Bankruptcy Case Law Update Materials

Case interpreting effect of Supreme Court's MOAC decision on 363(m)
In the Matter of Fieldwood Energy LLC, 2024 WL 686207 (5th Cir. 2024) - In this case, the Fifth Circuit stated that it perceived no narrowing of the effect of Section 363(m) by the Supreme Court's decision in *MOAC Mall Holdings, LLC v. Transform Holdco LLC*, 598 U.S. 288, 299 (2023) (which generally held that section 363(m) was not jurisdictional), other than to clarify that a party can lose the benefit of its terms by forfeiture, waiver or the like. "[T]he Supreme Court's recent explanation that the provision 'plainly contemplates that appellate courts might 'revers[e] or modif[y]' any covered authorization,' but that authority is limited because 'the reversal or modification of a covered authorization may not 'affect the validity of a sale or lease under such authorization.'" *Matter of Fieldwood Energy LLC*, 2024 WL 686207, at *5 (5th Cir. Feb. 20, 2024) (*quoting MOAC Mall*, 598 U.S. at 299 (*quoting* 11 U.S.C. § 363(m)).

No absolute right to dismiss after Chapter 13 case converted to Chapter 7
In re Pino, 2024 WL 1059074 (BAP 10th Cir. 2024) (not yet published) - Tenth Circuit Bankruptcy Appellate Panel affirmed the Bankruptcy Court's holding that the debtor in a case converted from Chapter 13 to 7 does not have an absolute right to dismiss the case after conversion. While 11 U.S.C § 1307(b) is unambiguous and provides a Chapter 13 debtor with an absolute right to dismissal, the Court held that Chapter 13 provisions do not hold sway after a case is converted from Chapter 13 to 7. The Bankruptcy Code is clear that provisions in Chapter 13 of the Code (like 11 U.S.C § 1307(b)) do not apply to a case that is in or converted to Chapter 7. *Id.* at *270.

Derivative Standing of Liquidating Trustee Upheld
In re X-Treme Bullets, Inc., 2024 WL 837043 (9th Cir. 2024) (not for publication) - The Bankruptcy Court dismissed a Liquidating Trustee's avoidance action on the ground that he lacked standing to pursue the claim that was originally brought by the Creditor's Committee and then transferred to the Liquidating Trust, with the approval of the Bankruptcy Court and as permitted by the Bankruptcy Code. The District Court reversed and the Ninth Circuit affirmed the District Court, noting that the Debtor granted derivative standing to the Committee, which the Bankruptcy Court approved. As a result, the Committee was not required to establish Article III standing; "The Committee 'filed suit ... on behalf of the estate,' and '[c]onsequently ... assert[ed] derivative standing[,]' obviating the requirement that the Committee demonstrate Article III standing 'in its own right.'" (internal citations omitted). The Ninth Circuit found support for its ruling in 11 U.S.C. § 1103(a)(5), which provides that a committee may "perform such other services as are in the interest of those represented." *Id.* at *1-2.

Tax Sale Certificate Foreclosure as Taking
Tyler v. Hennepin County, 598 U.S. 631 (2023) - Plaintiff had accumulated approximately $15,000 in unpaid real estate taxes along with interest and penalties. Hennepin County seized the Plaintiff's condo and sold it for $40,000, keeping the $25,000 excess over Tyler's tax debt for itself. Tyler filed suit, alleging that the County had unconstitutionally retained the excess value of her home above her tax debt in violation of the Takings Clause of the Fifth Amendment and the Excessive Fines Clause of the Eighth Amendment. The Supreme Court found that the

County's retention of the excess value of her home above her tax debt violated the Takings Clause of the Federal Constitution. *Id.* at 634-36, 647-48.
257-261 20th Ave. Realty, LLC v. Roberto, 477 N.J. Super. 339 (App. Div. 2023) - In a private tax sale foreclosure case, the Appellate Division addressed whether the United States Supreme Court's recent decision in *Tyler v. Hennepin County*, 598 U.S. 631 (2023), which declared a taxing authority's confiscation of a property owner's equity violated the Fifth Amendment Takings Clause, bars a third-party tax sale certificate holder's foreclosure of a property owner's equity under the New Jersey Tax Sale Law (TSL), N.J.S.A. 54:5-1 to -137. The Appellate Division found that the application of Tyler to New Jersey's similar TSL framework establishes that the confiscation of a New Jersey property owner's equity, through a tax sale foreclosure, violates the Fifth Amendment Takings Clause. *Id*. at 349, 355-67.

