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1. ACCOUNTANT LIABILITY - - NO LIABILITY TO THIRD PARTY

Overland Leasing Group, LLC v. First Financial Corporate Services, Inc., 2011 WL 2649713 (3d Cir. 2011) - - Accounting firms were sued by the seller of equipment to the firms' client. The seller argued that the accounting firms had negligently prepared the client's financial statements, upon which the seller allegedly relied in extending a credit sale to the client. The Third Circuit ruled, in a non-published decision, that the accounting firms had no liability to the seller, who was not their client. Neither accounting firm communicated with the seller regarding the purchase transaction. Furthermore, neither of the accounting firms were shown to have known or understood that the seller was relying on any representation made by either firm.

2. ALLOWANCE OF CLAIM - - DEFICIENCY CLAIM FOLLOWING NON-JUDICIAL FORECLOSURE

In re Cox, 456 B.R. 592 (Bankr. N.D. Ga. 2011) - - The lender made successive loans to a corporate borrower. Each of the loans were secured by separate parcels of real property. However, pursuant to a dragnet clause in the loan agreement, each parcel cross-collateralized the other loans. The lender foreclosed on one parcel but failed to obtain judicial confirmation of the non-judicial foreclosure sale, as required by Georgia law in order to obtain a deficiency. The bankruptcy court found that the failure to obtain confirmation of the first foreclosure sale did not preclude the lender from pursuing a deficiency on the second and third loans and did not require disallowance of a proof of claim filed by the lender with respect to these deficiencies in the bankruptcy case of the guarantors of the corporate debt.

3. DEFAULT RATE OF INTEREST - - SOLVENT DEBTOR

In re Del-A-Rae, Inc., 448 B.R. 303 (Bankr. S.D. Ga. 2011) - - The creditor held notes that matured prior to the debtor's bankruptcy case. The creditor who held the notes was over-secured by collateral of the debtor. The notes provided for a post-maturity default rate of interest. The post-maturity rate did not violate state law. The debtor urged that the post-petition interest rate on the notes should not be the post-maturity rate. The bankruptcy court ruled in favor of the creditor. The equities did not favor precluding the creditor's use of the post-maturity rate, as the debtor was solvent and any decrease in the interest rate would only inure to the benefit of the debtor after bankruptcy. Accordingly, the creditor was entitled to accrue interest at the post-maturity rate from the commencement of the bankruptcy case through confirmation of the debtor's plan.

4. ENFORCEABILITY OF FORBEARANCE AGREEMENT - - ABSENCE OF CONSIDERATION

In re 400 Walnut Associates, L.P., 454 B.R. 60 (Bankr. E.D. Pa. 2011) - - The borrower/mortgagor filed suit against the lender/mortgagee. The borrower alleged that, in exchange for the borrower's resumption of its obligation to collect rents, to pay the expenses of the property and remit the net amounts to the lender, the lender had agreed to terminate a foreclosure action and forbear from further exercise of contractual remedies based on the borrower's previous defaults. The lender filed a motion to dismiss the complaint. The bankruptcy court found that, while the complaint may have sufficiently pled the parties' mutual assent to the terms of an alleged forbearance agreement, the complaint was devoid of any allegation of consideration provided by the borrower. Other than the resumption of performance of contractual duties that the borrower was already obligated to perform, the complaint did not allege any other consideration. Hence, the borrower failed to plead the existence of an enforceable forbearance agreement and did not state a cause of action against the lender for breach thereof.

5. CONFIRMATION OF PLAN - - "DIRT FOR DEBT" PLAN

In re Riddle, 444 B.R. 681 (Bankr. N.D. Ga. 2011) - - The bank rejected the Chapter 11 plan filed by the debtor and objected to confirmation. The bankruptcy court determined that the plan met all confirmation requirements in Section 1129(a) except the requirement that all classes of impaired claims accept the plan, a requirement that the debtor could not meet because of the bank's rejection of the plan as the sole member in its class. The debtor invoked the "cram-down" provisions of Section 1129(b) of the Bankruptcy Code pursuant to which the bank would be forced to accept a surrender of approximately 36 acres of real property, asserted by the debtor to be worth $1.2 million and on which the bank held a first lien, in satisfaction of the bank's claim of approximately $907,000. The Effect of the surrender of the 36 acres of real property to the bank would be to force the bank to release its second priority lien on a condominium unit. The bankruptcy court first noted that Section 1129(b)(2)(A) requires for cram-down confirmation that a plan must be "fair and equitable." To be fair and equitable, a plan may, among other things, provide for the secured creditor to receive the "indubitable equivalent" of its claim. The evidence demonstrated that the 36 acres to be deeded to the bank at confirmation would likely sell for a price in the range of $1.2 million to $1.3 million and would net at least $940,000 at a "fire sale." With respect to the condominium unit on which the bank held a second lien, the net amount realizable was only $100,000 after payment of the first lien. The debtor testified that the release of the bank's second lien on the condominium unit was necessary to allow the debtor to utilize the property as collateral for additional financing for one of his companies, which was essential to feasibility of the plan. The court ruled that a "dirt for debt" plan may, under appropriate circumstances, provide the indubitable equivalent of the lender's claim. In order for treatment of a secured creditor's claim to qualify as being the "indubitable equivalent" of the claim, the treatment must be "completely compensatory." In other words, there must be no "reasonable doubt" that the creditor will be paid in full. When the plan proposes to transfer some, but not all, of the collateral to the creditor in satisfaction of its claim, the court must take a conservative approach to valuation to protect the secured creditor. The uncontroverted evidence before the court established that the fire sale value of the 36 acres, which reflected a discount of $200,000 from what the property could be sold for if it were marketed in the usual manner, covered the amount of the secured obligation of the bank, after first deducting taxes and closing costs. In addition, the fire sale amount is sufficient to cover principal and six months of interest owed to the bank.

