CARRINGTON COLEMAN

The art of Law

CURRENT CASE LAW UPDATE: BUSINESS BANKRUPTCY

Northern District of Texas, Fifth Circuit, and Beyond

March 25, 2016

J. Michael Sutherland
Lisa M. Lucas
Carrington, Coleman, Sloman & Blumenthal, L.L.P.
901 Main Street, Suite 5500
Dallas, TX 75202
214-855-3000
msutherland@ccsb.com
llucas@ccsb.com

TABLE OF AUTHORITIES

<u>United States Supreme Court</u>

Wellness Int'l Network, Ltd. v. Sharif, 135 S. Ct. 1932 (2015)

<u>Key Issue</u>: Post-*Stern v. Marshall*, whether a Bankruptcy Court (as an Art. I court) has a proper delegation of authority from the District Court (as an Art. III court) to enter findings of fact and final orders on non-core issues upon the consent of the parties and, if so, whether consent must be express or may be implied?

<u>Holding</u>: In a 5/1/3 opinion, relying heavily on *Commodity Futures Trading Comm'n v. Schor*, 478 U. S. 833 (1986), the majority (Sotomayor, J.) held that "Article III is not violated when the parties knowingly and voluntarily consent to adjudication by a bankruptcy judge." *Id*. at 1939. In context, this statement refers to adjudication by the Bankruptcy Court of statutorily "non-core" matters and to those statutorily "core" matters where, under *Stern*, the delegation by the Art. III court was nonetheless held to be unconstitutional. "[T]he cases in which this Court has found a violation of a litigant's right to an Article III decision maker have involved an objecting defendant forced to litigate involuntarily before a non-Article III court. The Court has never [held] … that a litigant who has the right to an Article III court may not waive that right through his consent." *Id*. at 1947. That consent need not be express but may be implied whenever "the litigant or counsel was made aware of the need for consent and the right to refuse it, and still voluntarily appeared to try the case" before the non-Article III adjudicator." *Id*. at 1948, citing *Roell v. Withrow*, 538 U. S. 580, 588, n.5 (2003).

<u>Practice Impact</u>: In practice, we suspect that most experienced Bankruptcy Courts will, in most instances, clarify the parties' consent on the record early on in a given proceeding. Local rules may likely as well.

Baker Botts L.L.P. v. ASARCO, 135 S. Ct. 2158 (2015)

<u>Key Issue</u>: Are fees incurred in successfully defending against objections to a fee application recoverable from the Estate under 11 U.S.C. § 330(a)(1) or otherwise?

<u>Pertinent Facts</u>: Debtor's counsel, engaged under 11 U.S.C. § 327(a), represented the estate throughout the chapter 11 case, which concluded with the successful confirmation and implementation of a plan of reorganization. During the case, Debtor's counsel represented the Debtor in suing Debtor's parent corporation. A substantial judgment, worth between $7 and $10 billion, was obtained against the parent corporation. The confirmation process involved multiple competing plans and eventually became, in essence, a bidding competition. The parent corporation ultimately increased the consideration to be paid under its proposed plan to a point sufficient to pay all allowed claims in full with interest. The Bankruptcy Court then confirmed the parent's proposed competing plan. After implementation of that plan, the Reorganized Debtor, now controlled by the parent corporation, objected to the final fee application filed by the former Debtor's counsel. After extensive discovery and a 6-day trial on fees, the

Bankruptcy Court rejected the Reorganized Debtor's objections and awarded Debtor's former counsel approximately $120 million, plus a $4.1 million fee enhancement. Debtor's former counsel was also awarded over $5 million for time spent litigating in defense of the fee applications. The Reorganized Debtor appealed, and the principal issue before the Supreme Court was the recoverability of fees incurred in defending the fee applications.

Holding: Applying the "American Rule" – the rule that each side must pay its own attorney's fees absent explicit statutory authority to the contrary – the Supreme Court affirmed the Fifth Circuit in disallowing the award of defense costs. The Court ruled that the text of § 330(a)(1) does not "displace the American Rule with respect to fee-defense litigation." The Court did not determine (*see*, n.4) the potential applicability of sanctions under Rule 11, Fed. R. Civ. P., for frivolous fee objections.

Concurrence and Dissent: Justice Thomas wrote for a 5-1-3 majority. Justice Sotomayor concurred with the statutory analysis but declined to join the later discussion on policy considerations. Justice Breyer dissented, siding with arguments by the petitioners and others that compensation for fee-defense work should be properly viewed as part of the compensation for the underlying services in the bankruptcy proceeding.

Practice Impact: Numerous subsequent efforts, mostly in Delaware and the SDNY, to work around the majority holding and the application of the American Rule have, so far, been unsuccessful. (*See, e.g., In re Boomerang Tube, Inc.*, No. 15-11247, 2016 Bankr. LEXIS 273 (Bankr. D. Del. Jan. 29, 2016).) Bench and Bar alike may instead need to develop rules and practices aimed at the early prevention and the more economical handling of those objections of a tactical nature.

Husky International Electronics, Inc., v. Ritz, **(Case No. 15-145), 578 U.S. ___ , (May 16, 2016)**

Key Issue: Should the phrase, "actual fraud" in 11 U.S.C. § 523(a)(2)(A) be read narrowly, to require that a "false representation" be made, or broadly, so that fraudulent conveyances that do not entail a "false representation" per se may also serve as the basis for a determination of non-dischargeability?

Pertinent Facts: According to fact findings from the bankruptcy trial court, Dan Ritz caused Chrysalis, an entity in which he owned a significant interest, to make transfers to other entities in which Ritz owned varying percentages of ownership. Ritz was not a direct transferee. Husky International sold on credit to Chrysalis, but was not aware of the transfers and did not receive or rely upon any overt representations. Ritz and Chrysalis each filed chapter 7 cases in close proximity. Trustees were respectively appointed. No fraudulent transfer actions were brought in either Ritz's or Chrysalis's case to avoid the transfers. No objection to Ritz's general discharge was filed under 11 U.S.C. § 727. After Ritz's case was reopened, Husky sought to pierce the corporate veil as against Ritz to make him liable for its claims against Chrysalis and to determine such claims non-dischargeable as against Ritz under 11 U.S.C. § 523(a)(2) (and other subsections). Neither of the Chapter 7 Trustees challenged Husky's standing to pierce the corporate veil or assert veil piercing as an asset of Ritz's bankruptcy estate. By this time, the Chrysalis case was closed. (And compare *Highland Capital Mgmt. LP v. Chesapeake Energy Corp. (In re Seven Seas* Petroleum, Inc.), 522 F.3d 575 (5th Cir. 2008) with *S.I. Acquisition, Inc. v. Eastway Delivery Serv., Inc. (In re S.I. Acquisition, Inc.)*, 817 F.2d 1142 (5th Cir. 1987) to determine when alter ego rights belong exclusively to the bankruptcy estate versus when the rights of individual creditors may persist.)

An evidentiary trial ensued. Bankruptcy Judge Jeff Bohm in Houston found that Ritz had committed multiple, uncommendable acts and that Ritz's testimony was inconsistent and unreliable. Nonetheless, Judge Bohm found that Husky had not met the strict factual and legal burdens under the Texas statute for piercing the corporate veil. Moreover, because Ritz had made no misrepresentations to Husky and Husky did not rely on any false statements in connection with its decisions to sell on credit, the bankruptcy court likewise found that Husky's goods had not been "obtained by" fraud, as contemplated in Bankruptcy Code § 523(a)(2).

On appeal, the District Court found that Husky had established a veil piercing claim against Ritz, notwithstanding the strict requirements of the Texas statute, but affirmed the bankruptcy court's ruling that, absent a misrepresentation and reliance, the elements of non-dischargeability had not been met. It is not clear if Ritz preserved the veil piercing determination as a point of error from the District Court to the Fifth Circuit. However, the Fifth Circuit did not review veil piercing and affirmed the lower courts on dischargeability. The Supreme Court granted certiorari to resolve a Circuit split.

<u>Holding</u>: Justice Sotomayor, writing for the 7-1 majority, stated, "[t]he term 'actual fraud' in §523(a)(2)(A) encompasses forms of fraud, like fraudulent conveyance schemes, that can be effected without a false representation." The case was remanded to the Fifth Circuit for further determinations on the new standard. Justice Thomas dissented, reasoning that, "[t]he logical conclusion then is that 'actual fraud'—as it is used in the statute—covers only those situations in which some sort of fraudulent conduct caused the creditor to enter into a transaction with the debtor. A fraudulent transfer generally does not fit that mold, unless, perhaps, the fraudulent transferor and the fraudulent transferee conspired to fraudulently drain the assets of the creditor. But the fraudulent transfer here, like all but the rarest fraudulent transfers, did not trick the creditor into selling his goods to the buyer …"

<u>Practice Impact</u>: The Supreme Court holding was perhaps intended to be more limited than initially reported in some bankruptcy industry headlines. The Court did not hold, for example, that non-dischargeability will per se result upon the entry of a judgment avoiding a transfer only under "constructive fraud" provisions (such as 11 U.S.C. § 548(a)(2) or similar state statutes, typically requiring only that the transferor was insolvent or rendered insolvent by the transfer and that the transfer was not in exchange for "reasonably equivalent value" (or, under some state statutes, "fair value")). However, the Court conversely did not say that mere "constructive fraud" will never result in non-dischargeability.

The Court also did not expressly say that the "actual fraud" element of Bankruptcy Code § 523(a)(2) necessarily requires a finding of intent to commit fraud, such as the element of "intent to hinder, delay, or defraud creditors" under Bankruptcy Code § 548(a)(1). (Notably, however, there was an "intent to hinder, delay or defraud" finding against Ritz.) Even though the opinion stretches some boundaries of the traditional notions of fraud, one might suspect that later opinions may still identify "intent to defraud" in some form as a required element. The opinion does make it clear however, in addressing points made by the dissent, that an overt misrepresentation and overt, classic reliance on such misrepresentation are no longer required. Timing now also matters less – the party seeking non-dischargeability does not necessarily need to establish that its claim resulted from or was "traceable to" "fraud at the inception of a credit transaction."