Cases regarding whether an asset's appreciation postpeition belong to debtor or is part of the Bankuptucy Estate after conversion from Chapter 13 to 7
In re Goetz, 2024 WL 998765 (8th Cir. March 8, 2024) - Affirming the Bankruptcy Court and BAP, Eighth Circuit held that under the plain language of the Bankruptcy Code, the postpetition, preconversion increase in equity in debtor's residence resulting from market appreciation and payments toward mortgage lien became property of the converted bankruptcy estate in a case converted from Chapter 13 to 7 as "[p]roceeds ... of or from property of the estate[,]" under 11 U.S.C. § 541(a)(6). *Id.* at *589.

Matter of Castleman, 75 F.4th 1052 (9th Cir. 2023), *cert. denied sub nom. Castleman v. Burman*, 2024 WL 674785 (U.S. Feb. 20, 2024) - Affirming the Bankruptcy and District Courts, in a matter of first impression for that Court, the Ninth Circuit found "that the plain language of § 348(f)(1)(A), coupled with this circuit's previous interpretation of § 541(a), compel the conclusion that any appreciation in the property value and corresponding increase in equity belongs to the estate upon conversion[from Chapter 13 to 7;]"; however, the dissenting opinion argued that "Congress believed that home equity which accrued during Chapter 13 proceedings should not be included in the converted estate." *Id.* at 1055, 1063.
In re Barrera, 22 F.4th 1217 (10th Cir. 2022) - Tenth Circuit held that "[t]he most faithful reading of the statutory text supports the conclusion that the proceeds from the sale of the Debtors' house belong to the Debtors, not the Chapter 7 estate[,]" and affirming the Bankruptcy Court and BAP's outcome but using a different rationale: the lower Courts determined that the statutory language is ambiguous and pivoted to legislative history, but the Tenth Circuit stated that the "Trustee's view that the post-confirmation proceeds from the sale of the Debtors' house became property of the estate ignores § 1327(b) 's revestment provision. At the time the Debtors sold their house, the Debtors' Chapter 13 plan had been confirmed and the house had been revested in the Debtors. As a result, the Debtors' house was not property of the Chapter 13 estate when the Debtors sold it. The proceeds generated from the sale of the house were therefore not 'proceeds ... of or from property of the estate.'" (internal citations omitted). *Id.* at 1224, 1226.

In re Montenegro, 655 B.R. 607 (2023) - Addressing whether a Chapter 13 debtor who sought to refinance the debt on non-exempt real property for significantly more than the secured debt determined by a valuation order entered early in the case can use the new loan proceeds to pay the secured and unsecured plan obligations early and keep any remaining proceeds [i.e., no conversion], the Bankruptcy Court stated it "agrees with courts that hold a debtor is entitled to the appreciated value upon conversion[,]" and later noting that "the Circuits are split over who

gets the appreciation in real property when a Chapter 13 converts to Chapter 7. *Id.* at 608-09, 612.