6. PERFECTION OF SECURITY INTEREST - - EFFECT OF UNAUTHORIZED TERMINATION STATEMENT

AEG Liquidation Trust v. Toobro NY LLC, 2011 WL 2535035 (N.Y. Sup. Ct. 2011) - - This case involved a priority dispute between two secured creditors with liens on the same assets of the debtor. The first priority creditor's financing statement was terminated by the debtor, without the knowledge or consent of the first priority creditor. The debtor then sought a loan from the second priority creditor, which conducted a lien search and found no outstanding lien on assets of the debtor. Thereafter, the first priority creditor learned of the unauthorized termination and filed a "correction statement" pursuant to UCC § 9-518. In the correction statement, the first priority creditor explained that the termination statement filed by the debtor was not an authorized filing. The New York court agreed with the first priority creditor. The termination statement filed by the debtor was a nullity. In so ruling, the court rejected a contrary ruling by the Southern District of New York in Roswell Capital Partners LLC v. Alternative Const. Technologies, 2010 WL 3452378 (S.D.N.Y. 2010). In rejecting the reasoning of the district court in Roswell Capital Partners, the court noted that the district court had not cited any UCC provisions in support of its ruling. The UCC clearly establishes a general rule that an unauthorized termination statement has no effect (UCC §§ 9-513(d) and 9-510(a)). In addition, the court rejected the policy considerations offered by the district court in support of its ruling, to the effect that the UCC places "the burden of monitoring for potentially erroneous UCC-3 filings on existing creditors, who are aware of the true state of affairs as to their security interests, rather than potential creditors who will not be in the position to know whether a termination statement was authorized or not."

7. TRIANGULAR SETOFF - - MUTUALITY REQUIREMENT

In re Lehman Brothers, Inc., 458 B.R. 134 (Bankr. S.D.N.Y. 2011) - - Lehman Brothers and UBS entered into a swap agreement pursuant to which each posted collateral to secure their respective obligations to the other. Thereafter, the parties entered into numerous foreign exchange transactions in accordance with the swap agreement. Upon termination of the swap agreement, UBS provided a notice of calculation of an "early termination amount," part of which was based on a setoff right that UBS asserted pursuant to the swap agreement with respect to amounts allegedly due from Lehman Brothers to an affiliate of UBS. The trustee in the Lehman Brothers bankruptcy case disputed the validity of any triangular setoff right, irrespective of any language in the swap agreement that allowed for a triangular setoff. The trustee then sought enforcement of the automatic stay and to compel UBS to pay the excess collateral relating to the triangular setoff to Lehman Brothers. In granting the motion of the trustee, the bankruptcy court ruled that a contractual right of setoff that permits netting by multiple affiliated members of the same corporate family outside of bankruptcy may no longer be enforced after the commencement of a bankruptcy case. Contractual provisions that purport to create "synthetic mutuality" are not authorized under the Bankruptcy Code, the bankruptcy court reasoned. In so ruling, the bankruptcy court agreed with In re SemCrude L.P., 399 B.R. 388 (Bankr. D. Del. 2009).

8. AUTOMATIC STAY - - PRE-PETITION WAIVER

In re DB Capital Holdings, LLC, 454 B.R. 804 (Bankr. D. Colo. 2011) - - As part of a pre-petition forbearance agreement with the lender, which held a deed of trust against the debtor's sole real estate asset, the debtor waived any right that it might have to oppose the lender's motion for stay relief in a later filed bankruptcy case by the debtor. After the debtor filed for bankruptcy, the lender moved for relief from the automatic stay, contending, among other things, that it was not adequately protected and that, in any event, the debtor had waived its right to protection of the automatic stay. The bankruptcy court declined to give effect to the pre-petition waiver of the stay, finding that such a waiver was unenforceable because it was too closely akin to a waiver of the right to file for bankruptcy relief. However, the court granted the lender's motion because it found that the debtor had failed to provide adequate protection to the lender. The lender's proposal to complete the partially developed real estate project and five years later commence payments to the lender was speculative and there was no proof by the debtor of its ability to prove that the real property was necessary to "an effective reorganization."

9. FRAUDULENT TRANSFER - - JOINDER OF INITIAL TRANSFEREE

In re Brooke Corp., 443 B.R. 847 (Bankr. D. Kan. 2010) - - The Chapter 7 trustee sued a subsequent transferee of an alleged fraudulent transfer, but failed to join the initial transferee. The defendants moved to dismiss for failure to join the initial transferee as an indispensible party. The bankruptcy court granted the motion. It first found that the absent party was necessary and that joinder of the party was feasible. If a court determines that the absent party is necessary but cannot be joined, the court must then ascertain whether the party is indispensible. If so, the dismissal motion must be granted. The party moving to dismiss for failure to join an indispensible party bears the burden of showing the nature of the unprotected interests of the absent individuals and the possibility of injury to them or that the parties before the court will be disadvantaged by their absence. In this case, the bankruptcy court ruled that the initial transferee was necessary and that joinder was required if feasible.