As a result, the outer boundaries to the new standard for "actual fraud" remain unclear for now. Perhaps the intended take away is that, because the human imagination for creating novel forms of fraud often seems boundless, the parameters of the non-dischargeability remedy for "actual fraud" should also be more flexible. At least until illuminated by further case law, entrepreneurs struggling to manage their businesses through the shoals of financial distress and potential personal liability may need to be more circumspect than usual in deploying inter-company assets and cash across corporate lines, in compensating themselves and other owners, and in entertaining survival plans that may err towards the cutting edge.

FIFTH CIRCUIT COURT OF APPEALS

Barron & Newburger, P.C. v. Texas Skyline, Ltd. (In re Woerner), 783 F.3d 266 (5th Cir. 2015)

Key Issues: Within the Fifth Circuit, should the retrospective, "material benefit" standard first enunciated in *In re Pro–Snax Distributors, Inc.*, 157 F.3d 414 (5th Cir. 1998) continue to control the grant or denial of professional fees, or should that be replaced with a prospective, "reasonably likely to benefit the estate" standard similar to that followed in other circuits?

Holding: Sitting En Banc, the Fifth Circuit recognized that the retrospective, "material benefit" standard of *Pro–Snax* was in conflict with the language and legislative history of § 330 and that it diverged from the decisions of other circuits. Noting that *Pro-Snax* had "sown confusion in our circuit," the Fifth Circuit (Prado, J.) overturned *Pro–Snax*'s attorney's-fee rule and adopted instead the prospective, "reasonably likely to benefit the estate" standard. Under the new standard, as enunciated, services are compensable based on the necessity or reasonableness of legal services at the time they are rendered. If a fee applicant establishes that its services were "necessary to the administration" of a bankruptcy case or "reasonably likely to benefit" the bankruptcy estate "at the time at which [they were] rendered," the test is met. See 11 U.S.C. § 330(a)(3)(C), (4)(A).

Procedural History: The complicated procedural history of the underlying Bankruptcy Court case is not particularly germane to the holding. After the lower courts recognized that they were bound by the prior standard of *Pro-Snax*, the initial three-judge panel of the Fifth Circuit recommended rehearing by the full court. The ultimate holding was supported by prior, valiant efforts by lower courts within the Circuit to find a reasonable but compliant path through or around the strictures of *Pro-Snax*. *See, e.g.*, *In re Gadzooks, Inc.*, 352 B.R. 796, 798 (Bankr. N.D. Tex. 2006), *rev'd Kaye v. Hughes & Luce, LLP*, 2007 U.S. Dist. LEXIS 50929 (N.D. Tex. July 13, 2007); *In re Broughton Ltd. P'ship*, 474 B.R. 206, 209 n.5 (Bankr. N.D. Tex. 2012), and *Quisenberry v. Am. State Bank (In re Quisenberry)*, 295 B.R. 855, 861 (Bankr. N.D. Tex. 2003). The Office of the United States Trustee also filed a notable brief in the Fifth Circuit in support of the rehearing en banc and the ultimate result.

Practice Impact: Although liberating Fifth Circuit practitioners from the onerous and sometimes confusing retrospective standard of *Pro-Snax* and placing practitioners here on an even footing with those in other circuits, the new standard is no license for frivolity in any bankruptcy case. Synthesizing the new rule as enunciated in Judge Prado's opinion, Judge Jolly said, "A bankruptcy court's analysis of attorney fee awards ordinarily should begin and end by applying the statutory language in 11 U.S.C. § 330. This analysis usually can be reduced as follows: (1) a court is permitted, but not required, to award fees under § 330 for services that could reasonably be expected to provide an identifiable, material benefit to the estate at the time those services were performed (or contributed to the administration of the estate); and (2) courts may consider all other relevant equitable factors, as stated in § 330(a)(3), including as one of those factors, when appropriate, whether a professional service contributes to a successful outcome." Stressing the phrase "*not required*," Judge Jolly went on to caution that, "An identifiable benefit distinguishes an actual benefit from a speculative one, and a material benefit distinguishes a necessary benefit from an irrelevant one." Professionals will be well served to discern the import of Judge Jolly's concurrence.

Cantu v. Schmidt (In re Cantu), 784 F.3d 253 (5th Cir. 2015)

Pertinent Facts: This case was originally filed as a chapter 11, and later converted to chapter 7. Debtors (husband and wife) sued their bankruptcy attorney for her representation prior to the conversion of their case. Trustee asserted that the Estate owned any such cause of action. Before conversion, the chapter 11 case had been contentious and expensive. Debtor's counsel entered the case about a month after it had been filed and served as counsel for about 13 months, earning fees of just over $200,000, which were later approved by the Bankruptcy Court. Creditors moved for conversion, arguing the assets of the Estate were diminishing. Finding the proposed plan of reorganization was non-confirmable, the Bankruptcy Court granted conversion.

After conversion, objections to the Debtors' discharge were granted, based in part on the failure to disclose significant assets and unauthorized transfers during the pendency of the case. In a separate state court lawsuit, the Debtors sued their counsel, and the Trustee filed an intervention. That suit was settled and the proceeds were deposited into the court registry.

Catchy Line: "In bankruptcy, as in life, timing can be everything." – Circuit Judge Costa.

Holding & Rationale: Upholding the findings below that the cause of action accrued during the chapter 11 phase of the case, and not after conversion, the Fifth Circuit affirmed the determination that the Estate owned the cause of action. To "the extent *Swift*[1] and *Wheeler*[2]cannot be reconciled, *Swift*—which is consistent with the law in other circuits—is the earlier decision and thus governs under our rule of orderliness." Applying the *Swift* test and concluding that the attorney's alleged "misconduct injured the creditor body in a number of ways during the pendency of the chapter 11 bankruptcy that would have allowed the estate to file suit prior to conversion," the Estate was held to own the cause of action and hence the settlement proceeds.

Bearing in mind that no negligence findings were ever entered against the attorney (in the settled, state court case), the Court was then forced to assess when the cause of action accrued based on the mere allegations of negligence, which may or may not have occurred. These allegations included: counsel had failed to timely file a request for the use of cash collateral which supposedly led to Debtor's unauthorized use of cash collateral; such use for personal expenses depleted the Estate's assets; counsel failed to schedule the assets which the Debtors then improperly sold or transferred; that the foregoing made confirmation of a plan more difficult; and, as the "culmination … of misconduct," counsel submitted an unconfirmable plan (because, inter alia, it is said to have violated the absolute priority rule). The Fifth Circuit's holding was thus in part based on the conclusion that such acts and omissions also damaged the Estate and not just the Debtors.

Practice Impact: The "property of the Estate" holding is easy, and possibly of less import than the potential blow-back effect the discussion in this opinion may have for Debtor's counsel in future cases. Of course the reader cannot, simply on the face of the opinion, determine whether any alleged acts and omissions of Debtor's counsel were committed or were actionable. (Indeed, the "cost of defense" size of the settlement at issue tends to mitigate in favor of Debtor's counsel.) Instead, the entire issue is determined in a theoretical vacuum after what might have been a cost of defense settlement. Yet in that forced, theoretical analysis, the Debtors' own misconduct is laid at the feet of counsel and becomes a breach of professional duty proximately causing damage to the Estate. The practical impact of this of course is that Debtor's counsel in nearly every case – individual and corporate – should redouble efforts not only to ensure that Debtors are in fact thoroughly apprised of the requirements and restraints of bankruptcy, but that they also retain a paper trail to prove that they have done so. The further insinuation that it may be malpractice to file a plan that is later determined to be non-confirmable is disturbing. For example, it has been said that the absolute priority rule is never actually violated upon the filing of a plan, but only later after the unsecured class of creditors votes to reject that plan, and the Debtor declines to amend. There are

[1] *Swift v. Seidler (In re Swift*), 198 B.R. 927, 935–36 (Bankr. W.D. Tex. 1996) (Applied state law in determining when a cause of action had accrued.)

[2] *Wheeler* [*v. Magdovitz (In re Wheeler)*, 137 F.3d 299 (5th Cir. 1998) (per curiam) (Applied a "middle ground" or "prepetition relationship" approach in which "a claim arises at the time of the negligent conduct forming the basis for liability," even if no injury has yet occurred, so long as a prepetition relationship between debtor and claimant existed.)

times when such a plan is the only plan that Debtor's counsel is authorized by the client to file (at least in the first instance, to see if it will be accepted). Presumably the risks of that course of action are disclosed to the Debtor, as client. If so, the decision maker directing counsel at that time is still the Debtor and the fallout of making an informed choice should not equate to malpractice. And, of course, most plans that are eventually confirmed evolve over a course of time that can involve objections, responses, amendments, negotiations and compromises, although some counsel may be more able than others to thread that particular needle. If anything, that should simply go to determination of the attorney's fees under section 330 and the new standard recently articulated in *Barron & Newburger, P.C. v. Texas Skyline, Ltd. (In re Woerner)*, 783 F.3d 266 (5th Cir. 2015). Unfortunately, at least on a few fronts, the discussion in this section of the opinion could be read (for example, by state courts trying malpractice claims post-bankruptcy) as an unintended redux of the recently abandoned hindsight tests applied in the *Pro-Snax* era. But, unless and until this discussion – hopefully treated merely as dicta – is cleared up, practitioners will be wise to carefully make and document thorough risk disclosures to a Debtor client all during the case and particularly in the plan formation and confirmation phases.

