**BANKRUPTCY UPDATE**
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# Recent Developments in Bankruptcy Law

(Covering cases reported through 520 B.R. 325 and 770 F.3d 435)

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# 1. AUTOMATIC STAY

## 1.1 Covered Activities

**1.1.a. Remand does not violate the automatic stay.** The defendant removed a state court action to federal court. The day before the hearing on plaintiff's motion for remand, the defendant filed a bankruptcy petition. The automatic stay prohibits continuation of any action against the debtor commenced before bankruptcy. A remand is a determination that the court lacks power to hear the case and that the case belongs in another court, not a continuation of the action. One of the stay's purposes is to give the debtor a breathing spell from collection efforts. Sending the case back to the proper court, which should stay the action, does not contravene that purpose. Therefore, the stay does not bar remand. *Sanders v. Farina*, ___ B.R. ___, 2014 U.S. Dist. LEXIS 178081 (E.D. Va. Nov. 18, 2014).

## 1.2 Effect of Stay

## 1.3 Remedies

# 2. AVOIDING POWERS

## 2.1 Fraudulent Transfers

**2.1.a. A fraudulent transferee has a good defense only to the extent of actual value, from the transferee's perspective, that it actually gave the debtor.** The debtor's affiliate borrowed money from a bank, secured by the affiliate's real property, which the debtor occupied. The debtor began monthly payments to the bank in an amount equal to the required loan payments but in excess of the property's fair monthly rental value. After bankruptcy, the trustee sued the bank to avoid and recover the payments as an actual fraudulent transfer. Under section 548(a), the trustee may avoid a transfer that the debtor made with actual intent to hinder, delay, or defraud creditors. Under section 548(c), a transferee "that takes for value and in good faith … may retain any interest transferred … to the extent that such transferee … gave value to the debtor in exchange." Because subsection (c) refers to the value the transferee gave to the debtor, and consistent with subsection (c)'s intent to protect a good faith transferee, the court must analyze the amount of value from the transferee's perspective, not from the debtor/transferor's. "Value" in subsection (c) is not the same as "reasonably equivalent value" in section 548(a), which determines whether a transfer is constructively fraudulent. Rather, "value" refers to the actual value that the transferee gave the debtor. Subsection (c) protects the transfer "to the extent" the transferee gave value. Therefore, the court must net the value of what the transferee received against the value it gave, and it is liable for the difference, thereby protecting the estate and its other creditors from undervalue transactions. *Williams v. Fed. Dep. Ins. Corp. (In re Positive Health Mgmt.)*, 769 F.3d 899 (5th Cir. 2014).

**2.1.b. Safe harbor protects withdrawals from stockbroker Ponzi scheme.** The stockbroker debtor ran a Ponzi scheme. It accepted deposits into customer accounts under customer account agreements and trading authorizations that directed the stockbroker to purchase and sell a set group of common stocks and options, produced false account statements that showed consistently profitable securities trading in the accounts and honored withdrawal requests as they were made, until it ran out of money, though the debtor did not engage in any securities transactions. The trustee sued to recover account withdrawals as preferences and fraudulent transfers. The section 546(e) safe harbor prohibits avoidance of a stockbroker's transfer that is a settlement payment or that is made in connection with a securities contract. A securities contract is defined with extraordinary breadth as a contract for the purchase, sale, or loan of a security; any other agreement or transaction that is similar to such a contract; a master agreement that provides for an agreement or transaction to purchase, sell, or loan a security; or any security agreement or arrangement related to any such agreement or transaction. The customer agreements are sufficient to create securities contracts, even though the stockbroker did not execute any trades, because they both provided for the purchase and sale of securities and acted as master

agreements for numerous trades; the definition does not require any actual trades for the contracts to qualify. A transfer is made "in connection with" a securities contract if it is related to or associated with the contract. The account withdrawals were related to the customer agreements and therefore were made in connection with a securities contract. The transfers are subject to the safe harbor. *Picard v. Ida Fishman Revocable Trust (In re Bernard L. Madoff Inv. Secs. LLC)*, 773 F.3d 411 (2d Cir. 2014).

**2.1.c. Extension agreement of more than one year does not take repurchase agreement out of the safe harbor.** The debtor financed mortgage backed securities with repurchase agreements, all of which provided for repurchase within less than one year. The counterparty issued substantial margin calls, which the debtor could not meet. They negotiated an agreement to defer further margin calls and delay the repurchase date to a date more than one year after the original repurchase agreement date. The debtor's trustee sued to avoid and recover payments the debtor made after the extension agreement. Section 546(f) protects from avoidance any payment made to a "repo participant … in connection with a repurchase agreement." A "repurchase agreement" is an agreement providing for repurchase within one year. Courts should construe "in connection with" in section 546(f) broadly. Although the extension agreement provided for repurchase outside of one year, the transfer was still in "connection with" the repurchase agreement and was not avoidable. *Sher v. JP Morgan Chase Funding Inc. (In re TMST, Inc.)*, 518 B.R. 329 (Bankr. D. Md. 2014).