10. AUTOMATIC STAY - - BANK'S IMPOSITION OF DEBIT RESTRAINT

In re Randolph Towers Coop., Inc., 458 B.R. 1 (Bankr. D.D.C. 2011) - - Shortly after the debtor filed for Chapter 11 relief, the bank sent to the debtor a letter advising that the bank was required by Section 542 of the Bankruptcy Code to act in good faith to prevent the payment of pre-petition debts from the debtor's pre-petition bank accounts. In furtherance of that obligation, the letter advised that the bank had placed a "debit restraint" on the debtor's pre-petition bank accounts until the bank was provided with a court order that allowed the debtor to continue to use the bank accounts. The letter went on to state that the bank would issue a cashier's check payable the debtor-in-possession or transfer funds to a debtor-in-possession bank account opened with the bank. The debtor responded with a motion for sanctions against the bank on the grounds that the imposition of the debit restraint was an act to exercise control over estate property in violation of Section 362(a)(3) of the Bankruptcy Code. Denying the requested relief, the bankruptcy court found that the bank had not exercised control over any estate property inasmuch as the property remained intact, and, at most, the bank had simply failed to perform a contract. Furthermore, even if the bank had violated Section 542(b) of the Bankruptcy Code, which requires an entity that owes a debt that is estate property and is matured to pay the debt to the trustee except to the extent of any allowable offset, such a violation could not serve as the basis for a finding of contempt. The turnover requirement in Section 542(b) is not a court order and cannot form the basis for a contempt action.

11. VALIDITY OF LIEN - - ECONOMIC VALUE OF FCC LICENSE

In re TerreStar Networks, Inc., 457 B.R. 254 (Bankr. S.D.N.Y. 2011) - - At issue was whether or not senior secured noteholders had a valid lien on the economic value associated with a broadcast license issued by the FCC to the Chapter 11 debtor. The bankruptcy court ruled that, while the noteholders could not obtain a lien on the license itself, the debtor's grant pursuant to the security agreement of a security interest in a right to receive proceeds or other consideration in connection with the sale, transfer or other disposition of any FCC licenses by the debtor was valid under the New York UCC.

12. LENDER LIABILITY - - APPLICATION OF TRUST FUNDS TO LOAN BALANCE

In re Arctic Exp. Inc., 636 F.3d 781 (6th Cir. 2011) - - In this class action, the plaintiffs, owner-operators who had entered into contractual arrangements with the debtor and its affiliate pursuant to independent contractor agreements and lease agreements, sought restitutionary relief against the debtor's bank. The plaintiffs provided hauling services to the debtor with tractor-trailers leased from the debtor's affiliate. Their compensation consisted of a percentage of amounts that the debtor received from its customers. Under the lease agreements, the debtor would deduct nine cents per mile for maintenance and the maintenance escrow funds were non-refundable if the lease was terminated by either party before the end of the lease's term. Alleging the bank's violations of the Motor Carrier Act's Truth-in-Leasing Regulations, the plaintiffs argued that the maintenance funds were subject to the regulations because they fell within the definition of "escrow fund." The debtor had a revolving asset-based lending line of credit with the bank and maintained its depository accounts with the bank. Funds were advanced under the line of credit to the debtor's depository/operating account and payments from customers went directly into a cash collateral account controlled by the bank and applied to the loan balance. The plaintiffs sought from the bank restitution or disgorgement of the maintenance escrow funds that were used by the bank to pay down the revolving line of credit. From an order of summary judgment granted by the district court in favor of the bank, the plaintiffs appealed. The Sixth Circuit agreed with the district court's ruling that the applicable Truth-in-Leasing Regulations impressed the maintenance escrow funds with the statutory trust, but reversed the decision that the plaintiffs could not recover those funds from the bank. Any monies paid from the cash collateral account consisting of funds impressed with the statutory trust was a breach by the debtor of its fiduciary duties. Accordingly, the plaintiffs were authorized to recover from the bank the escrow funds impressed with the trust from the bank.

13. CONFIRMATION OF PLAN - - TEMPORARY INJUNCTION TO PREVENT LENDER'S COLLECTION EFFORTS AGAINST GUARANTORS

In re Linda Vista Cinemas, LLC, 442 B.R. 724 (Bankr. D. Ariz. 2010) - - The bank's loan was guaranteed by the principal of the debtor. After the debtor defaulted on the loan, the bank sued the guarantors in state court to collect under the guaranty. The debtor filed for Chapter 11 and obtained from the bankruptcy court an order temporarily staying the state court actions against the guarantors. The debtor's reorganization plan provided that the lender's claims were to be paid in full over a period of seven years and that the guarantors would be responsible under their guaranty for such payments. However, the plan barred the lender from continuing to sue the guarantors as long as the installment payments were paid when due under the plan. The lender objected to confirmation, pointing to Section 524(e) of the Bankruptcy Code, which provides that the discharge of a debtor's obligations cannot affect the liability of any other entity for such debt. The temporary injunction, the bank argued, was tantamount to a discharge of the guarantors in violation of Section 524(e). The debtor argued that the stay of collection efforts was essential to the ultimate success of the plan, particularly in light of the fact that the guarantors had agreed to contribute approximately $437,000 over time to fund payments under the plan. Absent the injunction, the guarantors would be unable to fund the plan payments and the plan would fail. The bankruptcy court sided with the lender, finding that the temporary injunction of collection efforts violated Section 524(e).