Postpetition asset appreciation ownership in Chapter 13 cases without conversion
In re Elassal, 654 B.R. 434 (Bankr. E.D. Mich. 2023) - Chapter 13 debtor sought court approval to use proceeds from post-confirmation sale of home, which had significantly appreciated post confirmation, to purchase a new residence for cash, while making her promised dividend to unsecured creditors over the remainder of her plan. The Trustee objected and filed proposed plan modification whereby debtor would keep what remained of proceeds after unsecured claimants received full payment. The Court found that the debtor's home vested in her at confirmation and "the sale proceeds, derived from post confirmation appreciation of Debtor's pre-petition real property, cannot be untethered from the real property itself, and do not refill the estate." Choosing the estate replenishment theory among existing judicial theories, the Bankruptcy Court wrote: "The Sale Proceeds are the Debtor's property pursuant to 1327, cannot be separated from the underlying real estate, and according to the Supreme Court '[c]hapter 13 debtors are permitted to keep their property.' [*Hamilton v. Lanning*, 560 U.S. 505, 508 (2010).] Not only does [d]ebtor receive the benefit of the bargain struck with her creditors—without the benefit of foresight—but she also receives the fortified protections of section 1327 because the appreciation generating the Sale Proceeds arose post-confirmation. Consequently, the Sale Proceeds will not refill the bankruptcy estate." *Id.* at 443 *citing* with approval *In re Larzelere*, 633 B.R. 677 (Bankr. D. N.J. 2021) and *In re: Maynor*, 2023 WL 9102137 (Bankr. E.D.N.C. Nov. 27, 2023) (not yet published) (same: adopting the 'estate replenishment' approach).

Dischargeability of certain student loans
In re Kurz, 660 F. Supp. 3d 1046 (D. Colo. 2023) - Debtor, who was a physician, was as a participant in Colorado Health Service Corps. As part of the program, the Debtor had agreed to work in a medically underserved area of state in exchange for the state's repayment of his existing medical education student loans. When he failed to fulfill the service requirements set forth in the loan repayment contract, the Colorado Department of Public Health and Environment sought a determination under 11 U.S.C. § 523(a)(8) that the debt arising from his failure to fulfill his contract was dischargeable. On issues of apparent first impression, the District Court held that: 1) the debt was not nondischargeable as a "refinance" of otherwise qualified education loans, and 2) the debt was not nondischargeable as an "educational benefit." *Id.* at 1048-49, 1051-58.

[Whether certain retirement accounts are exempt assets
McDonnell v. Gilbert, 612 B.R. 687 (Bankr. D.N.J 2022) - This case addresses the split in authority after the Supreme Court's decision in *Patterson v. Shumate*, 504 U.S. 753 (1992). In his schedules, the Debtor claimed an exemption for two retirements accounts (a 401A account with a balance of $1.6M and a 401K account with a balance of $47K) but then later argued that the retirement accounts were excluded from property of the bankruptcy estate pursuant to 11 U.S.C. § 541(c)(2). The District Court affirmed the bankruptcy court's finding that if nonbankruptcy law provides a restriction on transfer, ERISA in that case, then the retirement accounts did not need to be both ERISA qualified and tax qualified under the Internal Revenue Code. Following *Patterson*, the caselaw in this area has broken down along two lines: those that

find that a retirement plan must not only contain the anti-alienation provisions required by ERISA, but must also comply with all tax regulations, and those that find that compliance with ERISA's anti-alienation requirements is sufficient. In other words, does the term “ERISAqualified,” as used by the Supreme Court in Patterson mean “tax-qualified.” The bankruptcy court, relying primarily on a plain reading of the relevant Code section, found that ERISA's antialienation requirements are sufficient to provide the required restriction on transfer and that a retirement account does not also need to comply with all of the requirements of the Internal Revenue Code to be excluded from property of the estate. *Id.* at 689, 693-98.**]**

Debts in Corporate Sub V Can be Nondischargeable
Avion Funding LLC v. GFS Industries LLC (In re GFS Industries LLC), 25-50237 (5th Cir. April 17, 2024) - On a direct appeal from the Bankruptcy Court, the Fifth Circuit reversed the lower court and held that debts of corporate debtors in Subchapter V of chapter 11 can be nondischargeable under Section 523(a) in nonconsensual plans. In so holding, The Fifth Circuit agreed with the Fourth Circuit (and disagreed with at least eight lower courts that held otherwise) and determined that the Debtor’s “plan was confirmed as a nonconsensual plan under § 1191(b), [ ] the dischargeability of its debts is governed by § 1192." The Court reasoned that “placing controlling weight” on the word “‘individual’ in § 523(a) disregards the plain language of § 1192(2)" as section 1192 deals with the discharge of debts of a “debtor,” and the word “debtor” in Subchapter V refers to “a person.” In turn, “person” is defined in Section 101(41) to mean both an individual and a corporation. For Judge Duncan, “the most natural reading of § 1192(2) is that it subjects both corporate and individual Subchapter V debtors to the categories of debt discharge exceptions listed in § 523(a).” Id. at 4, 6-7.