**2.1.d. Extension agreement is not an obligation that the trustee may avoid.** The debtor financed mortgage backed securities with repurchase agreements. The counterparty issued substantial margin calls, which the debtor could not meet. They negotiated an agreement to defer further margin calls and delay the repurchase date. The debtor's trustee sued to avoid the debtor's obligations under the extension agreement and the resulting payments the debtor made under the agreement. Section 548(a)(1)(B) permits a trustee to avoid an obligation the debtor incurs for less than reasonably equivalent value if the debtor was then insolvent. The effect of an obligation the debtor incurs without reasonably equivalent value is to increase its liabilities and potential claims against the debtor's assets without adding other assets to satisfy the new liabilities. An extension agreement does not by itself increase the debtor's liabilities. An extension obligation that merely reaffirms existing obligations does not incur an obligation. Therefore, the trustee may not avoid the extension agreement or the payments under the agreement. *Sher v. JP Morgan Chase Funding Inc. (In re TMST, Inc.)*, 518 B.R. 329 (Bankr. D. Md. 2014).

**2.1.e. Section 546(a) trumps state statute of repose.** The debtor ran a Ponzi scheme. The trustee sued under section 544(b) to avoid as fraudulent transfers payments to investors made within seven years before bankruptcy. Applicable nonbankruptcy law imposed a four-year statute of limitation on a creditor's right to avoid and recover a fraudulent transfer and a statute of repose that extinguishes the creditor's claim after seven years. The trustee filed his complaint within two years after the petition date but more than seven years after some of the transfers. Section 546(a) limits the time within which a trustee may bring an avoiding power action to two years. It preempts nonbankruptcy statutes of limitations that apply to claims under section 544(b), giving the trustee two years to bring an action if a creditor could have brought the action as of the petition date, furthering the bankruptcy policy to allow the trustee sufficient time to marshal the estate's assets. The same policy applies to a state statute of repose. The trustee may bring an avoiding power action after the statute of repose has expired, as long as it had not expired as of the petition date. *Rund v. Bank of America Corp. (In re EPD Inv. Co, LLC)*, ___ B.R. ___, 2015 Bankr. LEXIS 40 (9th Cir. B.A.P. Jan. 7, 2015).

**2.1.f. LLP is a corporation for Bankruptcy Code purposes.** The debtor law firm was a limited liability partnership under state law, which provides that partners are not liable for any obligations of the partnership, except that a partner is liable for "negligent or wrongful conduct committed by him or her or by any person under his or her direct supervision or control while rendering professional services" on behalf of the partnership. Section 101(9) defines "corporation" as including "a partnership association organized under a law that makes only the capital subscribed responsible for the debts of such association." The general liability limitation qualifies the debtor partnership as a "corporation" under the Bankruptcy Code. The exception does not make a partner liable for the partnership debts generally and, therefore, the debtor is a "corporation." *Jacobs v. Altorelli (In re Dewey & LeBoeuf LLP)*, 518 B.R. 766 (Bankr. S.D.N.Y. 2014).

**2.1.g. Partnership distributions to working partners are not for value.** The debtor law firm was a limited liability partnership. The partners were practicing lawyers who received distributions before

bankruptcy while the partnership was insolvent. Section 548 permits the trustee to avoid a transfer made for less than reasonably equivalent value while the debtor was insolvent. Generally, services provided to a debtor are "value" in exchange for compensation. However, under partnership law, partners are not entitled to compensation, because they are expected to devote their efforts to the partnership business and receive the firm's profits. Therefore, the services that the partners provided do not constitute value to the partnership debtor, and the distributions are avoidable. *Jacobs v. Altorelli (In re Dewey & LeBoeuf LLP)*, 518 B.R. 766 (Bankr. S.D.N.Y. 2014).

### 2.2 Preferences

### 2.3 Postpetition Transfers

### 2.4 Setoff

### 2.5 Statutory Liens

### 2.6 Strong-arm Power

**2.6.a. Unintentionally authorized UCC-3 terminates a financing statement.** The debtor borrowed under a synthetic lease facility, secured by specified assets, and under a general facility, secured by equipment and other assets at most of the debtor's manufacturing locations. The same bank acted as agent for both facilities. The bank filed two UCC-1 financing statements for the synthetic lease and a third UCC-1 for the other facility. The debtor arranged to pay off the synthetic lease and instructed its counsel to prepare the necessary documents, including a UCC-3 termination statement to release the security interest. Counsel prepared a UCC-3 that mistakenly listed the UCC-1 file number for the general facility. Neither the debtor, debtor's counsel, the bank, nor the bank's counsel caught the error. The bank's counsel signed off on the closing and related escrow instructions, and the mistaken UCC-3 was filed. The debtor later filed bankruptcy. The creditors committee challenged the perfection of the bank's security interest. Under UCC section 5-510(a), a termination statement is effective only if its filing is authorized under section 5-509. Under section 5-509(d), only the secured creditor (or the debtor, if the secured creditor fails to do so) may authorize the filing. Under section 5-513(d), an authorized filing terminates the financing statement. The secured creditor's intent in filing a termination statement is irrelevant if it has authorized the filing. Here, even though the bank did not know the termination statement was mistaken and never intended to terminate the financing statement for the general loan, the bank authorized the filing of the termination statement. Therefore, it was effective to terminate the general security interest. *Official Committee of Unsecured Creditors v. JP Morgan Chase Bank, N.A. (In re Motors Liquidation Co.)*, ___ F.3d ___, 2015 U.S. App. LEXIS 859 (2d Cir. Jan. 21, 2015).