14. FRAUDULENT TRANSFER - - PROCEEDS OF REFINANCING LOAN

In re TOUSA, Inc., 444 B.R. 613 (S.D. Fla. 2011) - - The debtor had guaranteed loans to various lenders and, after the commencement of litigation on the debtor's guaranty, a settlement was reached pursuant to which the debtor agreed to pay the lenders the sum of $421 million. To finance the settlement, the debtor obtained new loans that were made jointly to the debtor and its subsidiaries (each of which agreed to be co-borrowers with respect to the new loans and to grant liens on their assets to secure repayment of the new loans). After the debtor filed for Chapter 11 relief, the official committee of unsecured creditors sued the lenders on behalf of the subsidiaries to avoid as fraudulent transfers the settlement payment to the lenders and the liens granted and obligations incurred by the subsidiaries. The bankruptcy court ruled in favor of the committee, concluding that the transactions constituted fraudulent transfers for which the old lenders and the new lenders were liable and ordered disgorgement of an amount exceeding $480 million. The district court reversed the bankruptcy court's conclusion that the old lenders were liable (i) as direct transferees of the proceeds of the new loans and (ii) as the entities "for whose benefit" the subsidiaries granted liens and incurred obligations to the new lenders. Under Section 548 of the Bankruptcy Code, the old lenders could not be liable under a direct transferee theory of liability unless the subsidiaries had a property interest in the new loans. Here, no such property interests existed because, even though the subsidiaries were co-borrowers with respect to the new loans, the debtor had sole control over the disposition of the loan proceeds. Because they did not have any such control, the subsidiaries did not have a property interest in the new loans and the payment to the old lenders did not constitute a fraudulent transfer by the subsidiaries. The bankruptcy court's alternative theory of liability was that under Section 550 of the Bankruptcy Code recovery could be had from the old lenders as the entities "for whose benefit" the subsidiaries granted liens and incurred obligations to the new lenders. The district court ruled that Section 550 does not permit recovery from the old lenders since they were mere incidental beneficiaries of the liens granted and obligations incurred to the lenders. In short, the old lenders were too far removed from the transaction to be liable for a fraudulent transfer under Section 550 of the Bankruptcy Code. Finally, the district court overruled the bankruptcy court's conclusion that the liens granted and the obligations incurred by the subsidiaries to the new lenders were subject to avoidance as fraudulent transfers on the grounds that the subsidiaries allegedly did not receive reasonably equivalent value. The district found that "indirect benefits" could be considered reasonably equivalent value and that the subsidiaries in fact received reasonably equivalent value by virtue of avoiding bankruptcy or an impending default (even if only temporarily), maintaining continued access to financing through downstream loans from the parent and avoiding the entry of a judgment against the parent that would have triggered their liability under various guaranties.

15. PROPERTY OF ESTATE - - FACTORED ACCOUNTS

In re Siskey Hauling Co., Inc., 456 B.R. 597 (Bankr. N.D. Ga. 2011) - - The factor and the debtor entered into a factoring agreement prior to the debtor's commencement of its Chapter 7 case. Pursuant to the factoring agreement, the factor agreed to purchase the debtor's accounts receivable. However, the factoring agreement provided that the factor would have recourse against the debtor depending upon the collectibility of the accounts. As a result of this recourse arrangement, the purchase transactions did not constitute a true sale of the accounts receivable. Instead, the factoring arrangement was more in the nature of a secured transaction, as the risk of loss remained with the debtor. In light of the debtor's risk of loss, the debtor retained an interest in the accounts as of the commencement of the bankruptcy case and the accounts receivable constituted property of the estate under Section 541 of the Bankruptcy Code.

16. AUTHORITY TO APPEAL - - FORMER MANAGEMENT OF INVOLUNTARY DEBTOR

In re C.W. Mining Co., 636 F. 3d 1257 (10th Cir. 2011) - - An involuntary petition was filed against a corporate debtor. The bankruptcy court sustained the petition and a Chapter 7 trustee was appointed. Former management of the corporate debtor filed a notice of appeal of the order sustaining the involuntary petition. Reversing a decision of the bankruptcy appellate panel, the Tenth Circuit Court of Appeals held that, after a Chapter 7 trustee is appointed, the authority to make legal decisions for the debtor passed to the trustee. Accordingly, former management was divested of authority to act on the debtor's behalf. The United States Supreme Court denied certiorari from the Tenth Circuit's ruling, leaving unaddressed the argument that the effect of the Tenth Circuit's holding was to eliminate appellate review of orders for relief in involuntary Chapter 7 cases.