<u>Earmarking Defense and Imputing Fraudulent Intent</u>
***In re: Cyber Litigation, Inc., et. al.*, 20-12702-CTG, Adv. Nos. 22-50439, 22-50441, 22-50443 (Bankr. D. Delaware, October 19, 2023)**
Debtor was a cyber fraud prevention company. Five months pre-petition, Debtor’s board voted to make and did make a tender offer using new investor funds to repurchase $72 million in outstanding stock from existing shareholders, which included Adam Rogas, Debtor’s CEO and founder. The transaction was revealed to be based in fraud: Rogas had fabricated Debtor’s financial records from the beginning for the purpose of defrauding investors, and what was essentially a Ponzi scheme collapsed. Debtor filed Chapter 11, and a Cyber Litigation Trust was formed. The Trustee filed adversary proceedings against the recipients of the tender offer funds, which included Rogas and three LLCs owned by Rogas.
The Trustee claimed that the tender offer was a fraudulent conveyance, because the funds were transferred in exchange for worthless shares. Further, the transfer was made with fraudulent intent. The Trustee also claimed unjust enrichment.
The Defendants asserted four defenses: 1) the funds were earmarked and therefore not estate property; 2) Rogas’ fraudulent intent could not be attributed to the Board, and the majority of the board members lacked fraudulent intent; 3) the safe harbor provision of Section 546(e) protected them; and 4) unjust enrichment is not applicable because Debtor was contractually obligated to make the tender offer.
The Court granted summary judgment in the Trustee’s favor. It did not reach the safe harbor or unjust enrichment arguments; they were rendered moot, because the earmarking and intent defenses failed.

Specifically, the court found that:

1. Rogas' intent to defraud was imputed to Debtor even though the majority of the board did not have fraudulent intent. The Court recognized that Rogas deceived the board and that the majority of the board lacked fraudulent intent. The Court further recognized that, under Delaware law, the "intent" of a board is the intent of the majority of its members.

   However, the Court found that Rogas' fraud was the direct cause of the board's decision with no break in the causal chain. The board's decision was based upon reports of various professionals, and those reports all relied upon the information Rogas falsified. Rogas was the only person with access to Debtor's financial accounts. The chain can be broken by the introduction of new information that is not the "fruit of deception"; here, no decision was made that was not based upon Rogas' misrepresentations. As the Court explained, "the line between Rogas' intent to defraud creditors and the debtor's decision to purchase its shares in the tender offer is as straight as an arrow." No decision was made independent of the improper motive, and so Rogas' fraudulent intent was imputed to Debtor.
2. The funds were not earmarked and therefore, they were estate property. The earmarking doctrine provides that when a debtor is in possession of funds it received from a third party, and that party directed the debtor to use those funds in a particular manner, the funds are "earmarked" and are not estate property subject to an avoidance action. Here, the Court specified that earmarking is only present if Debtor were legally obligated to use the funds for the tender offer, and that was not the case. The Stock Purchase Agreement, in fact, required Debtor to repurchase up to a certain amount of shares, providing a ceiling but not a floor. The Court found that this gave Debtor discretion, and so the funds were not earmarked.

The Court avoided the transfers and disallowed the claims under Section 502 until repaid to the estate.
Rogas pled guilty to securities fraud in 2022 and is in prison until 2027.