**2.6.b. Relation back does not prime a tax lien, but equitable title does.** The debtor borrowed money from the bank and gave the bank a mortgage on its Maryland real property on January 4. The bank recorded the mortgage on February 11. The IRS filed notice of its tax lien against the debtor on January 10. Under Maryland law, a mortgage recordation relates back to the date of delivery, becoming effective once recorded against an intervening judicial lien creditor. Internal Revenue Code section 6323(a) provides that a tax lien is not "valid as against any … holder of a security interest … until notice thereof …has been filed by the [Treasury] Secretary." Section 6323(h)(1) defines security interest as "any interest in property acquired by contract for the purpose of securing payment or performance of an obligation," and provides "a security interest exists at any time—(A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation." The verb tenses in the statute determine the provision's interpretation. Although the mortgage recordation relates back, it was not protected against a subsequent judgment lien creditor at the time the IRS recorded its lien notice. Therefore, it was not then a "security interest," as defined, and it does not take priority over the tax lien as a result of Maryland's relation back doctrine. However, Maryland law also provides that delivery of a real property transfer instrument gives the transferee equitable title that is good immediately as against later judicial liens. The tax lien is protected only to the extent that a later judicial lien arising out of an unsecured credit extension would be protected. Therefore, the mortgage has priority over the tax lien. *Susquehanna Bank v. U.S. (In re Restivo Auto Body, Inc.)*, 772 F.3d 168 (4th Cir. 2014).

**2.6.c. Creditor may not use parol evidence against a trustee to save a defective security interest.** The security agreement secured a note dated December 15 "in the principal amount of

$______." The debtor's note was dated December 13. The lender and the debtor agreed that the date in the security agreement was an error; there was no note dated December 15, and they intended to secure the note dated December 13. Section 544(a)(1) gives the trustee the rights of a hypothetical judicial lien creditor. Although the lender might have been able to use parol evidence against the debtor to reform the security interest, a later creditor is entitled to rely on the face of the documents and need not investigate whether parol evidence or other documents would vary their terms. Such a rule promotes certainty in commercial transactions. Therefore, the trustee's rights are unaffected by parol evidence, and the trustee may avoid the security interest. *State Bank of Toulon v. Covey (In re Duckworth)*, 586 Fed. Appx. 672 (7th Cir. 2014).

### 2.7 Recovery

## 3. BANKRUPTCY RULES

**3.1.a. Inadequately-noticed DIP settlement stipulation does not bind chapter 7 trustee.** The debtor in possession sold assets in which a creditor claimed a security interest. The DIP stipulated with the creditor, the buyer, and the creditors committee that the proceeds would be segregated pending resolution of the creditor's claim. The creditor later moved for enforcement of the stipulation, claiming that the DIP had not segregated the proceeds. The DIP listed the motion on the hearing agenda filed two days before the hearing and served on parties in interest, but the parties settled on the hearing day. The DIP filed and served another agenda the same day stating that the matter had been settled and filed a certificate of counsel with the settlement stipulation, which the court approved the next day. The stipulation released the creditor from all claims relating to the debtor or the chapter 11 case. After the case was converted to chapter 7, the trustee sued the creditor to avoid prepetition transfers as preferences. Rule 9019 permits a bankruptcy court to approve a settlement under case-law standards on notice to creditors, among others. Here, there was no notice of the settlement, and the bankruptcy court did not find that it complied with the standards for approval of a settlement. Therefore, the settlement's broad release did not bind the chapter 7 trustee. *Burtch v. Avnet, Inc.*, ___ B.R. ___, 2015 U.S. Dist. LEXIS 5266 (D. Del. Jan. 16, 2015).