Baker Hughes Oilfield Ops. v. Morton (In re R.L. Adkins Corp.), 784 F.3d 978 (5th Cir. 2015)

Key Issue: Whether a creditor has the right to make an § 1111(b) election when the creditor's collateral is sold pursuant to § 363 and the creditor does not credit bid?

Holding: Debtor's plan provided for a sale of assets, including the creditor's collateral, pursuant to § 363. Creditor never sought to credit bid or to clarify its rights to do so. Because the creditor had the right to credit bid under § 363 but failed to do so, and because § 1111 denies the election when the property is sold pursuant to § 363, the creditor was not entitled to make a § 1111(b) election.

Templeton v. O'Cheskey (In re Am. Hous. Found.), 785 F.3d 143 (5th Cir. 2015)

Key Issues: (1) Were creditors' claims properly subordinated as arising from the purchase or sale of a security? (2) What are the limits of the Ponzi scheme exception to the ordinary course of business exception to preferential transfers? (3) What is the appropriate test for determining good faith under § 548(c)?

Holding: Creditors' claims were properly subordinated under § 510(b) because the claims were for damages arising from the purchase or sale of securities issued by an affiliate of the debtor. With respect to the limits of the Ponzi exception, the court explained that the theory behind the exception is that "Ponzi schemes simply are not legitimate business enterprises which Congress intended to protect in § 547(c)(2)." The court declined to expand the Ponzi exception to cover situations where some fraudulent or Ponzi-like transactions occurred in an otherwise legitimate business. Here, because the businesses at issue were not true Ponzi schemes, the ordinary course of business exception remained available. Finally, in determining "good faith" the court explained that it must "look to whether the claimant was on notice of the debtor's insolvency or the fraudulent nature of the transaction."

Villegas v. Schmidt, 788 F.3d 156 (5th Cir. 2015)

Pertinent Facts: Debtor (a business entity) filed for bankruptcy. A Trustee was appointed. Trustee operated the business for a time. After a few years, the case was closed and the Trustee's fees were approved. Four years later, the former Debtor and its principal sued the Trustee for negligence, gross negligence, and breach of fiduciary duties, mostly relating to allegations that the Trustee had failed to pursue collection under an insurance policy. (The carrier denied that such a policy had been issued.) The plaintiffs did not obtain prior leave of the bankruptcy court to sue the Trustee. The U.S. District Court presiding over the lawsuit dismissed on that basis.

Key Issues and Holding: Applying the so-called *Barton* doctrine [*Barton v. Barbour*, 104 U.S. 126, 128 (1881)] requiring Bankruptcy Court approval prior to suing a Trustee (or other officer) appointed or supervised by such Court, the Fifth Circuit affirmed the District Court's dismissal of the litigation. In the process, the Fifth Circuit rejected the Plaintiffs' argument that an exception to the *Barton* doctrine was created by *Stern v. Marshall*, 131 S. Ct. 2594 (2011). "If a bankruptcy court concludes that the claim against a trustee is one that the court would not itself be able to resolve under *Stern*, that court can make the initial decision on the procedure to follow," which procedure can in turn be reviewed by the senior courts. The Fifth Circuit also rejected the further argument of the Plaintiffs that *Barton* doctrine does not apply (i.e., that prior Bankruptcy Court approval should not be required) if the litigation against the Trustee was first commenced in the U.S. District Court. "[E]very other circuit to address the issue [besides the Ninth Circuit] has maintained the distinction between the bankruptcy court and the district court, holding that `a debtor must obtain leave of the bankruptcy court before initiating an action in district court when the action is against the trustee or other bankruptcy court-appointed officer, for acts done in the actor's official capacity'," citing *Carter v. Rodgers*, 220 F.3d 1249, 1252 (11th Cir. 2000).

Practice Impact: Get the Bankruptcy Court's prior approval before suing a trustee or other court-appointed officer of the Bankruptcy Court. Just get it.

Rossco Holdings, Inc. v. McConnell, 613 F. App'x. 302 (5th Cir. 2015)

Pertinent Facts: Debtor B was the guarantor of debt secured by a hotel property in the case of Debtor A. Before the bankruptcy case of Debtor A was filed in Texas, the applicable loan documents waived Debtor B's rights as guarantor to contest any deficiency claim that might result from any foreclosure of the hotel by the secured lender. Debtor B later alleged that counsel for Debtor A was also its own counsel. (Although contested, this allegation was later taken as true for purposes of dismissal under Rule 12(b)(6).) Debtor B further claimed that it asked counsel to somehow obtain a revival of the right to contest a foreclosure deficiency. A settlement order was entered in the bankruptcy case of Debtor A, and Debtor B alleged that counsel represented that this settlement order revived such rights. Meanwhile, Debtor B filed its own bankruptcy case in California. Debtor A's bankruptcy case was also transferred to California. Plans were confirmed in each case. The lender foreclosed upon the hotel property and filed proofs of claim for the deficiency. Debtors sought to contest the deficiency claim. The California bankruptcy court ruled that the settlement order entered by the Texas bankruptcy court did not revive the right to contest the deficiency claim. Debtors then filed suit in U.S. District Court back in Texas, alleging negligent misrepresentation and malpractice by counsel. Counsel, as Defendant, moved to dismiss the Texas malpractice suit, arguing that the confirmed plans did not reserve the claims the Debtors sought to pursue against them. *See*, *In re SI Restructuring Inc.*, 714 F.3d 860, 864 (5th Cir. 2013); *In re United Operating, LLC*, 540 F.3d 351, 355–56 (5th Cir. 2008). The District Court in Texas granted dismissal.

Key Issue: Did the confirmed plans of reorganization or confirmation orders "specifically and unequivocally provide for reservation" of any claims by the Debtors against the Defendant attorneys?

Holding: No, the plans did not specifically and unequivocally reserve any cause of action by the Debtors against bankruptcy counsel from the Texas bankruptcy case. (Additionally, the Debtors were found not to have preserved several other points of error they attempted to bring in the appeal to the Fifth Circuit.)

Practice Impact: Although this might have been the case anyway, Debtor counsel should preferably have a written engagement letter with any Debtor and that letter should expressly state that other non-debtor relatives of the Debtor and the principals of the business entity Debtor are not represented by Debtor's counsel. Including that same disclaimer of representation in the order approving the engagement of Debtor's counsel might also be best practices. Moreover, in an ideal situation, the engagement letter and engagement order would also specify the identity of the separate counsel for the principals of a business entity Debtor. Still, none of these protections will necessarily preclude Debtor's relatives or principal from at least alleging that Debtor's counsel nonetheless also acted as counsel to them.

Janvey v. Golf Channel, Inc., 792 F.3d 539 (5th Cir. 2015)

Background: Following the SEC's discovery of a Ponzi scheme, Ralph S. Janvey was appointed as receiver over Stanford International Bank Limited. Janvey filed suit against The Golf Channel to recover certain payments made by Stanford under an advertising agreement. The district court granted The Golf Channel's motion for summary judgment, determining that "although Stanford's payments to Golf Channel were fraudulent transfers under TUFTA, Golf Channel was entitled to judgment as a matter of law on its affirmative defense that it received the payments in good faith and in exchange for reasonably equivalent value (the market value of the advertising on The Golf Channel)." On appeal, the Fifth Circuit initially reversed the district court, finding that The Golf Channel "failed to offer any evidence showing that its advertising services benefited the creditors." The Court held "for purposes of the 'good faith and for a reasonably equivalent value' affirmative defense in section 24.009(a) [of the Texas Business and Commerce Code], value must be measured from the standpoint of the debtor's creditors and proof of market value is insufficient." The Golf Channel petitioned for a panel rehearing and rehearing *en banc*.

<u>Holding</u>: The petition for panel rehearing was granted, the original opinion vacated, and the panel certified the following question to the Supreme Court of Texas. "Considering the definition of 'value' in section 24.004(a) of the Texas Business and Commerce Code, the definition of 'reasonably equivalent value' in Section 24.004(d) of the Texas Business and Commerce Code, and the comment in the Uniform Fraudulent Transfer Act stating that 'value' is measured 'from a creditor's viewpoint,' what showing of 'value' under TUFTA is sufficient for a transferee to prove the elements of the affirmative defense under section 24.009(a) of the Texas Business and Commerce Code?"

Janvey v. The Golf Channel, Inc., No. 15-0489 (Tex. April 1, 2016).

<u>Holding</u>: On April 1, 2016, the Supreme Court of Texas answered the certified question, concluding that "TUFTA's 'reasonably equivalent value' requirement can be satisfied with evidence that the transferee (1) fully performed under a lawful, arm's length contract for fair market value, (2) provided consideration that had objective value at the time of the transaction, and (3) made the exchange in the ordinary course of the transferee's business." The Court further held "TUFTA does not contain separate standards for assessing 'value' and 'reasonably equivalent value' based on whether the debtor was operating a Ponzi scheme. Transactions for consumable goods and services may deplete a debtor's leviable assets, but that factor alone does not render the exchange valueless. Value must be determined objectively at the time of the transfer and in relation to the individual exchange at hand rather than viewed in the context of the debtor's entire enterprise, viewed subjectively from the debtor's perspective, or based on a retrospective evaluation of the impact it had on the debtor's estate."

<u>Impact</u>: At least in actions seeking to avoid constructively fraudulent transfers under TUFTA following this latest decision,[3] the party seeking relief will have to bear the burden of proof under this more realistic standard.

Bodin Concrete, L.P. v. Concrete Opportunity Fund II, L.L.C. (In re Bodin Concrete, L.P.), 616 Fed. Appx. 738 (5th Cir. 2015)

<u>Key Issue</u>: Whether a creditor who filed a competing plan is entitled to reimbursement for legal fees and expenses for substantial contribution under § 503(b)(4)?

