an ethical wall between lawyers working on the chapter 11 case and lawyers providing the unrelated services to the lender. *In re Invitae Corp.*, 2024 Bankr. LEXIS 1267 (Bankr. D.N.J. May 16, 2024).

13.3 Committees

13.3.a **Creditor has no protected right to serve on a committee.** A lawyer for four committee members violated a confidentiality order. The bankruptcy judge ordered the U.S. trustee to remove the four members, and the U.S. trustee appointed three new members. The removed members appealed. Under Article III standing requirements, an appellant must have a legally protected interest. Under the more demanding bankruptcy "person aggrieved" standing

requirement, an appellant must have a pecuniary interest in the outcome of the appeal. A creditor does not have a right to serve on a committee and therefore suffers no loss of any protected right when being removed from the committee. Therefore, the court dismisses the appeal for lack of standing. *Adams v. Roman Catholic Church of the Archdiocese of New Orleans (In re Roman Catholic Church of the Archdiocese of New Orleans)*, 101 F. 4th 400 (5th Cir. 2024).

13.3.b **Court orders a U.S. trustee to appoint indenture trustee to committee, despite a signed RSA.** The debtor had two bond issues, comprising the overwhelming majority of the debtor's debts. The holders of 95% of one issue and the holders of 78% of the other issue signed an RSA, which the court had not yet approved and which remained subject to further negotiations, but neither indenture trustee had signed. The U.S. trustee had appointed three trade creditors to the committee. One was a competitor, and one was about to resign. The indenture trustees moved for an order to require the U.S. trustee to appoint an indenture trustee to the committee. Section 1102(a)(4) permits the court to order the U.S. trustee to change committee membership if necessary to assure adequate representation. Factors to consider include the committee's ability to function, the nature of the case, the constituencies' standing and desires, the creditors' ability to participate without a committee or need representation, and the movant's motivation. Here, adequate representation requires at least one indenture trustee on the committee. Since neither indenture trustee had signed an RSA, they would not be conflicted. Therefore, the court orders the U.S. trustee to appoint at least one indenture trustee to the committee. *In re Enviva Inc.*, 2024 Bankr. LEXIS 1195 (Bankr. E.D. Va. May 21, 2024).

13.4 Other Professionals

13.5 United States Trustee

14. TAXES

15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

15.1.a **Chapter 15 eligibility does not depend on section 109(a)'s requirement of domicile, residence, or property in the United States.** The debtor was the subject of an insolvency proceeding in the UK, where he resided. Through off-shore subsidiaries, he indirectly owned property in the United States, but did not own any property directly and had no other contact with the United States. Section 101(13) defines "debtor" as person or entity concerning which a case under title 11 has been commenced. Section 1502 defines "debtor" as entity that is the subject of a foreign proceeding. Under section 103(k), chapter 1 of the Code, including section 109, applies in a chapter 15 case. Section 109(a) provides that only a person with a domicile, residence, place of business, or property in the United States is eligible to be a debtor under title 11. The definitions create an anomaly. Read literally, section 109(a) applies in chapter 15 and requires the debtor to have the requisite contact with the United States to be eligible for a chapter 15 case. However, the court had previously determined that prior section 304, which chapter 15 replaced, suffered from the same anomaly. The court determined that the resolution of the anomaly should take into account section 304's purpose to prevent dismemberment by local creditors of assets belonging to a foreign debtor. On that basis, the court adopted an expansive definition of the class of foreign proceedings for which ancillary relief is available. Chapter 15 has a similar purpose, so the court follows its precedent, adopts the broader definition of "debtor" to include a debtor in a foreign proceeding, and permits the case to proceed. *Zawawi v. Diss (In re Zawawi)*, 97 F. 4th 1244 (11th Cir. 2024).