17. POST-CONFIRMATION PROSECUTION OF CLAIMS - - ADEQUACY OF RETENTION UNDER PLAN

In re Crescent Resources, LLC, 455 B.R. 115 (Bankr. W.D. Tex. 2011) - - At issue in this case was whether the debtor's plan adequately preserved, pursuant to Section 1123(b)(3) of the Bankruptcy Code, a right to pursue a post-confirmation turnover action. The bankruptcy court viewed the issue in the context of the Fifth Circuit's opinion in In re United Operating, LLC, 540 F.3d 351 (5th Cir. 2008), where the Fifth Circuit ruled that the plan of reorganization must "specifically and unequivocally" retain a cause of action as a condition to the debtor or liquidating trustee having standing to pursue the cause of action after confirmation of the plan. The plan in this case provided for the establishment of a liquidation trust, the assets of which would include causes of action "arising under Chapter 5 of the Bankruptcy Code," including those that could be brought under Sections 544, 547, 548, 549, 550 and 551 of the Bankruptcy Code, against any person or entity. The language in question did not specifically mention either Section 542 or turnover causes of action pursuant to that section. Nevertheless, while finding that a blanket retention would not satisfy the Fifth Circuit's requirements in United Operating, the court concluded that the language in question was "specific and unequivocal" to retain a turnover cause of action under Section 542. The court reasoned that it was "far-fetched" to believe that a creditor would not be on notice that the liquidating trust anticipated pursuing turnover claims after confirmation and that a creditor "could not feign surprise" that the trust would pursue a claim under Section 542. While the plan language was "more generic than language considered in other cases," the court felt "that it was sufficient to put creditors voting on the Plan on notice that 542 turnover claims may be pursued."

18. FRAUDULENT OBLIGATION - - DOWNSTREAM GUARANTY

In re Renegade Holdings, Inc., 457 B.R. 441 (Bankr. M.D.N.C. 2011) - - At issue was whether a Chapter 11 trustee's complaint to avoid, as a fraudulent obligation, the debtor's guaranty of its subsidiary's obligations was sufficient to withstand a motion to dismiss. The trustee alleged that the guaranty was executed with respect to a loan the proceeds of which were advanced entirely to the subsidiary; and both the debtor and its subsidiary were insolvent at the time of the loan and the guaranty. Based on these allegations, the complaint sufficiently pled lack of any benefit, direct or indirect, to the debtor and therefore an absence of any "reasonably equivalent value." Accordingly, the trustee stated a claim for avoidance of the guaranty as a constructively fraudulent obligation.

19. ARBITRATION IN BANKRUPTCY - - CORE MATTER

In re Salander O'Reilly Galleries, 453 B.R. 106 (Bankr. S.D.N.Y. 2011) - - The debtor's Chapter 11 plan established a liquidation trust. A pre-petition consignor of artwork to the debtor's art gallery moved for relief from the automatic stay to enforce a choice of law clause in the consignment agreement and to pursue arbitration of claims under applicable foreign law in a foreign proceeding. The liquidation trust under the plan opposed the motion, contending that the consignment arrangement was subject to avoidance under Section 544 of the Bankruptcy

Code. The bankruptcy court found that it had discretionary authority to deny the enforcement of the arbitration clause, despite the fact that the Federal Arbitration Act manifests a strong Congressional policy in favor of arbitration. Denial of arbitration was warranted because the consignor held an allegedly unperfected security interest in the artwork consigned to the debtor prior to bankruptcy and sought to arbitrate in a foreign proceeding issues regarding the priority of the trust's interest in the artwork. The trust was asserting rights derived under the Bankruptcy Code's strong-arm powers under Section 544 of the Bankruptcy Code. The dispute between the trust and the consignor was substantively a core matter and therefore denial of arbitration was in the discretion of the bankruptcy court given the impact that the outcome of the dispute would have on the estate.

20. INVOLUNTARY PETITION - - STANDING TO CHALLENGE

Zais Inv. Grade Ltd. VII, 455 B.R. 839 (Bankr. D.N.J. 2011) - - Junior note holders of the debtor moved to dismiss the involuntary petition filed by senior note holders The bankruptcy court ruled that the junior note holders lack standing to challenge the qualifications of the creditors that filed the involuntary petition and could not raise the petitioners' alleged ineligibility to join in the filing of the involuntary petition.

21. VOIDABLE PREFERENCE - - MERE CONDUIT DEFENSE

In re Robert Plan of New York Corp., 456 B.R. 150 (Bankr. E.D.N.Y. 2011) - - The debtors made payments to a tort plaintiff pursuant to a settlement agreement entered into prior to bankruptcy. The payments were made to the tort claimant's law firm, which placed the funds in its escrow account. Thereafter, the claimant's law firm disbursed 70% of the settlement amount to the claimant and then transferred 30% of the settlement payment to the law firm's operating account in payment of their contingency fee. After bankruptcy, a preference suit was filed against both the claimant and her law firm. The claimant settled, but the suit against the law firm continued. The bankruptcy court first determined whether the transfers to or for the benefit of the claimant were voidable, and concluded that all of the elements for a preference existed. The bankruptcy court then turned to the question whether the law firm could be liable as the "initial transferee" for the amounts that it received in its escrow account and forwarded on to the claimant. The bankruptcy court ruled that the law firm had a duty to transmit the monies to the claimant and therefore was a "mere conduit" of the money for the benefit of the client. A mere conduit, the bankruptcy court ruled, could not be an "initial transferee" of the preferential transfer under Section 550 of the Bankruptcy Code. However, the question remained whether the payments that the law firm received when it transferred monies from its escrow account to its operating account in payment of its contingency fee were recoverable preferences from the law firm as a mediate or immediate transferee under Section 550 of the Bankruptcy Code. The bankruptcy court found that the law firm transferred the money and paid its contingency fee in good faith, for value, and without knowledge of the voidability of the transfer, despite the firm's awareness of conflicting rumors regarding the debtors' financial status. As a result, the good faith defense applied under Section 550 to preclude the trustee's recovery of the avoided transfers from the firm.