<u>Holding</u>: The creditor's involvement in the case following expiration of exclusivity put pressure on the Debtor to propose a more favorable plan that provided a greater return, thus the creditor was entitled to reimbursement for a substantial contribution.

[3] The surviving import of ***<u>Janvey v. Romero</u>***, 2016 U.S. App. LEXIS 4835 (5th Cir. Tex. Mar. 16, 2016), may then be that a party sued for avoidance, under the original *Golf Channel* ruling and before the recent decision by the Texas Supreme Court, can potentially lose the benefit of the new standard if it is not timely asserted and preserved.

McMillan v. Schmidt (In re McMillan), 614 F. App'x. 206 (5th Cir. 2015)

<u>Key Issue</u>: Whether alleged Debtor's motion under § 303(i) to collect fees, costs and damages from parties who did not sign or join in the involuntary petition was sufficient to bring those parties within in the jurisdiction of the bankruptcy court?

<u>Holding</u>: "[O]nly 'petitioning creditors' – i.e., entities that file a petition under § 303(b) or join it under § 303(c) – are parties to a contested matter and therefore properly before the court on a motion for fees." Because the parties at issue were not signatories to the involuntary petition, they are not parties to the contested matter, and the alleged Debtor is required to serve them with process to bring them within the jurisdiction of the bankruptcy court.

Firefighters' Ret. Sys. v. Citco Grp. Ltd., 796 F.3d 520 (5th Cir. 2015)

<u>Key Issue</u>: Whether the district court was entitled to permissively abstain and equitably remand under 28 U.S.C. §§ 1334(c)(1) and 1452(b) in light of the defendants' pending Chapter 15 bankruptcies?

<u>Holding</u>: Under § 1334(c)(1) "a court may abstain from 'a particular proceeding arising under title 11 or arising in or related to a case under title 11' but not from a proceeding 'with respect to a case under chapter 15 of title 11.'" The court further explained that "[r]eading §§ 1334(c)(1) and 1452(b) together, then, the prohibition against abstention from proceedings related to Chapter 15 cases also applies to bar the equitable remand of those proceedings under § 1452." Thus, the District Court erred when it permissively abstained and equitably remanded the cases at hand.

Kelley v. Cypress Fin. Trading Co., L.P. (In re Cypress Fin. Trading Co., L.P.), 620 F. App'x. 287 (5th Cir. 2015)

<u>Key Issue</u>: Whether dismissal of a corporate Chapter 7 case was appropriate under § 707(a) when the bankruptcy served no purpose, resulted in no benefit to the debtor or its creditors, and delayed pending litigation against the Debtor?

<u>Holding</u>: "A corporate Chapter 7 bankruptcy has one purpose: to allow an entity breathing space to marshal assets for orderly distribution to creditors. When, as here, the debtor has no assets, no viable claims or causes of action, and no other money-making prospects, Chapter 7 bankruptcy cannot serve even this limited function. Under 11 U.S.C. § 707(a), 'cause' to dismiss exists when bankruptcy cannot benefit outside creditors or the debtor and the process serves only to delay the prosecution of a lawsuit against the debtor."

Petfinders, L.L.C. v. Sherman (In re Ondova Ltd. Co.), 620 Fed. Appx. 290 (5th Cir. 2015)

<u>Key Issue</u>: Whether the appeal of a sale order is moot, when the sale was to a good faith purchaser, and the sale was not stayed pending appeal?

Holding: Appellant failed to obtain a stay pending appeal and therefore, the appeal is moot. Section 363(b) "patently protect[s] from later modification on appeal an authorized sale where the purchaser acted in good faith and the sale was not stayed pending appeal. . . . a challenge to the purchaser's good-faith status itself is not mooted by the sale if timely raised, but 'such a challenge may not be raised for the first time on appeal.'"

Official Comm. of Unsecured Creditors v. Moeller (In re Age Ref., Inc.), 801 F.3d 530 (5th Cir. 2015)

Pertinent Facts: Creditor filed a post-petition claim for principal, interest, and other charges under § 506(b), asserting that it was oversecured and entitled to post-petition interest. The Committee filed a motion to value the Creditor's claim, challenging the Creditor's alleged oversecured status. The Trustee and the Creditor ultimately negotiated a settlement of the post-petition claim and filed a 9019 motion to approve the settlement. The Bankruptcy Court found the proposed settlement agreement, the motion to value, and the claim objection "intertwined [such that] the resolution of one resolve[d] the others." The Bankruptcy Court approved the settlement agreement and denied the motion to value and claim objection. The Committee appealed.

Key Issues: (1) Whether the bankruptcy court abused its discretion in approving the Settlement Agreement? (2) Whether the bankruptcy court erred in denying the Motion to Value and the Claim Objection concurrent with its approval of the Settlement Agreement?

Holding: The Fifth Circuit was persuaded that the bankruptcy court applied the appropriate analysis under *Jackson Brewing, Foster Mortgage*, and *Cajun Electric Power*, explaining that "the record provides support for the Trustee's conclusion that the estate faced some probability of failure in litigating Chase's post-petition claim such that the Settlement Agreement poses a fair and equitable, and favorable alternative." With respect to the Claim Objection, the Fifth Circuit determined that although the Bankruptcy Court did not adequately determine the amount of Chase's allowed claim under section 502(b), the Bankruptcy Court's approval of the Settlement Agreement included an implicit denial of the Claim Objection. Finally, a determination under section 506(a) is permissive rather than mandatory, and therefore "the bankruptcy court did not abuse the discretion afforded it by Rule 3012 in declining the Committee's request to undertake a 'more precise determination of value'" and "did not err in denying the Motion to Value simultaneously with its approval of the Settlement Agreement."

Practice Point: Proper designation of issues on appeal is important. The Committee designated eight issues on appeal in this case. However, six of those challenged only district court actions. The Fifth Circuit explained, "[a]cting as a 'second review court' in a Chapter 11 bankruptcy case, we do not review the findings or conclusions of the district court – rather, we review the findings and conclusions of the bankruptcy court. As an initial matter, we conclude that the issues the Committee designates challenging exclusively district court actions do not require our consideration, and we do not address those issues."

***Neurology & Neurophysiology Assocs., P.A. v. Tarbox (In re Neurology & Neurophysiology Assocs., P.A.),* No. 15-50105, 2015 U.S. App. LEXIS 18007 (5th Cir. Tex. Oct. 15, 2015)**

<u>Key Issue</u>: Whether the district court abused its discretion when it denied Debtor's motion to extend the deadline to file its brief and dismissed Debtor's bankruptcy appeal?

<u>Holding</u>: The district court has "broad discretion" to extend filing deadlines, and may extend the time to file a motion for "good cause" if the party failed to act because of "excusable neglect." Here, the district court's decision to dismiss the appeal was reasonable when (1) Debtor's delay of over one month prejudiced Appellee in its state court suit against the Debtor, (2) the 34 day delay was substantial, (3) Debtor's failure to exercise diligence in filing and pursing its appeal was the sole reason for the delay, and (4) Debtor failed to show good cause to excuse the late filing.

***Treaty Energy Corp. v. Hallin (In re Treaty Energy Corp.),* 619 F. App'x. 443 (5th Cir. 2015)**

<u>Key Issue</u>: Whether the alleged debtor was entitled to costs and damages under 11 U.S.C. § 303(i)(2) for losses incurred in the sale of restricted shares of the alleged debtor's stock during the pendency of the involuntary petition?

<u>Holding</u>: The alleged debtor was not entitled to recover its claimed losses because it failed to introduce proper evidence demonstrating (1) that the sales price of the stock declined during the pendency of the involuntary petition, or (2) that it intended to sell the sell the restricted shares at particular discount off the market price for unrestricted shares.

***Fortune Natural Res. Corp. v. United States DOI,* 806 F.3d 363 (5th Cir. 2015)**

<u>Key Issue</u>: Whether Fortune, a working interest owner holding a claim for decommissioning costs related to a lease, has standing to appeal the bankruptcy court's order approving the sale of certain assets (not including Fortune's lease) when the order was not stayed and the sale closed?

<u>Holding</u>: Courts apply the "person aggrieved" test to determine whether a party has standing in the bankruptcy court. Fortune argued that it had standing to appeal because it was directly and adversely affected by the final sale order. Fortune asserted that earlier versions of the order covered decommissioning obligations, such as those under its lease, while the final sale order gave the parties discretion to allocate those funds. The Fifth Circuit found Fortune's interpretation of the language ignored the plain meaning and was unreasonable. Even if Fortune proved that prior versions of the order required a different allocation, it still failed to show how the final order directly and adversely affected Fortune pecuniarily. "[B]ecause Fortune did not show that it would have accessed any funds from the bankruptcy estate had the court not approved the Sale, the Final Sale Order left Fortune in the same position (i.e., without any funds from ATP to assist in the decommissioning obligations for the Fortune Lease)."

Collins v. Sidharthan (In re KSRP, Ltd.), 809 F.3d 263 (5th Cir. 2015)

Key Issue: Whether the bankruptcy court had related to jurisdiction over indemnity claims appellant asserted were illusory, lacked merit, and had no chance of succeeding?

Holding: The Fifth Circuit explained that "[f]ederal courts have 'related to' subject matter jurisdiction over litigation arising from a bankruptcy case if the 'proceeding could conceivably affect the estate being administered in bankruptcy.'" In this case, Appellant "sets up a dichotomy between potentially meritorious claims, over which there would be 'related to' jurisdiction, and meritless claims, over which there would be no such jurisdiction." The court rejected Appellant's arguments, stating "[g]enerally, courts should analyze their own authority to hear a case as a separate matter from whether that case involves a viable claim." Thus, the bankruptcy court and the district court had "related to" jurisdiction.