## 4. CASE COMMENCEMENT AND ELIGIBILITY

### 4.1 Eligibility

### 4.2 Involuntary Petitions

**4.2.a. Regulatory payment prohibition does not make debtor's payment obligation contingent.** The alleged debtor issued trust preferred securities: it issued subordinated notes to an affiliated trust, which issued preferred equity securities to an investor. The note indenture permitted the debtor to defer interest payments for up to 20 quarters. The debtor's regulator prohibited it from making interest payments. After the deferral period expiration, the debtor defaulted on interest payments. The note indenture permits a trust preferred holder, upon a default, "to institute a suit directly against [the debtor] for enforcement of payment" of principal and interest. A "suit" is a proceeding by one party against another in court. An involuntary petition is a proceeding by the creditor against the alleged debtor in court and is therefore a suit that the investor may bring under the indenture. A creditor is eligible to file an involuntary petition if it holds a claim "that is not contingent as to liability or the subject of a bona fide dispute as to liability or amount." A claim is "contingent" when the debtor's payment obligation does not arise until the occurrence of a future event that was in the parties' contemplation. Although the regulatory order disabled the debtor from paying interest, the debtor's legal obligation to pay was fixed. Therefore, the investor is a qualified petitioning creditor. *FMB Bancshares, Inc. v. Trapeza CDO XII, Ltd. (In re FMB Bancshares, Inc.)*, 517 B.R. 361 (Bankr. M.D. Ga. 2014).

### 4.3 Dismissal

**4.3.a. No-asset, single-creditor corporate debtor's chapter 7 case is filed in bad faith.** The corporate debtor invested in a Ponzi scheme and had no assets after the Ponzi scheme collapsed. The

Ponzi scheme trustee sued the debtor to recover its withdrawals from the Ponzi scheme as fraudulent transfers. The Ponzi scheme trustee was the debtor's only creditor. After two years of litigation, the debtor filed a chapter 7 case, which stayed the litigation. The chapter 7 trustee filed a no asset report. The Ponzi scheme trustee moved to dismiss the case as a bad faith filing. A bankruptcy court may dismiss a voluntary case that is filed in bad faith. Using bankruptcy solely as a litigation tactic is bad faith. Bankruptcy's twin pillars are a discharge and a fair distribution of the debtor's assets among creditors. A corporate debtor does not receive a discharge in chapter 7, and here, there are no assets to distribute. The bankruptcy case's only effect is to stay the fraudulent transfer litigation. Therefore, the case was filed in bad faith and should be dismissed. *Kelley v. Cypress Fin. Trading Co., L.P.*, 518 B.R. 373 (N.D. Tex. 2014).

**4.3.b. Section 305(a) abstention is not an appropriate remedy for a bad faith filing.** The creditor obtained a state court judgment against an individual. In the year after the judgment, the individual transferred real property among himself, his wife and related entities, until it rested with an LLC owned by a trust for which the individual defendant is the trustee. The creditor sued in a sister state's court to enforce the judgment against the LLC on constructive trust, reverse veil piercing and fraudulent transfer theories. The LLC owed property taxes, three banks with secured claims, all of which were parties to the state court action, and a few small unsecured claims. It filed a chapter 11 petition three days before the start of trial in the state court. A party in interest, including a creditor, may raise and appear and be heard on any issue in a case. A creditor is one who holds a prepetition claim, even a disputed, contingent, or unliquidated claim, against the debtor. Party-in-interest status is not limited to a creditor who has filed a proof of claim. It also includes anyone with a financial stake in the case's outcome. The creditor had a stake based on the claims he asserted in the state court action and therefore had standing to challenge the filing. Under section 305(a), a bankruptcy court may suspend proceeding in or dismiss a case if the interests of creditors and the debtor would be better served by abstention. Abstention must serve the interests of both creditors generally and the debtor. Abstention is an extraordinary remedy that should be granted sparingly. Rarely will a voluntary case meet the abstention requirements, because abstention is not likely to be in the debtor's interest where the debtor has commenced the case. Even where the debtor filed in bad faith, section 305(a) does not permit dismissal, though section 1112 does. Here, abstention might have served the parties to the state court action, but not the property tax creditor, the unsecured creditors, or the debtor. Therefore, the district court reverses the bankruptcy court's section 305(a) dismissal order and remands to consider in view of the debtor's apparent bad faith filing, whether dismissal under section 1112(b) or stay relief, either of which may be granted based on the debtor's bad faith, should be granted. *Sapphire Dev., LLC v. McKay*, ___ B.R. ___, 2014 U.S. Dist. LEXIS 179406 (D. Conn. Nov. 5, 2014).

## 5. CHAPTER 11

### 5.1 Officers and Administration

**5.1.a. Claim objection and cram down plan support do not violate intercreditor agreement.** Second lien creditors supported the debtor in objecting to a portion of first lien claims and in proposing a cram down plan against first lien creditors. Under an intercreditor agreement, second lien creditors agreed not to contest or support any other person in contesting first lien creditors' request for adequate protection or their objection to any motion based on lack of adequate protection and agreed not to take any action to hinder any first lien creditor remedy exercise or object to the manner in which the first lien creditors sought to enforce their claims or liens. However, the agreement permitted second lien creditors to take any action available to them as holders of unsecured claims. An intercreditor agreement of the type at issue here (as opposed to a "silent second" type) contemplates that the senior creditor controls all matters related to the common collateral, but does not restrict the junior creditors to the extent that their rights derive from holding, or are the same as the rights of holders of, an unsecured claim. An unsecured claim holder may object to claims or support the debtor in doing so and may support the debtor in proposing a cram down plan against a senior lien holder. Therefore, the second lien holders' actions do not violate the intercreditor agreement. *BOKF, N.A. v. JPMorgan Chase Bank, N.A. (In re MPM Silicones, LLC)*, 518 B.R. 742 (Bankr. S.D.N.Y. 2014).