22. ENTRY OF MONEY JUDGMENT ON AVOIDED TRANSFER - - CONSTITUTIONAL AUTHORITY OF BANKRUPTCY COURT

In re Teleservices Group, Inc., 456 B.R. 318 (Bankr. W.D. Mich. 2011) - - In this case, the bankruptcy court ruled that a bankruptcy court, as a non-Article III court, lack constitutional authority to enter a money judgment against the transferee on an avoided transfer unless otherwise consented to by the parties. Absent such consent, the bankruptcy court could only issue a report and recommendation to the district court to allow the district court to make an independent assessment of the trustee's claims and the transferee's defenses.

23. FRADULENT TRANSFER - - INITIAL TRANSFEREE

In re CNB International, Inc., 440 B.R. 31 (W.D.N.Y. 2010) - - A litigation trust established under the debtor's Chapter 11 plan recovered approximately $12.9 million from a bank in connection with a constructively fraudulent conveyance. On appeal, the issue presented was whether the bank was an initial transferee of the funds in question that were part of the constructively fraudulent conveyance so as to be subject to liability and recovery under Section 550 of the Bankruptcy Code. The constructively fraudulent conveyance arose out of the debtor's acquisition of assets of three entities, one of which held assets subject to liens in favor of third parties, including the bank. The acquisition transaction was found to be constructively fraudulent because the debtor conveyed approximately $11 million more to various parties than it received in exchange, and the debtor was rendered insolvent by the transaction. The bankruptcy court found that the bank did not constitute an initial transferee of the funds for purposes of Section 550(a)(1) of the Bankruptcy Code, but was a subsequent transferee that was not entitled to the good faith defense under Section 550(b) of the Bankruptcy Code inasmuch as the bank lacked good faith and had knowledge of the constructively fraudulent transfer. On appeal, the district court affirmed on other grounds. It first noted that the Bankruptcy Code does not define "initial transferee," but observed that courts had found an initial transferee to be an entity that has dominion and control over the transferred property and is not a mere conduit of that property. Here, the purchase consideration from the debtor was remitted to the three seller entities whose assets were being purchased. The seller entity whose assets were subject to the bank's liens transferred the funds to the bank in exchange for the release of the bank's liens. However, the district court noted, the debtor's transfer of funds to the seller entities was conditioned upon its transferring the money directly to the bank to obtain the bank's lien release. Accordingly, the seller whose assets was subject to the bank's liens was a mere conduit and did not have lawful dominion and control over the funds. Therefore, because the seller entity was a mere conduit, the bank was the initial transferee. The court went on to note that the bank did not act in good faith and had knowledge of the constructively fraudulent conveyance, but authorized certain offsets against liability.

24. ATTORNEYS' FEES PROVISION IN NOTE - - ALLEGED UNCONSCIONABILITY

BKB Properties, LLC v. SunTrust Bank, 2011 Fed. App. 0473N (6th Cir. 2011) - - The district court granted the bank's motion for recovery of $69,716 in fees and expenses from the borrower after having prevailed in a lawsuit brought by the borrower against the bank alleging breach of contract and fraud. The attorney fee provisions in the contract, literally read, authorized the bank to recover its fees and expenses even if it were not the prevailing party in litigation. The borrower argued that the provision was unconscionable under Tennessee law. While conceding that the provisions may have been one-sided, the Sixth Circuit Court of Appeals ruled that the provision was not facially unconscionable. The appeals court noted that, under Tennessee law, the provision was not sufficiently unfair and so one-sided as to "shock the judgment of the person of common sense." The provision was negotiated by sophisticated entities and the borrower was not presented with the contract terms on a "take it or leave it basis." The borrower could have negotiated a different version of the provision or demanded its removal.

25. CRAM-DOWN CONFIRMATION - - NEW VALUE

In re PHA Gliding Design, Inc., 55 BCD 33 (Bankr. N.D. Ga. 2011) - - The plan provided for the payment to 14 unsecured creditors in Class 3 an aggregate amount equal to 3% of the total amount of their claims (or $25,040 of the total $834,699 in claims) and annual salary to the debtor's owner during the 4 year term of the plan of $150,000 per year. The unsecured creditor class voted against the plan. The plan provided for the owner to retain 100% of his stock in consideration of the owner's commitment to fund 2011 projected operating losses of approximately $293,000. The court denied confirmation of the cram-down plan because it failed to satisfy the absolute priority rule under Section 1129(b)(2)(B)(ii) of the Bankruptcy Code. The owner did not provide a firm commitment of future payments to the debtor and declined to provide an up-front infusion of cash or its equivalent to satisfy the new value exception. For there to be "new value," the court stated, money or money's worth on the effective date of the plan is required. The owner testified that he would not and could not guarantee future payment of his commitment to fund operating losses, and therefore the court found no commitment really existed.

26. COMPOUNDING UNPAID INTEREST - - LOAN ASSIGNEE'S RETROACTIVE COMPOUNDING

In re 400 Walnut Associates, L.P., 2011 WL 5024289 (Bankr. E.D. Pa. 2011) - - During the period that it held the loan, a mortgage lender waived its right to compound unpaid interest. The assignee of the loan subsequently sought to compound interest retroactively for the time period prior to its purchase of the underlying note. The bankruptcy court ruled that, while the assignee was not authorized to compound the interest for the period prior to its acquisition of the note, it was authorized to compound interest for the time period after it bought the note absent evidence that the lender had bargained away the future right to compound interest.