Southwest Sec., FSB v. Segner (In re Domistyle, Inc.), No. 14-41463, 2015 U.S. App. LEXIS 22787 (5th Cir. Dec. 29, 2015)

Pertinent Facts: A liquidating plan was confirmed. The Plan Trust was premised on the assumption that the improved real estate (the "Property") was worth around $6 million whereas as the debt secured by the Property was $3.69 million. The Trustee was given a target date for the sale of the Property. The Plan Trust required that the Property be kept up and insured. The Trustee attempted to market the Property and, along the way, the Trust paid for numerous expenses. No offers were received sufficient to pay the secured debt which was, of course, growing over time. The Trustee and lender discussed but did not agree on any surcharge for the expenses that were being incurred. Eventually, the Trustee moved to abandon the Property, sought to surcharge the lender, and advised the lender that he would no longer pay for maintenance expenses and insurance. After hearing, the Property was abandoned and some expenses (incurred shortly after the notice of intent to abandon) were satisfied by a partial agreement. The surcharge of earlier expenses remained contested. After hearing, the Bankruptcy Court allowed a surcharge for the remaining, contested expenses and granted a priming lien. A direct appeal to the Fifth Circuit was granted.

Key Issues: Did the secured creditor benefit from the contested expenses to an extent sufficient to warrant a surcharge for such expenses and the imposition of a priming lien? The Trust maintained the Property with the intent of selling it for an amount in excess of the secured lender's claim, with some left over to make a distribution to other creditors, whereas in reality these hopes had not come to pass – only the secured creditor received benefit. The secured lender contended that this forward looking intent should require a conclusion that the expenses were not incurred *primarily* for the secured creditor, citing language from *In re Delta Towers, Ltd.*, 924 F.2d 74, 76 (5th Cir. 1991). The Trustee contended that a hindsight test should instead apply, testing who actually benefitted from the expenses. The Trustee relied in part on the treatise in 4 COLLIER ON BANKRUPTCY ¶ 506.05 and *In re JKJ Chevrolet, Inc.*, 26 F.3d 481, 483 (4th Cir. 1994).

The secured lender also contended that the Trustee had failed to bear its burden of proving (or quantifying) the extent to which the secured lender was benefitted.

<u>Holding & Rationale</u>: Affirmed; the surcharge and priming lien were upheld. On the forward looking versus hindsight testing, the panel questioned early on where the "primarily for the benefit of" language in *Delta Towers* had come from, noting that § 506(c) instead speaks of "costs and expenses" that are "reasonable" and "necessary ... [to] preserv[e], or dispos[e] of" collateral property. Tracing the subsequent history in other Circuits of the authorities on which *Delta Towers* itself had relied, the Court followed the hindsight test, reasoning that there was "no basis for adopting a rule that is largely unmoored from the statutory text." However, if a trustee holds an asset longer than necessary to determine and realize its value, and the value turns out to be less than the creditor's secured interest, the creditor can challenge the necessity of the costs incurred by the trustee.

On the burden of proof point, the Court found that the Bankruptcy Court had not clearly erred in finding that the secured creditor had received a direct and quantifiable benefit from the Trustee's stewardship of the Property. The Court contrasted the Trustee's own expert's testimony to the effect that value was preserved dollar for dollar by the expenses, which it found sufficient. The Court also observed that the secured lender did not offer any competing expert or other contradictory value testimony.

<u>Practice Impact</u>: Obviously, trustees and secured lenders alike will want to keep *Domistyle* in mind whenever negotiating or litigating any similar, proposed scheme for maintaining and eventually selling property – a hindsight test will most likely apply unless the parties expressly agree to or the Bankruptcy Court decrees something else. (Although *Domistyle* does note that whether expenses meet the requirements of § 506(c) still depends upon the facts of each particular case.) As to burden of proof, a strategic decision to offer no adverse case but to only attack the merits or credibility of the moving party's evidence by cross-examination may have high potential upside, but also high potential risk. In some cases, the sheer cost of putting such adverse evidence forward will, in and of itself, make the opposing party's decision for them.

Torres v. Krueger, 812 F.3d 365 (5th Cir. 2015)

<u>Key Issue</u>: Whether Debtor's bad faith behavior is cause for dismissal under § 707(a)?

<u>Holding</u>: The Fifth Circuit explained "[e]very bankruptcy statute since 1898 has incorporated literally, or by judicial interpretation, a standard of good faith for the commencement, prosecution, and confirmation of bankruptcy proceedings." (citing *Little Creek Dev. Co. v. Commonwealth Mortg. Co. (In re Little Creek Dev. Co.)*, 779 F.2d 1068, 1071 (5th Cir. 1986).) In deciding whether "cause" exists to dismiss a case, "a court may consider the debtor's entire course of conduct – before, during, and after the filing of a chapter 7 petition." Here, the court found the record "replete with evidence that [the Debtor] filed bankruptcy for illegitimate purposes, misled the court and other parties, and engaged in bare-knuckle litigation practices, including lying under oath and threatening witnesses," and therefore, Debtor's "duplicitous behavior is exactly the sort of conduct contemplated by most courts as giving cause for dismissal under § 707(a)."

Garner v. Knoll, Inc. (In re Tusa-Expo Holdings, Inc.), 2016 U.S. App. LEXIS 1377, No. 5-10274, (5th Cir. Jan. 28, 2016)

Pertinent Facts: Trustee sued to recover transfers under § 547. The Debtor was a retail distributor for Knoll. By the original 2002 contract, the contemplated sequence was: (1) a customer would order furniture from the Debtor; (2) Debtor would then order from Knoll; (3) Knoll would then deliver to Debtor; (4) Debtor would deliver to customer and install; (5) Debtor then invoiced the customer; (6) customer would then pay Debtor; and (7) Debtor would then pay Knoll. Debtor granted Knoll a first lien in most assets, including ARs from Debtor's customers. In 2008, this arrangement was amended to supposedly cap Knoll's "over 90 day" exposure on its sales to the Debtor, and the lien in ARs was renewed.

In 2009, Debtor obtained $6.5 of additional financing from Textron, granting a first lien in current and after-acquired assets, including Knoll's collateral and agreeing to a lockbox arrangement in favor of Textron. As a condition precedent, Textron and Knoll entered into a Subordination Agreement. Under this agreement, Knoll retained a first-priority security agreement in specified ARs and agreed to a second-priority lien in all other current and after-acquired assets. Except for those specified ARs, Textron's lien would have priority.

Debtor's ARs from customers were paid directly into the lockbox, an account controlled by Textron. Textron swept the lockbox daily, and applied the swept funds to reduce its own outstandings, which in turn created availability on the line of credit. Debtor drew from the availability on the Textron line and, from this, used borrowings to pay Knoll.

After the Nov. 2008 bankruptcy filing by Debtor, Trustee sought to recover almost $4.6 million in transfers from Knoll. In Count I, the Trustee sought recovery of the $4.6 million as paid by the Debtor to Knoll, relying heavily on the Fifth Circuit's analysis in *Krafsur v. Scurlock Permian Corp. (In re El Paso Refinery, LP)*, 171 F.3d 249 (5th Cir. 1999) of the "Source Rule" and "Application Rule" defenses. In Count II, the Trustee sought to avoid transfers made to Knoll pursuant to a "dealer participation agreement" between Debtor and Knoll that was incident to a "direct bill contract" between Knoll and Bank of America relating to a specific project.

Key Issue(s): (1) Did the "Source Rule," "Application Rule," or both serve as defenses to Knoll or, conversely, did the application of those rules instead indicate that Knoll had been paid instead either from Textron's line of credit or from Textron's collateral? and (2) Under §§ 9.102, 9.315, 9.332(a), etc., of the Texas UCC, did Knoll retain a security interest in funds paid to it by Tusa as "proceeds" after they went into Textron's lockbox and were swept by Textron, or did Textron's sweep of the lockbox funds (and its subsequent application of those funds to reduce Tusa's debt owed to Textron), cut off any proceeds defense in favor of Knoll?

<u>Holding</u>: Siding with the Courts below, the transfers to Knoll withstood the avoidance challenge under *El Paso Refinery* under § 547(b)(5) because the Courts found that the Trustee had failed to establish that the funds paid to Knoll were not proceeds of Knoll's collateral under the "source rule." The Fifth Circuit concluded that Knoll's lien in proceeds survived the deposit of those funds into the lockbox because the Debtor, "not Textron, owned the lockbox, [and accordingly,] § 9.332(a) does not apply." Moreover, the Court concluded that Knoll's lien remained attached to the funds, notwithstanding that Textron swept the lockbox funds and applied them to reduce Tusa's debt owed to Textron.

In a motion for rehearing, the Trustee pointed out that Knoll's lien in the proceeds in question was in fact a second lien (behind Textron's) even before they went into the lockbox and that the correction of this error should upset the Fifth Circuit's analysis under *El Paso Refinery*. The Trustee and Knoll agreed that Textron had a first lien on the funds deposited into the lockbox, and never disputed this fact. The Trustee also pointed out that the inability of the parties to trace the alleged Knoll proceeds into and through the lockbox process mitigated against Knoll, and not in its favor. These points did not gain sufficient traction to obtain rehearing.

<u>Practice Impact</u>:

Issues re: UCC and Intercreditor Agreements. As the Fifth Circuit noted, "§ 9.332 is a recent addition to the UCC," and "the jurisprudence interpreting it is scarce." Still, the Fifth Circuit's construction of this statute is likely to be controversial among UCC scholars and practitioners and, consequently, in the Bankruptcy bar as well. If the Court's UCC ruling, *i.e.*, that Knoll's lien survived transit through the lockbox arrangement, was incorrect, then the transfers to Knoll might well have been avoided. Had Knoll been paid with funds that were not sourced from its own collateral and/or if any lien in those funds had not survived the transit through the lockbox arrangement, Knoll would have almost certainly received more than would have been the case in liquidation absent the transfers. Time will tell, but these § 9.332 issues may, in the future, be settled differently than the Fifth Circuit has done here.