Debt Collection vs. Debt Servicing – FDCPA and Proof of Claim
***Petro v. Lundquist Consulting, Inc.*, No. 22-3051 (3rd Cir., February 7, 2024) (Not Precedential)**
Pennsylvania's Consumer Discount Company Act ("CDCA") protects borrowers from usurious interest rates on small loans such that "small dollar lenders" may not charge more than 6% interest. A "lender" is an entity "in the business of negotiating or making loans or advances of money on credit". The CDCA also requires these "small dollar lenders" to obtain a license, and it prohibits CDCA-licensed lenders from selling their contracts to an unlicensed person or entity.
The appellee, Lundquist Consulting, Inc. ("LCI") is a debt collector. The appellant, Robert Petro ("Debtor"), owed a debt to a CDCA-licensed lender, which lender charged off the loan after default. The charged-off debt was sold twice, and the eventual holder hired LCI to collect the debt.
Debtor filed a bankruptcy case, and LCI filed a proof of claim. Debtor sued LCI for FDCPA violations, averring that the proof of claim filing was unlawful because the underlying debt originated with a CDCA-licensed lender who sold the loan to an unlicensed third party in violation of the CDCA. The District Court ruled granted judgment on the pleadings in favor of LCI. Debtor appealed to the Third Circuit.

In its non-precedential opinion, the Third Circuit noted that Debtor's FDCPA claim was based upon "a false, deceptive or misleading representation" and/or "unfair or unconscionable means" in connection with debt collection.

The Third Circuit ruled that the CDCA regulates credit, not debt collection, and that debt buyers and debt collectors are not subject to the CDCA's strictures. The Court found that LCI is a debt collector and is not in the business of lending. The purchasers of the obligation were debt buyers and not in the business of lending. Finally, the CDCA prohibits lenders from selling CDCA-authorized contracts to unlicensed third parties; however, a charged-off debt is not a "contract", and so selling such an obligation is the sale of a debt, not the sale of a contract.

Therefore, the CDCA did not apply, and the District Court's decision was affirmed.

<u>363 Sale of Avoidance Actions</u> (2 cases)

***In re Simply Essentials, LLC*, 78 F.4th 1006 (8th Cir. 2023)**

Simply Essentials, LLC ("Debtor") was pushed into an involuntary Chapter 7 case. The Chapter 7 Trustee determined that the Estate did not have sufficient funds to pursue numerous avoidance actions. Rather than leave money on the table, the Trustee auctioned off the avoidance actions and moved to approve the compromise and sale. The losing bidder, Pitman Farms ("Pitman") appealed, arguing that an avoidance action cannot be sold as estate property.

Pitman argued that the avoidance actions are not property of a bankruptcy debtor but are property of a creditor or a trustee. The Eighth Circuit ruled that avoidance actions are for the benefit of the estate and are therefore estate property, because "property of the estate" is "broadly defined".

The Court also ruled that there is no requirement for a debtor to have a possessory interest in property for such property to be estate property. Debtor had an inchoate interest in the actions pre-petition, because Debtor had the right to file bankruptcy, and a trustee would have the right to avoid them, and so they're estate property under 11 U.S.C. § 541(a)(1).

Further, even if that were not the case, Section 541(a)(7) includes interests acquired by the estate post-petition.

Pitman argued 1) that a ruling against it would create surplusage, as Section 541(a)(6) provides that proceeds of estate property are also estate property, but the Code specifies elsewhere that proceeds of avoidance actions are estate property; and 2) that such a ruling would undermine the purpose of avoidance actions and violate the Trustee's fiduciary duty.

The Court dismissed the surplusage argument on the grounds that it is "not unreasonable that Congress would repeat itself in order to ensure the results it intended were followed" and redundancies in statutes are not uncommon.

Regarding the Trustee's duty and the purpose of avoidance actions, the Court opined that the Trustee's duty is to maximize the Estate, and by selling the avoidance actions the Estate could not afford to litigate, the Trustee <u>did</u> maximize the estate.

The Court referenced *In re Cybergenics Corp.*, 226 F.3d 237 (3rd Cir. 2000), which held that avoidance actions are not property of the <u>debtor</u>, but which stressed that the debtor's assets and the estate's assets have different meanings; further, the subsequent Third Circuit case of *In re Wilton Armetale, Inc.*, 968 F.3d 273 (3rd Cir. 2020) stressed that *Cybergenics* does not prohibit a trustee from transferring causes of action.