**5.1.b. Reorganized debtor common stock is not proceeds of collateral.** The plan provided for first lien creditors to retain their lien on their collateral to secure new, cram-down notes and for second lien creditors to receive all the reorganized debtor's stock. In addition, the plan contemplated a rights offering, which second lien creditors back-stopped for a fee. Under an intercreditor agreement, second lien creditors agreed not to take any action to hinder any first lien creditor remedy exercise or object to the manner in which the first lien creditors sought to enforce their claims or liens. Second lien creditors also agreed not to receive any proceeds of common collateral or rights arising out of common collateral until first lien claims were paid in full in cash. However, the agreement permitted second lien creditors to take any action available to them as holders of unsecured claims. "Proceeds" includes whatever is received upon disposition of collateral. In this case, first lien creditors retain their lien on the common collateral. The reorganized debtor's stock was not part of the collateral or even property of the debtor. Therefore, it is not proceeds of the second lien. The common stock second lien creditors receive is on account of their claims, but not on account of the common collateral, so second lien creditors' receipt of the new stock does not violate the intercreditor agreement. Second lien holders became entitled to the back-stop fee as a result of their new, postpetition back-stop commitment, not their second lien claim, and the fee is therefore not proceeds of the common collateral. Therefore, the plan and the back-stop fee did not violate the intercreditor agreement's prohibition on second lien creditors' receipt of common collateral proceeds before payment in full of first lien claims. *BOKF, N.A. v. JPMorgan Chase Bank, N.A. (In re MPM Silicones, LLC)*, 518 B.R. 742 (Bankr. S.D.N.Y. 2014).

### 5.2 Exclusivity

### 5.3 Classification

### 5.4 Disclosure Statements and Voting

### 5.5 Confirmation, Absolute Priority

**5.5.a. Trust Indenture Act prohibits a restructuring transaction that deprives note holders of the practical (but not legal) right to payment.** The debtor, worth only about $1.0 billion, had issued $1.3 billion in secured debt and $200 million in unsecured notes. The debtor's arguably-solvent parent guaranteed the unsecured notes. The notes indenture released the guarantee upon a majority vote of noteholders or a release of a parent guarantee of the secured notes. The debtor was unable to pay all interest and principal on the debt as they became due, but a bankruptcy filing would have rendered it ineligible for federal programs that provided the majority of its revenue. It initiated restructuring negotiations with its secured debt holders. Before concluding a restructuring deal, the secured debt holders agreed to an interim extension of some obligations and received a parent guarantee. Further negotiations resulted in a complete restructuring agreement under which the secured debt holders would release the parent guarantee, foreclose on their security interest under Article 9, bid in their claims, and, upon acquiring the assets, sell them back to a new subsidiary of the parent, which would purchase them by issuing debt and equity to secured debt holders and equity to consenting unsecured note holders. The Trust Indenture Act prohibits impairment of a note holder's right to receive payment of principal and interest or to bring suit for enforcement of payment without the holder's consent. The indenture contained an identical prohibition. The TIA's purpose is to prevent nonconsensual modification of payment rights, to protect judicial scrutiny of the fairness of restructuring plans, and to permit nonconsensual debt adjustment only through bankruptcy. Therefore, a court should not read the TIA narrowly, to protect only the legal entitlement to payment and to bring suit, but should apply its prohibition to protect the practical right to payment as well. However, to prevent litigation over any corporate activity that might adversely affect an issuer's ability to pay TIA-governed debt, a court should apply the modification prohibition only when the modification effects an involuntary debt restructuring. Here, combination of the guarantee release, the foreclosure, the re-sale to the debtor's affiliate, and the resulting overall debt restructuring deprived the complaining note holders of their practical right to payment and therefore violated the TIA's involuntary modification prohibition. The court refuses to enjoin the transaction, however, based on the balance of the equities and public policy grounds. *Marblegate Asset Mgmt v. Educ. Mgmt. Corp.*, ___ F. Supp. 3d ___ (S.D.N.Y. Dec. 30, 2014); *accord MeehanCombs Global Credit Opp. Funds, LP v. Caesars Entertainment Corp.*, ___ F. Supp. 3d ___, 2015 U.S. Dist. LEXIS 5111 (S.D.N.Y. Jan. 15, 2015).