In real life, however, any dispute such as found in this case will more typically surface between the competing creditors and be resolved by interpretation of their own intercreditor or subordination agreements. Creditors would then likely implead funds still trapped in any lockbox or seek reimbursement of funds that had been directed in contravention of their agreements. (This same conflict may also be found not far below the surface in the *El Paso Refinery* opinion itself, where the other potentially competing secured creditor, Bank Brussels Lambert, never contested Scurlock's prior entitlement under that intercreditor agreement to the proceeds placed in dispute by the trustee in that case.) Accordingly, to avoid the potential expense of litigation, creditors entering into complex intercreditor agreements where variables may affect the priority of lien positions or the allocation of collateral may do well to specify in some detail the implications, inter se, of a bankruptcy case of the underlying borrower.

Issues re: Burden of Proof and of Going Forward. Furthermore, both *El Paso Refinery* and *Garner v. Knoll* present a possible Bankruptcy Code anomaly regarding the burden of proof required of the preference litigants. According to these cases and perhaps the text of the Bankruptcy Code itself, the party seeking avoidance can be required to bear the burden of proof under § 547(b)(5) ("more than such creditor would receive if … the transfer had not been made") to essentially negate the underlying elements of the "Source Rule" and "Application Rule" defenses (before and perhaps even if they are not affirmatively pled by the defendant) while, under § 547(c), including (c)(5), the defendant is required to bear essentially that same burden of proof to establish the elements of those defenses.[4] This statutory conundrum may eventually be resolved either by legislation or by the establishment of some "initial burden of proof / shifting burden of proof" mechanism. However, in the meantime, litigants on either side should be aware that, one the one hand, the application of § 547(b)(5) may in some instances require the plaintiff to anticipate and disprove unasserted (or untimely asserted) defenses under the "Source Rule" or "Application Rule," while, on the other hand, the application of § 547(c)(5) may result in other instances in a defendant losing such defenses if not timely pled and substantiated by proof. Professionals on both sides should likely then address these issues early on in pleadings and discovery and, if applicable, a pretrial order. Likewise, Courts should perhaps be proactive to determine, in early status conferences, whether these issues are or are not in play and, if so, how they will be developed and presented in a particular case.

Valence Tech., Inc. v. KPMG Corporate Fin., L.L.C. (In re Valence Tech., Inc.), 2016 U.S. App. LEXIS 8196 (5th Cir. Tex. May 4, 2016)

Key Issues: What amount of Success Fee did the Debtor owe to KPMG and Roth Capital under the operative engagement agreement?

Background: Debtor retained KPMG and Roth to arrange a private placement of its equity. As set forth in the parties' engagement agreement, the Debtor agreed to pay KPMG and Roth an engagement fee, a retainer, and a Success Fee "equal to 2.5% of the Private Placement Value … less the amount of the previously paid Engagement Fee and Retainer Fee." The definition of Private Placement Value excluded "any consideration received by the Company's creditors in satisfaction of claims or debts existing on the date hereof." The agreement further specified that "[a]ny consideration received from Berg & Berg … will be subject to a Success Fee of 1.25% (and not 2.5%)".

Ultimately, Berg & Berg agreed to convert its prepetition debt of $50 million to equity in the reorganized debtor. As a result, the bankruptcy court awarded KPMB and Roth each $595,000, which amounted to 1.25% of the $50 million minus the engagement and retainer fees paid by the Debtor, as provided in the engagement agreement. Debtor appealed.

[4] Interestingly enough, the difficulty of proof in *Garner v. Knoll* chiefly related to tracing funds after they were deposited into the lockbox. Some bankruptcy practitioners might see this as a failure of the Trustee's proof under §547(b)(5), while a UCC practitioner might see this instead as a failure of a defendant's proof of a retained security interest ("Source Rule" defense) under the U.C.C.

Holding: In an unpublished, per curiam opinion, the majority of the panel (Judges Prado and Haynes) upheld the Success Fee. While the fee agreement initially defined "Private Placement" to exclude "any consideration received by the Debtor's creditors in satisfaction of existing debts," the next sentence of the agreement specifically carved out and addressed any consideration received from Berg & Berg. Under the specific provision, KPMG and Roth were found to be entitled to a Success Fee of 1.25%. This reasoning "comports with the interpretive principle that a later, specific sentence in a contract controls over an earlier, general sentence." Judge Owen dissented.

UNITED STATES BANKRUPTCY COURT FOR THE NORTHERN DISTRICT OF TEXAS

Cao v. Garner (*In re Garner),* No. 15-4019, 2015 Bankr. LEXIS 1984 (Bankr. N.D. Tex. June 18, 2015)

Key Issue: When a party mails a pleading to the clerk via the USPS, on what date is the pleading deemed filed?

Holding: The date the pleading is received by the clerk. "[C]ompliance with a filing requirement is not satisfied by mailing the necessary papers within the allotted time. The papers must be filed by the clerk within the filing period specified in the applicable rule or order. Even if a party deposits a filing with the postal service for delivery prior to the deadline, if the clerk does not receive the filing before the deadline passes, the filing is not timely and dismissal is appropriate."

In re Crosby Nat'l Golf Club, LLC, 534 B.R. 888 (Bankr. N.D. Tex. Aug. 3, 2015)

Key Issues: (1) Whether venue was proper in the Northern District of Texas, and (2) if so, whether the court should exercise its discretion to transfer venue in the interest of justice or for the convenience of the parties?

Holding: While the Debtor was a California L.L.C., with its principal assets located in California, the Debtor's principal place of business was in Fort Worth, and therefore venue was proper in the Northern District of Texas. Debtor's "nerve center" or high level management, including 13 employees who made performed management operations including accounting, marketing, finance, human resources, strategic decision making and other functions, was located in Fort Worth.

With respect to whether the interests of justice would be best served by transferring the case to California, the court explained that the disputes in this case were based on California real property rights, and the dispute between the Debtor and the HOA was set for trial in a California state court prior to the filing of the bankruptcy case. "When the central issue in the bankruptcy case is the resolution of that dispute and the matter was set for trial in another court prior to the bankruptcy filing, a bankruptcy court should hesitate to take on the task of setting precedent on issues as to which another state has a compelling interest. Because of this concern I am reluctant to determine the dispute between the debtor and Crosby HOA, and that factor weighs in favor of transferring the case to California." The court further noted that there was no indication that a California bankruptcy court would be less efficient, economical or fair than it would be in during the administration of the case. As a result, the interests of justice would be best served by transferring venue to the Southern District of California.

The court also addressed the convenience of the parties. While the largest creditor was located in Texas, there were likely only a few hearings the creditor's representative would be required to attend. And, while the Debtor's management was located in Texas, which would support retaining the case, the court explained that is highly unlikely that the disputes will be resolved in the courtroom. Given the possible resolutions of the case, the resolution would affect many more people in California than Texas.

In re ERG Intermediate Holdings, LLC, No. 15-31858, 2015 Bankr. LEXIS 3639 (Bankr. N.D. Tex. Oct. 26, 2015)

Key Issues: (1) Whether venue is proper in any District within the state where an entity is organized, including those Districts in which the entity does not have its principal place of business, and (2) if so, whether the court should exercise its discretion to transfer venue in the interest of justice or for the convenience of the parties?

Holding: The court held that venue was technically proper and should not be changed, explaining that "an entity incorporated in a given state is domiciled in the entire state and may initiate a bankruptcy proceeding in any federal district in that state." With respect to the request for a transfer of venue for the convenience of the parties or in the interest of justice, the Court explained that there were pros and cons for almost all the Districts in which the Debtors could have chosen to file these cases. "[T]he common thread that seems to run through each of these factors is that each venue would be more convenient for some parties and less convenient for others, but no venue is clearly superior to all others." Therefore, a change of venue is not warranted in these cases for the convenience of the parties or in the interests of justice.

In re Positron Corp., 541 B.R. 816 (Bankr. N.D. Tex. 2015)

Key Issue: (1) Whether venue was proper the Northern District of Texas when the alleged debtor was a Texas corporation with operations in the Lubbock, and (2) if venue is proper, whether the case should be transferred to the Northern District of Illinois under 28 U.S.C. § 1412.

Holding: Venue was appropriate in Texas, and within the Northern District, as the alleged Debtor is a Texas corporation and maintained operations in Lubbock. In determining whether the alleged Debtor's request to transfer venue to the Northern District of Illinois should be granted, the bankruptcy court noted that the alleged Debtor has no significant ongoing business operations, and the alleged Debtor's only assets of real significance and importance are the equipment and radioactive materials maintained and held at the Debtor's Lubbock facility. The bankruptcy court explained "[i]f relief is granted here upon trial of the involuntary petition, the maintenance and likely disposition of the radioactive material will be the most important part of the [alleged Debtor's] administration in bankruptcy." Retaining venue in the Northern District of Texas, Lubbock Division, best addresses the concerns of the parties.

In re Samuel Evans Wyly, No. 14-35043 (Bankr. N.D. Tex. May 10, 2016)

In a lengthy Memorandum Opinion, the Court relied on prior findings from *SEC v. Wyly et al.*, Case No. 10-5760-SAS (SDNY) (treating most of these as binding by collateral estoppel) and made additional findings in connection with a motion under 11 U.S.C. § 505 to determine tax liability. In the complex ruling, the Court determined, by clear and convincing evidence, that Sam Wyly and his late brother Charles committed tax fraud in connection with a series of offshore trusts created in the 1990s, attempting to shield in excess of $1 billion. The "heart of the Wyly offshore system had been established through deceptive and fraudulent actions." As a result, Sam Wyly faces an allowed tax claim, including interest and penalties, of up to $1.4 billion. However, as to Debtor Dee Wyly (widow of the late Charles), the Court found her innocent of any wrongdoing and entitled to the benefit of the innocent spouse defense.