***In re South Coast Supply Co.*, No. 22-20536 (5th Cir., January 22, 2024)**

South Coast Supply Co. ("Debtor") filed a preference action as debtor-in-possession against its former CFO, Robert W. Remmert ("Remmert"), seeking to avoid and recover transfers of more than $300,000. After litigation over the Chapter 11 plan with Briar Capital Working Fund Capital, LLC ("Briar") for payment of its claim, the Plan was ultimately confirmed with an assignment of the preference action from Debtor to Briar. Briar was substituted into the preference action as Plaintiff, and Remmert moved to dismiss after three years of litigation, arguing that Briar lacked standing. The District Court agreed and dismissed the suit.

The Fifth Circuit reversed. Following *Simply Essentials* and other cases from other circuits, the Court agreed that avoidance actions are estate property. Remmert argued that regardless, Briar is not a "representative of the estate" under 11 U.S.C. § 1123(b)(3)(B) and so still lacked standing. The Court found that fact irrelevant, because the purchaser of estate assets need not be a

representative of the estate. Because the cause of action is an asset that can be sold, the purchaser has standing to pursue it.

In re Mullins, 2023 WL 6884254 (Bankr. E.D.Mich. October 18, 2023)

In a joint case, the Debtor husband died before being able to take the instructional course for financial management. A Motion was filed seeking to excuse him from compliance with this pre-discharge obligation. The Motion did not make clear how the movant had standing. The Court made it clear that the lawyer did not have the right to make the motion without the directive from the Debtor's personal representative appointed in his estate and it was not clear that the co-debtor was, in fact, the authorized representative of the estate.

Note the new proposed Rule in the District.

D.N.J. LBR 1016-1. Death or Finding of Incompetency of a Debtor

Within 30 days of learning of (i) the death, or (ii) a finding of incompetency of a debtor through appropriate legal process, debtor's counsel must file Local Form *Notice of Death or Finding of Incompetency of a Debtor*. Debtor's counsel must also separately file the certificate of death or the court order pertaining to incompetency or guardianship. The certificate of death or court order pertaining to incompetency or guardianship will be immediately restricted from public viewing by the clerk's office without the necessity of a motion under these Rules. In the case of a self-represented debtor, any person who becomes aware of a debtor's death or incompetency may also file said Local Form and the certificate of death or court order pertaining to incompetency or guardianship. Any relief related to the death or incompetency of a debtor must be requested by separate motion.

2024 Comment

This Rule is amended to include the requirements for filing a certificate of death or court order pertaining to incompetency or guardianship.

In re Hicks, 653 B.R. 562 (Bankr. ND Ill, August 31, 2023)
Chapter 7 Trustee filed his Final Report in a surplus case seeking to pay all creditors interest on their allowed claims at the federal judgment rate of 0.1% rather than the Illinois statutory judgment rate of 9%. The City of Chicago as creditor objected to the interest rate being paid on its claim. The Court followed 7th Circuit and Supreme Court pre-bankruptcy code precedent finding that the adoption of the Bankruptcy Code did not abrogate the "solvent" debtor rule whereby creditors of a solvent estate are entitled to be paid the state statutory interest rate. The case is a detailed analysis of statutory construction, overrules the US Trustee position and creates a direct conflict with the 9th Circuit decision in *Onink v. Cardelucci (In re Cardlucci)*, 285 F.3d 1231 (9th Cir. 2002).

Swift, Liquidation Trustee v. Halimi (In re CL H Winddown, LLC), 2023 WL 5740195 (Bankr. D.Del. September 5, 2023)