# 6. CLAIMS AND PRIORITIES

## 6.1 Claims

## 6.2 Priorities

**6.2.a. Section 510(b) subordinates claim against broker-dealer for failure to purchase parent's debt securities.** The debtor broker-dealer was the creditor's executing broker. The creditor held the debtor's parent's unsecured bonds. It sold them before the debtor's SIPA proceeding, but the debtor did not complete the transaction, leaving the creditor with a loss when it later sold the bonds, for which it asserted a claim against the debtor. Section 510(b) requires subordination of a claim for damages arising from the purchase or sale of a security of the debtor or of an affiliate of the debtor. Courts read "arising from" broadly, to include a claim that would not have arisen but for a purchase or sale. Therefore, section 510(b) applies to the damage claim here for failure to purchase the affiliate's security. Section 510(b) specifies the subordination level, which is subordination to "all claims or interests that are senior or equal to the claim or interest represented by the [security]," separately referencing the claim subject to subordination, the underlying security, and the claim the security represents. Section 510(b) applies to securities of a debtor's affiliate, so it applies even though the underlying security is not within the debtor's capital structure or claim priority ladder. The subordination level is based on the kind of claim the security represents. Here, the bonds represented general unsecured claims against the debtor's parent. Therefore, it is subordinated to general unsecured claims against the debtor. *In re Lehman Bros., Inc.*, 519 B.R. 434 (S.D.N.Y. 2014).

**6.2.b. IRS claim for reimbursement of replacement refund check is not entitled to priority.** The trustee filed amended tax returns for the individual debtor to carry back her net operating losses for prepetition years. The IRS accepted the amendments and mailed a refund check, but to the debtor, who cashed the check and spent the money. The trustee sued the IRS for turnover, which the bankruptcy court ordered. The IRS then filed a proof of a priority tax claim for the extra refund. Section 507(c) provides "a claim of a governmental unit arising from an erroneous refund … has the same priority as a claim for the tax to which such refund or credit is due." In this case, the refund was not erroneous; it was correct. But the IRS sent the check to the wrong place. Therefore, section 507(c) does not apply, and the IRS's claim for priority is disallowed. *McCarthy v. IRS (In re Naeem)*, 515 B.R. 297 (Bankr. E.D. Va. 2014).

# 7. CRIMES

# 8. DISCHARGE

## 8.1 General

## 8.2 Third-Party Releases

## 8.3 Environmental and Mass Tort Liabilities

# 9. EXECUTORY CONTRACTS

**9.1.a. Section 365(d)(5) gives a lessor an automatic administrative expense claim for rent arising from and after 60 days after the order for relief.** The equipment lessor filed an administrative expense claim for postpetition rent. The debtor in possession contended the lease was a secured financing and the estate did not use the equipment during the case in a way that benefited the estate.
Section 503(b)(1) allows an administrative expense claim for the actual and necessary costs and expenses of preserving the estate. The claimant has the burden of establishing benefit to the estate.
Section 365(d)(5) requires the trustee to perform all the debtor's obligations under a personal property

lease arising from and after 60 days after the order for relief, unless the court orders otherwise, based on the equities of the case. The trustee has the burden of showing equities of the case. Accordingly, rent arising from and after 60 days after the order for relief is entitled to allowance as an administrative expense unless the trustee shows otherwise. Therefore, to consider the lessor's claim properly, the court must first determine whether the transaction is a true lease or a secured financing. If the former, then the court must allow rent arising from and after 60 days after the order for relief as an administrative expense unless the trustee shows otherwise based on the equities of the case. The claimant has the burden of showing entitlement to an administrative expense claim for the 60-day period or, if the transaction is a secured financing, for the entire postpetition period. *GE Capital Comm'l, Inc. v. Sylva Corp., Inc. (In re Sylva Corp., Inc.)*, 519 B.R. 776 (8th Cir. B.A.P. 2014).

## 10. INDIVIDUAL DEBTORS

### 10.1 Chapter 13

### 10.2 Dischargeability

### 10.3 Exemptions

### 10.4 Reaffirmation and Redemption

## 11. JURISDICTION AND POWERS OF THE COURT

### 11.1 Jurisdiction

**11.1.a. Securities class action plaintiff does not gain automatic class standing in the defendant's chapter 11 case.** The plaintiff's securities class action was stayed when the corporate defendant filed a chapter 11 case. The district court named the plaintiff as lead plaintiff in the class action, but denied his request to be named lead plaintiff for the bankruptcy case. He did not seek class representative or lead plaintiff status in the bankruptcy case or seek application of the class action rules there. The chapter 11 plan provided for a third-party release of claims against the individual defendants but permitted creditors to opt out of the release. The plaintiff opted out but objected to confirmation to the extent it included the release. Because the release did not bind the plaintiff, he could not object to confirmation on his own behalf. He also could not object on behalf of the class, because the district court did not grant him authority to act as lead plaintiff anywhere other than in the securities class action, and he did not obtain authority to act in the chapter 11 case from the bankruptcy court. Therefore, the lead plaintiff did not have standing in the bankruptcy court, and the court dismisses the appeal from denial of his objections. *Lucas v. Dynegy Inc. (In re Dynegy Inc.)*, 770 F.3d 1064 (2d Cir. 2014).