27. VOIDABLE PREFERENCE - - ALLEGED NOVATION OF PRIOR PERFECTED LIEN

In re O&G Leasing, LLC, 456 B.R. 652 (Bankr. S.D. Miss. 2011) - - The debtor was indebted under debentures that were secured by the debtor's grant of a security interest in favor of the indenture trustee in various personal property assets of the debtor. Prior to the debtor's commencement of Chapter 11 relief, the debtor and the debenture holders agreed to a consolidation of the prior debentures and executed a new security agreement pursuant to which a security interest was granted in the same personal property of the debtor. However, the debenture trustee did not file a financing statement under the new security agreement for more than 30 days after the execution of the security agreement. The financing statement was filed within the 90-day period prior to bankruptcy. The debtor in its Chapter 11 case sought to avoid the debenture trustee's security interest as a preference under Section 547 of the Bankruptcy Code. The debtor contended that the new security agreement resulted in a novation of the old security agreement, thereby extinguishing the earlier grant of a security interest and leaving the new security interest exposed as a preferential transfer. The bankruptcy court ruled in favor of the debenture trustee. It first noted that the filing of the second financing statement did not result in any diminution or depletion of the debtor's estate for a preference to have occurred, because the debtor's assets were already subject to a prior perfected security interest, the financing statement for which had never been terminated. The amount of the prior debentures exceeded the amount of the consolidated debentures, and therefore the aggregate amount of secured indebtedness did not result in a reduction in the amount available for creditors. Turning to the issue of whether there was a novation when the second security agreement was executed, the bankruptcy court noted that under Mississippi law the parties must intend a novation for a novation to be accomplished, and the creditor must assent to the novation. Here, there was no evidence of an intended novation, debtor was never discharged from the previous contractual obligation and the original UCC financing statement was never terminated. There was never a point in time after the debtor entered into the first debenture agreement or after the signing of the second security agreement that the debenture trustee ever released the debtor from its obligations.

28. BANKRUPTCY COURT JURISDICTION - - LOCK-UP RESTRICTIONS ON NON-DEBTOR GUARANTORS UNDER PLAN

In re Safety Harbor Resort and Spa, 456 B.R. 703 (Bankr. N.D. Fla. 2011) - - The debtor's plan provided for the contribution of substantial assets from the principals of the debtor's parent company. The principals were also guarantors of the debt owed to a creditor. In exchange for the principal's contribution, the debtor requested releases for the principals as guarantors. The bankruptcy court instead imposed a four-year stay on any actions by the creditor against the guarantors. The creditor then requested that the court impose certain "lock-up" restrictions on the debtor's business operations as well as the guarantors to prevent the debtor and the guarantors from disposing of assets during the four-year injunction period toward any potential future collection efforts. The debtor objected to the restrictions on the non-debtor guarantors on the grounds that they exceeded the court's constitutional authority under the Supreme Court's decision in Stern v. Marshall. The bankruptcy court rejected the argument, finding that nothing in Stern limited a bankruptcy court's jurisdiction over "core matters" besides final judgments on counterclaims. In all events, parties can still consent, either expressly or impliedly, to a bankruptcy court's jurisdiction after Stern. Here, the guarantors, by virtue of their controlling interest in the debtor as proponent of a plan providing for the issuance of a third-party injunction, expressly and impliedly consented to the bankruptcy court's entry of final orders that, as a prerequisite to the entry of the injunction, barred the guarantors from disposing of their assets during the four-year period of the injunction.

29. USURY - - USE OF 365/360-DAY YEAR

Kreisler & Kreisler, LLC v. National City Bank, 657 F.3d 729 (8th Cir. 2011) - - The commercial borrower filed a class action lawsuit against the lender in which the borrower alleged that the lender had breached its contract with the borrower, and others, by charging interest in excess of the rate specified in the applicable promissory notes evidencing commercial loans. The promissory note in this case provided for a variable rate of interest over the lender's announced prime rate. Other provisions in the note stated that the calculation of interest would be on the basis of a 365/360-day year. The district court granted the lender's motion to dismiss for failure to state a claim. The Eighth Circuit affirmed. It found that the note's non-contradictory and unambiguous provisions were enforceable under Illinois law, rejecting the borrower's charge that by charging interest on a 365/360-day basis instead of a 365/365 time factor, the interest charges were 101.389% of the otherwise agreed upon rate. The note clearly disclosed that interest was based on a 365/360-day year, rather than a 365-day year, which, the appeals court noted, resulted in increasing the effective rate by .01389 in a non-leap year. Such a provision did not violate Illinois law.