A LITTLE INTERSTATE DIALOGUE ON CRAMDOWN INTEREST

In re MPM Silicones, LLC, No. 14-22503, 2014 Bankr. LEXIS 3926 (Bankr. SDNY Sept. 9, 2014) (Cramdown Interest Rate on Secured Claims)

Although oral arguments have already been held in the Second Circuit, we are still awaiting that Court's ruling on the interest rate methodology to be used in cramming down a secured claim in Chapter 11. The District Court in the SDNY had previously affirmed Bankruptcy Judge Robert Drain's prior ruling which approved an effective cramdown rate of 4.09% per annum.

SDNY District Court

In the appeal from the Bankruptcy Court's earlier cramdown confirmation ruling, the appellants contended that the cramdown interest rate should be determined using an "efficient market" approach based on the interest rate the market would pay on such a loan, in this case measured by "the rates on the exit and bridge financing the Debtors actually obtained." The appellees argued, to the contrary, in favor of the Bankruptcy Court's use of a formula approach as laid out in *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), i.e., calculated by augmenting a risk-free (or low risk) base rate to account for the risk of nonpayment posed by borrowers in the financial position of the debtor. The District Court affirmed the Bankruptcy Court both on the formula based approach and on its use of the 7-year Treasury rate as the appropriate base rate.

SDNY Bankruptcy Court – *U.S. Bank N.A. v. Wilmington Sav. Fund Soc'y (In re MPM Silicones, LLC),* 531 B.R. 321 (SDNY 2015)

At the Bankruptcy Court level, Bankruptcy Judge Drain issued several bench rulings on cramdown interest rates, the availability of a make-whole premium, third party releases, and the extent of the subordination of senior subordinated noteholders. On the subject of the appropriate cramdown interest rate for secured claims, Judge Drain adopted a "formula" approach. By that formula, the cramdown interest rate is one that eliminates profit, eliminates fees, and compensates a secured creditor at an essentially riskless base rate, supplemented by a risk premium of between 1-3%, to account for a debtor's unique risks emerging from chapter 11. Using a 7-year Treasury rate as his base rate, the resulting cramdown interest rate was 4.09% per annum.

Somehow bridging several obvious dissimilarities between chapter 13 automobile loans and chapter 11 corporate loans, Judge Drain applied the plurality opinion in *Till* as the guiding authority, and relied upon the prior Circuit authority of *In re Valenti*, 105 F.3d 55 (2d Cir. 1997) in doing so. The Court determined initially that *Till* and *Valenti* established key "first principles" to be followed when considering the proper interest rate to present value a secured creditor's deferred distributions under a plan for cramdown purposes even in chapter 11. The Bankruptcy Court also rejected alternatives that required a market-based analysis or inquiry into interest rates for similar loans in the marketplace and the so-called "forced loan" or "coerced loan" approach, "which *Valenti* defined as adopting the 'interest rate on the rate that the creditor charges for loans of similar character, amount, and duration to debtors in the same geographic region.'"

Bankruptcy Judge Drain cited *Wells Fargo Bank, N.A. v. Texas Grand Prairie Hotel Realty, L.L.C. (In re Texas Grand Prairie Hotel Realty, L.L.C.)*, 710 F.3d 324, 330 (5th Cir. 2013), for the proposition that the vast majority of cases have ultimately applied a *Till* prime-plus approach or base rate-plus approach to the chapter 11 cramdown rate because most often there is no "efficient market." "This should not be surprising because it is highly unlikely that there will ever be an efficient market that does not include a profit element, fees and costs, thereby violating *Till* and *Valenti's* first principles, since capturing profit, fees and costs is the marketplace lender's reason for being.… (Moreover, the two-step approach has a perverse underpinning: if the debtor is healthy enough to correspond to borrowers who could receive comparable loans in the marketplace, it would in all likelihood have to pay a higher cramdown rate than under the *Till* and *Valenti* formula approach for debtors who could not obtain a comparable loan in the market.)"

NDTX Bankruptcy Court – *In re Couture Hotel Corp.,* 536 B.R. 712 (Bankr. N.D. Tex. 2015) (provisionally denying confirmation) and *In re Couture Hotel Corp.,* No. 14-34874, 2016 Bankr. LEXIS 35 (Bankr. N.D. Tex. Jan. 5, 2016)(findings of fact and conclusions of law permitting plan modification and confirming modified plan)

The approach approved in *MPM* (often popularly referred to as *Momentive*) is somewhat different from that taken by Bankruptcy Judge Barbara Houser in *In re Couture Hotel Corporation*, where the secured creditor had made an election under § 1111(b). In the initial September 2015 memorandum opinion, Judge Houser early on observed that "[T]he Fifth Circuit [in *Texas Grand Prairie Hotel*] reaffirmed its holding in *Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship (In re T-H New Orleans Ltd. P'ship)*, 116 F.3d 790 (5th Cir. 1997), stating that 'In *T–H New Orleans*,' we '[declined] to establish a particular formula for determining an appropriate cramdown interest rate under Chapter 11, reviewing the bankruptcy court's entire § 1129(b) analysis for clear error. We reasoned that it would be imprudent to 'tie the hands of the lower courts as they make the factual determination involved in establishing an appropriate interest rate.'"

Unlike the *MPM* decisions, the Bankruptcy Court in *Couture Hotel* did not follow a strictly formulaic approach: "[U]nder binding Fifth Circuit precedent, this Court is not required to follow a formulaic prime-plus approach when evaluating the Cramdown Interest Rate. *Texas Grand Prairie*, 710 F.2d at 331, 337. Instead, the Court has the discretion to consider additional factors in determining a proper cramdown interest rate, including industry risk. The Court importantly noted that, "in contrast to *Texas Grand Prairie*, the parties here have not stipulated that a strict, prime-plus formula should be used."

In that initial memorandum opinion, the Bankruptcy Court overruled numerous objections to methodology, disclosure and document exchange issues, and the like, and observed that while the Debtor's expert's methodology "is not in strict compliance with *Till*, *Texas Grand Prairie* clarified that *Till* is merely instructive in determining cramdown rates in the Chapter 11 context." Being so instructed by the various approaches offered while being critical of aspects of each, the Court then went on to provisionally find that the Debtor's initial interest rate proposal of 4.25% per annum did not satisfy the criteria of § 1129(b)(2)(A) on the facts of the case and in light of the § 1111(b) election. However, [*id*. at 48, fn. 37], the Court added that it would, on these facts, confirm a plan otherwise on the same terms if the cramdown interest rate was at least 6.75% per annum.

Following plan modification on this and other points, the plan was ultimately confirmed. However, because that 6.75% rate resulted from an extensive analysis and balancing of various risk factors specific to that case, it should not automatically be regarded as a universal "go-by" for cramdown rates in the N.D. Tex.

<u>SOUND BITES FROM OTHER CIRCUITS – THINGS TEXANS VENTURING OUT NEED TO KNOW</u>

<u>Second Circuit</u>:

In re Sabine Oil & Gas Corp., 547 B.R. 66 (Bankr. S.D.N.Y. 2016)

Bankruptcy Judge Chapman allowed the Debtors to reject certain contracts with "midstream gatherers," finding that these contracts did not "run with the land."[5]

The Debtors contended that the agreements were burdensome because the contracts in question required them to deliver minimum amounts of gas and condensate which, under prevailing conditions would result in the Debtors having to make contractual deficiency payments to cover shortfalls. One counter-party contended, inter alia, that the covenants in their agreement requiring the Debtors to dedicate specified products and to pay transportation fees were covenants running with the land, which would therefore survive rejection. The other major counter-party made similar arguments but advanced the conclusion that these covenants rendered the agreements not subject to rejection.

In determining that these particular agreements did not "run with the land," the Court sought to apply Texas law as enunciated in *Musgrave v. Brookhaven Lake Property Owners Ass'n*, 990 S.W.2d 386, 395 (Tex. App. 1999), *Inwood North Homeowners' Ass'n, Inc. v. Harris*, 736 S.W.2d 632, 635 (Tex. 1987), etc. and found that, in particular, the requirement of "horizontal privity" was not met. The "horizontal privity" standard was taken to mean that there must be '"simultaneous existing interests or mutual privity' between the original covenanting parties as either landlord and tenant or grantor and grantee." Consequently, rejection was permitted.

Picard v. Legacy Capital Ltd. (In re Bernard L. Madoff Inv. Sec. LLC), No. 08-01789, 2016 Bankr. LEXIS 777 (Bankr. SDNY Mar. 14, 2016)

Bankruptcy Judge Bernstein granted motions to dismiss several counts of an avoidance action brought by the Trustee of Madoff and his entities against certain hedge fund management companies, allowed the plaintiff a chance to replead, and let one count (seeking avoidance and recovery of a transfer of "fictitious profits" within two years of the petition date) survive. The facts as alleged were harsh sounding indeed. The Trustee, as plaintiff, had attached to his Complaints transcripts and excerpts of testimony taken before the SEC, an investigative report generated during the periods in question, and numerous emails to support his allegations that the Defendants knew of numerous indicia of fraud; some of the Madoff options trading was impossible; some of the timing of trades was impossible; the Madoff fee structure was "unusual"; they should have been on

---

[5] The Bankruptcy Court used industry terminology to refer to the objecting counterparties as "midstream gatherers," situated operationally between upstream companies such as the Debtors and downstream refining companies. "[M]idstream gatherers gather, treat, transport, and/or process mineral products produced from a well before such products enter the commercial market." *See*, *id.*, fn. 3.

alert with Madoff's purportedly enormous trading volumes never impacted the market; the reported rates of return were impossible; the Madoff operations lacked transparency and controls; there was no capable auditor in place; many trades were reported outside of the daily range; and some account statements showed impossible dividends. The Court applied the pleading criteria of *Ashcroft v. Iqbal*, 556 U.S. 662 (2009) and *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544 (2007).