Trustee filed a preference complaint against defendant for transactions outside the 90 day period. The ability to continue hinged on the status of the defendant as an "insider"; he was identified as an "insider" on the Debtor's Statement of Financial Affairs, but the Trustee faced a Motion to Dismiss regardless. The Defendant lent money to the Debtor pursuant to three promissory notes. Between April 9 and November 3, 2020, the Debtor paid the Defendant $2.714,833.34 which satisfied the second and third notes; a Chapter 11 petition bankruptcy was filed on March 8, 2021. A Plan was confirmed on September 20, 2021. This suit was brought by the liquidating trust. The Defendant does not fit the definition in the Bankruptcy Code of an insider. The Court found that to be a non-statutory insider there must be "a close relationship" and the transaction "was not conducted at arm's length." The Court cited to the definition from *Burtch v. Opus, LLC (In re Opus East, LLC)* 528 B.R. 30, 93 (Bankr. D.Del. 2015). The Court then reviewed the complaint and determined that the complaint did not allege that the loans were on terms that reflected *other than* an arm's length transaction. The Court noted that the complaint was *silent* on this issue; the Court had no facts on which to find that the Trustee met this standard. Since the preference complaint failed, the Court noted that there was an alternative theory of recovery, i.e., a fraudulent transfer claim. The problem with that count was a that since the payments were made in satisfaction of the signed promissory notes, the overwhelming body of case law says that the transfer is made for value, defeating the basic premise of a fraudulent transfer claim. Finally, the Court considered the Trustee's request for the opportunity to amend the complaint. The Trustee did not identify how she intended to amend the complaint and/or provide a draft second amended complaint. Under these circumstances, the Court did not believe that a right to amend was triggered.

Miller v. United States, 71 F.4th 1247 (10th Cir. 2024)
Section 106 of the Bankruptcy Code specifically abrogates sovereign immunity as to a governmental unit with regard to actions brought under, among other things, section 544. That seemed pretty clear until a Chapter 7 Trustee in a converted Chapter 11 pursued the Internal Revenue Service (the "IRS") for payments made by the Debtor on behalf of and for the benefit of the Debtor's principals totaling over $145,000. The Trustee was applying Utah's fraudulent transfer act, through the application of section 544. In the face of what would appear to be a clear path to recovery, the IRS contended that since 544 required that the Trustee "stand in the shoes" of a general creditor, it had a complete defense. In sum, since the *general creditor* itself would not be able to proceed against the IRS under state law (outside of bankruptcy) because of sovereign immunity, the Trustee, cloaked in that creditor's rights also could not.
On cross-motions for summary judgment, the bankruptcy court ruled in favor of the Trustee which was affirmed by the District Court. The Tenth Circuit undertook a painstaking statutory construction and determined that the government's position was circular, i.e., if Congress abrogated sovereign immunity for state law fraudulent transfer claims brought under 544(b)(1), it certainly understood that these claims would not have been brought by a general creditor outside of a bankruptcy context. As a result, it must have been Congress' intention to allow these claims to proceed.
This opinion is another vote in an on-going split among the Circuits. Here, the Tenth Circuit joins the Ninth Circuit (in *In re DBSI, Inc.*, 869 F.3d 1044 (9th Cir. 2017)) by holding for the Trustee and, in doing so, opposing the Seventh Circuit's decision in *In re Equip. Acquisition Res., Inc.*, 742 F.3d 743 (7th Cir. 2014)

Payments to a Trustee in a Subchapter V case
In re: Deborah A. Rose (Bankr. D. Ore. 2024).

This case involved a Subchapter V Trustee's motion for an order requiring the Debtor to post a retainer for the Trustee's fees and expenses. The judge withheld a final decision until the Trustee provided service on all creditors and the remaining creditors had an opportunity to be heard.

One of the issues that the court addressed was whether Section 1184 divests a subchapter V trustee from the power to use Section 363(b). The court determined that Section 1184 does not say that the debtor in possession has exclusive use to the rights and powers of the Bankruptcy Code and consequently and that the subchapter V trustee "may use the trustee's rights and powers under the Bankruptcy Code to the extent it is necessary for a subchapter V trustee to fulfill the statutory duties given to the subchapter V trustees in section 1183."

In this case, the Subchapter V Trustee was seeking the payment of $7,500 in funds outside of the ordinary course of business for the payment of his fees. The court determined, that although the fee request was reasonable. he was not entitled to a retainer that insured to his benefit to the exclusion of other administrative claimants. The Court held, "any use of funds outside the ordinary course of business should be provided for the benefit of all administrative claimant equally, and no single out the Subchapter V Trustee for more favorable treatment." IN this case, the Subchapter V Trustee was seeding a retainer to insure payment, not payment in the ordinary course. IN this case there were no other administrative claimants, and if, after service of the motion, none of the previously unserved creditors failed to make timely objections, the court would approve the requested $7,500 retainer.