**11.1.b. Case dismissal does not deprive the court of jurisdiction to award committee counsel fees.** The court dismissed the chapter 11 case without condition or jurisdictional reservation and closed the case. A short time later, committee counsel filed a compensation application. A debtor remains liable after dismissal for debts incurred during administration. Committee counsel fees are not owing until the court awards them under section 330. The court has jurisdiction over proceedings arising in or related to a bankruptcy case. A fee request is both. Dismissal does not deprive the court of jurisdiction to tie up loose ends such as the fee request. Therefore, the court should consider the fee application. It may award the fees, creating the debtor's obligation to counsel, but may not order payment, as there is no estate after dismissal. If the court awards the fees, counsel may pursue collection after dismissal in the state courts. *In re Sweports, Ltd.*, ___ F.3d ___, 2015 U.S. App. LEXIS 470 (7th Cir. Jan. 9, 2014).

### 11.2 Sanctions

### 11.3 Appeals

**11.3.a. Equitable mootness doctrine applies to an appeal from an order confirming a liquidating plan.** The debtor confirmed its liquidating chapter 11 plan. Two weeks later, arguing lack of adequate

notice, three creditors moved for leave to file late proofs of claims and to certify a class of similarly situated creditors. The bankruptcy court denied the motions seven months later, finding that they had adequate notice of the bar date. They appealed but did not seek a stay of the confirmation order, and the estate had by then already paid administrative and priority claims. An appeal from a plan confirmation order is equitably moot "when, even though effective relief could conceivably be fashioned, implementation of that relief would be inequitable" such as by being impractical or imprudent. In the Second Circuit, the court presumes such an appeal is equitably moot if the plan has been substantially consummated. The appellant may rebut the presumption by showing the court can still grant some relief, which will not affect the debtor's reemergence as a revitalized company or knock the props out from under plan transactions and create an unmanageable situation for the bankruptcy court, adverse parties have a chance to participate, and the appellant pursued a stay diligently. As in connection with a reorganizing plan, parties and the court may have devoted substantial time and resources to plan formulation and confirmation, and substantial interests may have attached. Therefore, the equitable mootness presumption should apply equally to an appeal from a liquidating chapter 11 plan confirmation order. Here, the plan was substantially consummated, and the appellants did not assure adequate protection for potentially affected parties or pursue a stay. Therefore, the court dismisses the appeal. *Beeman v. BGI Creditors' Liquidating Trust (In re BGI, Inc.)*, 772 F.3d 102 (2d Cir. 2014).

**11.3.b. Seeking a stay is required to prevent equitable mootness dismissal.** The debtor raised money from investors to extend mortgage loans by granting the investors interests in the notes and mortgages and acting as servicer. The bankruptcy court confirmed a plan that transferred the servicing rights to a new manager. The manager sought to sell some of the loans. An investor objected on the grounds, among others, that the plan did not transfer the agreement to the manager and if it did, the investor could revoke its servicing agreement as a revocable agency agreement. The bankruptcy court overruled the objection and granted the manager a declaratory judgment affirming its authority. The investor appealed and sought a stay. The bankruptcy court conditioned the stay on a bond that the investor could not afford. The district court affirmed the bankruptcy court's ruling on the stay. The manager sold some of the properties while the appeal was pending. A court may dismiss a bankruptcy appeal as equitably moot based on whether a stay was sought, the plan was substantially consummated, the remedy would affect third parties not before the court and would not knock the props out from under the plan. A party must seek a stay to show diligence but need not obtain a stay to defeat a mootness ruling, as equity requires diligence, not success. In this case, though the plan had been substantially consummated, the appellant diligently sought a stay from the bankruptcy and district courts, and a ruling affecting the manager's authority only as to future stays would neither adversely affect innocent third parties nor undermine the plan. Therefore, the appeal is not moot. *Rev Op Group v. ML Manager LLC (In re Mortgages Ltd.)*, 771 F.3d 623 (9th Cir. 2014).

### 11.4 Sovereign Immunity

## 12. PROPERTY OF THE ESTATE

### 12.1 Property of the Estate

### 12.2 Turnover

### 12.3 Sales

## 13. TRUSTEES, COMMITTEES, AND PROFESSIONALS

### 13.1 Trustees

### 13.2 Attorneys

**13.2.a. Court denies compensation for services rendered before an employment application and after confirmation.** Counsel represented the LLC debtor and debtor in possession in its chapter 11 case