Notwithstanding the harsh allegations, the Court ruled that "allegations of the Amended Complaint do not plead a plausible claim that [the Defendants] … actually knew that Madoff was not trading securities. . . The "red flag" theory of scienter has been rejected in the Madoff-related federal securities law litigation because it amounts to pleading fraud by hindsight. . . . Hindsight is infallible, but connecting the dots in real time may require clairvoyance. In many cases, it requires a regular comparison of information in [Madoff] generated trade confirmations and monthly account reports with market information. Even if the comparison is made, many red flags are no more than pale pink especially when they crop up infrequently over a long period. . . [W]hile [the Complaint] alleges the first prong of willful blindness – [the Defendant] strongly suspected that, at a minimum, [Madoff's] option trades were not real -- it does not allege the second prong, that [the Defendant] turned a blind eye to its suspicions. Instead, it alleges that [the Defendant] hired [a third party] to conduct due diligence regarding Madoff's trades for [the Defendant's] account." It remains to be seen whether the Trustee will be able to replead the counts that were rejected.

Deutsche Bank Trust Co. Ams. v. Large Private Beneficial Owners (In re Tribune Co. Fraudulent Conveyance Litig.), **No. 13-3992, 2016 U.S. App. LEXIS 5787 (2d Cir. N.Y. Mar. 29, 2016)**

The Second Circuit found that the Bankruptcy Code's securities safe harbor of § 546(e) barred avoidance for constructive fraudulent transfer (and excluding avoidance based on "intent to hinder, delay or defraud …") against former holders of common equity whose shares had been subject to mandatory redemption in a pre-petition "going-private" LBO transaction. The District Court had previously held that bondholders could not pursue avoidance of the redemption under state fraudulent transfer laws because they were preempted by the Trustee's avoidance rights under §§ 548 and 550. The question of whether the Trustee might be barred by the safe harbor was reserved. The District Court prudently suspended activity in the litigation while the Second Circuit pondered the appeal. The Second Circuit first found that the bondholders were not preempted after all, because standing to pursue avoidance under the state statute had revested in them due both to plan confirmation and the express provisions of the plan. However, the Second Circuit then went on to find that pre-petition transaction to mandatorily redeem equity was barred by the safe harbor defense. (No word yet on a motion for rehearing or petition for certiorari, so check back on this one later.)

Weisfelner v. Blavatnik (In re Lyondell Chem. Co.), 543 B.R. 127 (Bankr. SDNY 2016)

In a far ranging opinion dealing among other things with *in personam* jurisdiction and motions to dismiss, Bankruptcy Judge Gerber found, on the subject of the extraterritorial reach of property of the estate, "[t]his Court agrees with Professor Westbrook [*Avoidance of Pre-Bankruptcy Transactions in Multinational Bankruptcy Cases*, 42 TEX. INTL L.J. 899] that section 541(a)(3) of the Bankruptcy Code supports a finding that Congress intended section 548 to extend extraterritorially. Section 541(a)(3) provides that any interest in property that the trustee recovers under section 550 becomes property of the estate. Section 550 authorizes a trustee to recover transferred property to the extent that the transfer is avoided under either section 544 or section 548. It would be inconsistent (such that Congress could not have intended) that property located anywhere in the world could be property of the estate once recovered under section 550, but that a trustee could not avoid the fraudulent transfer and recover that property if the center of gravity of the fraudulent transfer were outside of the United States."

In re Berau Capital Resources PTE, Ltd., (Bankr. SDNY, Case No. 15-11804 (MG), Oct. 28, 2015)

In this Chapter 15 case, Bankruptcy Judge Glenn held that a debt indenture governed by New York law constitutes "property in the United States." Accordingly, the debt indenture was found to satisfy the § 109(a) requirement of "property in the United States," an issue which Judge Glenn thought "likely to recur in other cases."

Third Circuit:

Official Comm. of Unsecured Creditors v. CIT Grp./Bus. Credit Inc. (In re Jevic Holding Corp.), 787 F.3d 173 (3d Cir. Del. 2015)

Chapter 11 bankruptcy cases can be resolved through a structured dismissal that deviates from the Bankruptcy Code priority system.

Tribune Media Co. v. Aurelius Capital Mgmt., L.P., 799 F.3d 272, 274 (3d Cir. Del. 2015)

The Third Circuit Court of Appeals deemed one appeal equitably moot because it attempted to undo a crucial component of the already consummated plan of reorganization. A second appeal, which sought disgorgement of funds from other creditors, was not equitably moot because it was found not to jeopardize the plan of reorganization or harm third parties who had justifiably relied on plan confirmation.

In re LCI Holding Co., 802 F.3d 547 (3d Cir. Del. 2015)

Senior lenders could distribute non-estate property to lower-ranked creditors in order to resolve objections as long as the property distributed is not property of the estate.

Delaware Trust Co. v. Wilmington Trust, N.A. (In re Energy Future Holdings Corp.), 546 B.R. 566 (Bankr. D. Del. 2016)

On a complex set of facts and agreements, the Bankruptcy Court (Sonchi, J.) found that the adequate protection payments and distributions under a plan of reorganization were governed by the priority structure of the Bankruptcy Code and the plan of reorganization, and not by the terms of an otherwise applicable intercreditor agreement. In reaching its decision, the court determined that distributions to secured creditors pursuant to a plan of reorganization are not, per se, distributions of collateral or proceeds thereof.

In re Millennium Lab Holdings II, LLC, 543 B.R. 703 (Bankr. Del. 2016)

The Bankruptcy Court (Silberstein) certifies for direct appeal to the Third Circuit from the confirmation of a plan of reorganization which entailed nonconsensual third party releases. The certification of direct appeal was based on Judge Silberstein's finding that her confirmation order was in conflict with *In re Washington Mutual, Inc.*, 442 B.R. 314 (Bankr. D. Del. 2011). "[T]he *Washington Mutual* court stated … 'This Court has previously held that it does not have the power to grant a third party release of a non-debtor … Rather, any such release must be based on consent of the releasing party (by contract or the mechanism of voting in favor of the plan).' … My decision is to the contrary."

In re Trump Entm't Resorts Unite Here Local 54, 810 F.3d 161 (3d Cir. Del. 2016)

Section 1113 of the Bankruptcy Code allows debtor-employers to reject the continued term of a CBA even after the CBA has expired.

Seventh Circuit:

Grede v. Bank of N.Y. Mellon Corp. (In re Sentinel Mgmt. Grp.), 809 F.3d 958 (7th Cir. 2016)

Reversing the district court and holding that the trustee for a failed investment management firm established at trial that the bank should have known that pledged collateral actually belonged to the firm's customers, and that because the bank did not accept the collateral in good faith its liens were avoidable as fraudulent transfers.

The bank had "inquiry notice" and therefore was not acting in good faith when it accepted a pledge of assets from the Debtor. "The term [inquiry notice] signifies awareness of suspicious facts that would have led a reasonable firm, acting diligently, to investigate further and by doing so discover wrongdoing." Here, the bank had sufficient information to create the "requisite suspicion" when the bank's managing director sent an email to a colleague asking "How can [the Debtor] have so much collateral? With less than $20MM in capital I have to assume most of this collateral is for somebody else's benefit. Do we really have rights on the whole $300MM?"

Peterson v. McGladrey, LLP**, 792 F.3d 785 (7th Cir. 2015)**

Holding that the *in pari delicto* doctrine barred the trustee's malpractice claims against bankrupt mutual funds' former auditor because the debtors and their principals themselves engaged in wrongdoing, even where – as argued by the trustee – the auditor's wrongdoing was different from that of the debtors and their principals.

Ninth Circuit:

Zachary v. California Bank & Trust, **No. 13-16402, 2016 U.S. App. LEXIS 1368 (9th Cir. Jan. 28, 2015)**

The Ninth Circuit overruled *In re Friedman*, 466 B.R. 471 (Bankr. 9th Cir. 2012) and held that the absolute priority rule still applies in individual chapter 11 cases. This decision is also notable for what the Ninth Circuit did not decide -- in a footnote, the Court comments on, but elects not resolve the split of authority as to whether bankruptcy courts are bound by BAP decisions.

Ozenne v. Chase Manhattan Bank (In re Ozenne), **No. 11-60039, 2016 U.S. App. LEXIS 5602 (9th Cir. Mar. 25, 2016)**

The Ninth Circuit determined *sua sponte* that the Ninth Circuit BAP did not have jurisdiction to entertain an application for writ of mandamus, even though the BAP had denied the application. Even though *Stern v. Marshall* is in the discussion, it is not cited as the sole or even main basis for this determination.

Grasslawn Lodging, LLC v. Transwest Resort Props.**, 801 F.3d 1161 (9th Cir. 2015)**

The Ninth Circuit held that an appeal of a confirmation order was not equitably moot even though the plan had been substantially consummated because the lender had diligently sought a stay and it would be possible to fashion an equitable remedy to at least partially address the lender's objections.

Double Bogey, L.P. v. Enea**, 794 F.3d 1047 (9th Cir. 2015)**

The Ninth Circuit held that, even if two individuals were the alter egos of a corporate fiduciary, they were not "fiduciaries" of a creditor within the meaning of section 523(a)(4).

U.S. Bank v. Village at Lakeridge, LLC (In re Village at Lakeridge, LLC)**, Nos. 13-60038, 13-60039, 2016 U.S. App. LEXIS 2307 (9th Cir. Feb. 8, 2016)**

The Ninth Circuit held that a plan proponent may rely on a vote cast by a creditor who bought his claim from a statutory insider to satisfy the requirement that its plan be accepted by at least one impaired consenting class.