Subchapter V grounds for extending the the deadline for filing a plan.
In re: Signia, LTD (Case No. 23-14384 (Bankr. D. Colo. 2024) (2024 WL 331967

In the court's prefatory remarks, the judge opined about the merits of a Subchapter V reorganization. The repeated theme of this opinion is that Subchapter V reorganizations are to proceed quickly. The court observed that the debtors and attorneys rarely met the 90-day mandate for the filing of a plan.

Although the 90-day mandate exists, the statute provides for extensions "attributable to circumstances for which the debtor should not justly be held accountable." (Section 1189(b)) The observed that attorneys by and large were merely paying "lip service" to the time requirements in the statute.

In the case before the court, the debtor filed its Chapter 11 Subchapter V. on September 27, 2023. Instead of filing its plan no later than December 27, 2023, the debtor requested a 44-day extension so that it could prosecuted its debtor-in-possession financing motion. No parties in interest objected to the request. Subsequently, the debtor-in -possession withdrew it financing motion but had still not filed its Subchapter V plan. The Court rejected the requested delay and issued its decision to "encourage debtor and their counsel to comply" with Section 1189 (b) by filing viable Subchapter V plans.

It is the Debtor's burden of proof to show grounds that justify an extension of time under Section 1189(b). The court determined that it is a higher standard that the mere "for cause" standard. It underlies the concept behind the very purpose of the Subchapter V. Generalized excuses for an extension will not suffice. The court then addressed the aspect of the statute that

referred to extensions "due to circumstances beyond the debtor's control." This would mean that there is a higher standard that the excusable neglect standard of Rule 9006(b)(1).

The court discussed the Equitable Balancing Standard and the Case-by-Case Approach utilized by several courts but determined that it would adhere to the "Beyond-the-Debtor's Control Standard for Section 1189(b) Requests." The court went on to say:

> *It means simply that the debtor should not be responsible for external events that the debtor did not cause. And, the corollary is that the debtor is responsible for the debtor's own conduct. This corresponds exactly with the Beyond-the-Debtor's-Control Standard. Extensions may be warranted for external events beyond a debtor's control which make it impossible for a debtor to file a timely plan.*

Based on the facts of this case, it should be no surprise that the Court denied the debtor's motion to extend.

Extension of statute of limitations by Bankruptcy Court
<u>In re: Ho Wan Kwok (Bankr. D. Conn. 2024) (2024 WL 1261803)</u>

An individual debtor filed a voluntary Chapter 11 petition that was jointly administered with two affiliated corporate Chapter 11 cases. The Court appointed a Trustee. The Trustee filed a Motion to Toll or Extend Statute of Limitations Deadlines that was disputed. The defendants raised objections that (i) the court lacked jurisdiction to determine this matter because the avoidance actions were private matters and therefor could only be determined by an Article III Court if the parties consented to jurisdiction; and (2) there was no case or controversy because no party had asserted a statute of limitations defense.

The Court determined that the extension of the statute of limitations is a matter of equity and is addressed in Sections 108(a), 546(a) and 549(d). The court held that the court must balance "the of the need or a trustee to determine and prosecute the estate's causes of action and the mandate to ensure the just, speedy, and inexpensive determination of every case and proceeding." The court also concluded that there was a present case or controversy because of the potential causes of action that the Trustee was pursuing but could not file before the two-year period expired.

The Court found, over objections, that Sections 108(a), 546(a) and 549(d) are subject to extension under principles of equity. The Court concluded that Rule 9006(b) could provide a mechanism to extend the statues of limitation set forth by Sections 108(a), 546(a), and 549(d).

As an aside, the debtors in the consolidated cases were recalcitrant and failed to comply with discovery demands on numerous occasions. The Court concluded that the Trustee had acted diligently in his pursuit of the Individual's financial affairs and recovery of assets.