and its two individual principals in their later-filed chapter 13 cases. Due to inadvertence, he filed his employment application in the LLC case five weeks after the petition date. Some of his legal services involved both substantive consolidation and dischargeability issues for the individuals in connection with plan negotiations. The court denied substantive consolidation. Ultimately, the court confirmed a creditors' plan that vested all estate assets in the creditors and in a liquidating trust. After the effective date, counsel performed services on behalf of the debtor that the plan required for its implementation. Section 330 permits the court to award compensation to a professional employed under section 327. An employment application may be granted *post facto* only in extraordinary circumstances. Inadvertence does not amount to extraordinary circumstances, so the court may not grant his employment retroactively for the five-week immediate postpetition period. Accordingly, he was not "employed" under section 327 during that period, so section 330 does not permit allowance of his compensation for that period. For the period during which counsel was employed, the court may award compensation if the services are necessary and benefit the estate, both measured as of the time the services are rendered. Benefit may derive from promoting the bankruptcy process and estate administration, even if counsel's position is not ultimately successful or does not result in confirmation of his client's plan. Therefore, counsel may be compensated for services related to consolidation and dischargeability. Section 330 permits compensation only for counsel for the trustee or debtor in possession. Vesting of the estate's assets upon the plan's effective date terminates the estate. After that, counsel's services are not for the estate or for the benefit of the estate. Therefore, the court disallows compensation for post-effective date services, even though the plan required the debtor's actions to carry out the plan. *Rose Hill Bank v. Mark J. Lazzo, P.A. (In re Schupach Investments, LLC)*, ___ B.R. ___, 2014 Bankr. LEXIS 4936 (10th Cir. B.A.P. Nov. 25, 2014).

### 13.3 Committees

**13.3.a. Committee members do not have standing to sue a committee professional.** The debtor confirmed a plan that provided for a sale to an unrelated entity. The price was to be paid in four installments, secured by a lien, with the sale proceeds paid to unsecured creditors. Debtor's counsel failed to file a financing statement to perfect the lien. The buyer defaulted. The unperfected lien resulted in a lower recovery than otherwise would have been the case. The creditors committee sued its counsel in state court for malpractice for failing to ensure that the lien was properly perfected. The chapter case was reopened and converted to chapter 7, dissolving the committee. The committee members substituted as plaintiffs. A chapter 11 committee professional represents the committee, not its members, and the professional's duty runs solely to the committee. Therefore, the committee members lacked standing to sue the committee's counsel. *Schultze v. Chandler*, 765 F.3d 945 (9th Cir. 2014).

### 13.4 Other Professionals

### 13.5 United States Trustees

## 14. TAXES

**14.1.a. Tax attributes of disregarded entity are not property of the debtor or the estate.** The single-member LLC debtor incurred losses for four years before bankruptcy. The debtor was a disregarded entity for tax purposes. Its parent corporation applied the debtor's tax losses in the parent's tax return, creating a tax benefit for the parent. After bankruptcy, the trustee sought turnover and recovery from the parent under sections 542 and 549. A disregarded entity does not have a separate existence for purposes of the Internal Revenue Code; its taxpayer parent is treated as owning all the entity's assets and owing all the entity's liability. Therefore, any tax benefit that the debtor generated was not property of the debtor or the estate, so the trustee may not obtain turnover from the parent, and there was no transfer that the trustee could avoid and recover. *Stanziale v. CopperCom, Inc. (In re Conex Holdings, LLC)*, 518 B.R. 792 (Bankr. D. Del. 2014).

## 15. CHAPTER 15—CROSS-BORDER INSOLVENCIES

**15.1.a. Court enforces Brazilian confirmation order.** The Brazilian debtors confirmed a reorganization plan under Brazilian bankruptcy law. The plan provided 25% recoveries to U.S. and non-U.S. holders of U.S. dollar-denominated bonds but higher recoveries to holders of other claims against the debtors, based on a deemed consolidation of the Brazilian debtors for distribution purposes. The foreign representative sought enforcement of the plan in the U.S. Holders of 37% of the U.S. bonds objected. Section 1521(a) permits a court to grant appropriate relief to a foreign representative, including staying U.S. enforcement actions, subject to any conditions it deems appropriate, and only if the debtor's and creditors' interests are sufficiently protected. The court may also grant additional assistance to a foreign representative under section 1507(a), consistent with comity principles, considering whether the additional relief will reasonably assure just treatment of creditors, protection of U.S. claim holders against prejudice and inconvenience in prosecuting claims in the foreign proceeding, prevention of preferential or fraudulent transfers, and distributions substantially in accordance with the Bankruptcy Code. Section 1507 relief is available only if section 1521 relief is unavailable or inadequate. Relief is discretionary with the court. Relief is not available, however, if it would be manifestly contrary to U.S. public policy, which is narrowly defined. An order enforcing a foreign proceeding confirmation order is available under section 1521(a). In this case, the debtors' and creditors' interests are sufficiently protected, because the Brazilian confirmation order permits reorganization and creditor distributions, even though holders of a minority of U.S. bonds found the distribution unsatisfactory. Denying enforcement would scuttle the plan and allow the minority to negotiate for a more favorable recovery without any evidence that any such effort would be successful. Therefore, the court grants enforcement. *In re Rede Energia S.A.*, 515 B.R. 69 (Bankr. S.D.N.Y. 2014).