30. RIGHT TO VOTE JUNIOR CREDITOR'S CLAIM - - CONTRACTUAL SUBROGATION

Avondale Gateway Ctr. Entitlement, LLC v. Nat'l. Bank of Ariz. (In re Avondale Gateway Ctr. Entitlement, LLC), 2011 WL 1376997 (D. Ariz. 2011) - - The debtor borrowed approximately $30.7 million from the first lien lender, whose loan was secured by a first lien mortgage on property of the debtor. The second lien lender loaned $18 million, secured by a second lien mortgage on the same property. The first lien and second lien lenders entered into a subordination and intercreditor agreement which provided that the second lien lender agreed that the first lien lender would be "subrogated to" the second lien lender with respect to the second lien lender's claims against the debtor and the second lien lender's rights, liens and security interests in any of the debtor's assets and proceeds thereof until the senior debt was paid in full, in cash. After the debtor filed for Chapter 11 relief and filed a plan of reorganization, the second lien lender voted to accept the plan, but the first lien lender cast two votes - - one in its own name to reject the plan and the other, as subrogee, to reject the plan on behalf of the second lien lender. After the bankruptcy court upheld the first lien lender's votes as appropriate, the debtor appealed. Although the subrogation clause did not expressly assign the second lien lender's voting rights to the first lien lender, the district court on appeal nevertheless ruled that the right to vote is a derivative right possessed by the holder of the claim in bankruptcy. Subrogation is the substitution of one party (the subrogee) in the place of another (the subrogor) with respect to a claim. The subrogee succeeds to all of the subrogor's rights with respect to the claim. Those rights include the right to vote the claim for or against a plan of reorganization. The district court rejected the debtor's argument that the first lien lender's right to subrogation did not arise until it paid the second lien lender's claims, as under Arizona law a right of subrogation can arise by contract. So-called "conventional" subrogation arises by contract, whereas "equitable" subrogation arises as a result of the payment of the subrogor's claim by the subrogee. When conventional subrogation rights exists, the language of the applicable contract governs when the subrogation rights are triggered. Because here the subrogation clause did not condition the exercise of contractual subrogation rights on payment of the second lien lender's claim, the rights were effective immediately and until the first lien lender's claims were paid in full.

31. JUDICIAL ESTOPPELL - - APPLICABILITY TO TRUSTEE

Reed v. City of Arlington, 650 F.3d 571 (5th Cir. 2011) (*en banc*) - - The debtor won a $1 million judgment against the City which appealed the judgment. The debtor filed for Chapter 7 relief, but did not disclose the judgment to the bankruptcy trustee and without advising his attorney of the bankruptcy. After the debtor's discharge, the City offered a judgment to the debtor's attorney who then learned for the first time of the bankruptcy. The attorney notified the Chapter 7 trustee, who had the case reopened and the discharge revoked. The Chapter 7 trustee then accepted the City's offer of judgment, but the City, which had filed a petition for rehearing on the judgment in the Fifth Circuit, sought leave to argue that the debtor should be judicially estopped from collecting the judgment due to his failure to disclose the judgment in his bankruptcy case. The Fifth Circuit remanded the matter to the district court, which held that judicial estoppel should not apply to the trustee even though it might apply to the debtor. The district court ruled that the trustee would be free to collect the judgment on behalf of the estate, but any funds remaining after payment of creditors would be refunded to the City rather than reverting to the debtor. The Fifth Circuit initially reversed, but on rehearing *en banc*, the Fifth Circuit held that, absent unusual circumstances, an innocent trustee can pursue for the benefit of creditors a judgment or cause of action that the debtor fails to disclose in bankruptcy.

32. ARBITRATION - - REQUIREMENT TO ARBITRATE PART OF DISPUTE

KPMG, LLC v. Cocchi, No. 10-1521 (U.S. Nov. 7, 2011) - - In a *per curiam* decision, the United States Supreme Court ruled that the Federal Arbitration Act must be enforced in both state and federal courts. Accordingly, in the case at bar, the Court vacated a Florida appellate court's ruling that upheld a trial court's refusal to compel arbitration after determining that two or four claims in the complaint were not subject to arbitration. Citing Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213 (1985), the Court ruled that lower courts must send arbitrable claims to arbitration even if there are related claims that are not subject to arbitration and piecemeal litigation may result.

33. ENFORCEMENT OF GUARANTY - - ACCORD AND SATISFACTION

Smith v. Community National Bank, 344 SW.3d 561 (Tex. Ct. App. 2011) - - The guarantor guaranteed a sizable loan from the bank to the debtor. After the debtor filed for Chapter 11 relief, the bank sought stay relief to foreclose its security interest in property of the debtor and also sued the guarantor in state court. The bankruptcy trustee entered into a stipulation to assign to the bank all of the trustee's and the debtor's rights in the collateral as well as a related insurance claim arising from a destruction of part of the collateral. The bankruptcy court approved the stipulation, and title and possession of the collateral was transferred to the bank. Thereafter, the state court granted summary judgment to the bank for the unpaid balance of the loan and the guarantor appealed. On appeal, the guarantor argued that the assignment of the collateral to the bank had the effect of a common law "accord and satisfaction" that discharged the debt and therefore discharged the guarantor's obligation. Alternatively, the guarantor argued that the bank's acceptance of the collateral was a "strict foreclosure" that had the same affect as an accord and satisfaction. The appeals court first found that the transfer of the collateral to the bank did not result in an accord and satisfaction because there was no indication in the stipulation or the agreed order that the parties intended for the assignment to satisfy the debt, either in full or in part. The fact that possession and title to the collateral were transferred to the bank was not sufficient to demonstrate a contractual intent to resolve all claims. Furthermore, the court pointed to strong waiver language in the guaranty agreement, which, among other things, stated that any full or partial release of the debtor would not relieve the guarantor and provided for the guarantor to waive all suretyship defenses other than discharge by payment. Such a waiver would include the affirmative defense of accord and satisfaction, the appeals court ruled. As for the strict foreclosure argument, the appeals court also rejected that position of the guarantor. For strict foreclosure, UCC § 9-620 requires the debtor's consent, in the case of a partial satisfaction of the debt, or the debtor's failure to file an objection to strict foreclosure within 20 days after the written proposal, in the case of a full satisfaction. Here, the requirements for strict foreclosure under UCC § 9-620 were not met. There was no consent to a strict foreclosure by either party or any evidence of intent that the assignment of the collateral would satisfy the underlying obligation.