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## Bankruptcy


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# BANKRUPTCY

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## I. INTRODUCTION

This Survey covers a number of notable bankruptcy opinions in the U.S. Court of Appeals for the Fifth Circuit and three decisions handed down by the U.S. Supreme Court. These courts addressed some challenging issues, including (1) whether good faith bars a finding of civil contempt; (2) whether the rejection of a trademark license is the functional equivalent of rescission; and (3) whether a creditor's injury is direct or derivative. This Survey also addresses three pieces of bankruptcy legislation that were enacted in 2019, all of which seek to expand the Bankruptcy Code's protections to certain debtors. The authors have selected these topics based on their importance to future bankruptcy practice, and we hope that the discussion below may continue to be useful to consumer and business bankruptcy practitioners.

## II. DISCHARGE

## A. FAMILIAR TERRAIN: THE SUPREME COURT DIGS THROUGH THE “OLD SOIL” AND FINDS “NO FAIR GROUND OF DOUBT”

In *Taggart v. Lorenzen*,<sup>1</sup> the U.S. Supreme Court addressed the legal standard for holding a creditor in civil contempt of court when such creditor attempts to collect a debt in violation of a bankruptcy discharge order. Specifically, does a creditor’s good-faith belief that the discharge injunction does not apply to its debt collection efforts preclude a finding of civil contempt?<sup>2</sup> In answering in the negative, the Supreme Court declined to adopt the lower bankruptcy court’s “strict liability” standard, and the U.S. District Court of Appeals for the Ninth Circuit’s “purely subjective standard.”<sup>3</sup> Instead, the Court held that “a court may hold a creditor in civil contempt for violating a discharge order if there is *no fair ground of doubt* as to whether the order barred the creditor’s conduct.”<sup>4</sup> The Court further clarified, “civil contempt may be appropriate if there is no objectively reasonable basis for concluding that the creditor’s conduct might be lawful.”<sup>5</sup>

The dispute in *Taggart* involved a real estate developer and petitioner, Bradley Taggart (Taggart), who formerly owned an interest in an Oregon company called Sherwood Park Business Center, LLC (Sherwood).<sup>6</sup> Sherwood had two other owners, who brought a lawsuit in Oregon state court against Taggart.<sup>7</sup> Before the state court action commenced, however, Taggart filed for relief under Chapter 7 of the Bankruptcy Code and received a discharge.<sup>8</sup> The discharge order provided, as with many discharge orders in bankruptcy, that the debtor “shall be granted a discharge under § 727.”<sup>9</sup>

Following entry of the discharge order, the Oregon state court entered a judgment against Taggart.<sup>10</sup> Sherwood next filed a petition in state court seeking attorney’s fees that were incurred after Taggart filed his bankruptcy petition.<sup>11</sup> The parties agreed that under Ninth Circuit precedent, a discharge order would typically bar the recovery of post-petition attorney’s fees from prebankruptcy litigation unless the discharged debtor “returned to the fray” post-petition.<sup>12</sup> The Oregon state court found that here, Taggart had “returned to the fray,” and the state court awarded

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1. 139 S. Ct. 1795, 1799 (2019).

2. *See id.*

3. *Id.*

4. *Id.* (emphasis in original).

5. *Id.*

6. *Id.*

7. *Id.*

8. *Id.* at 1799–80.

9. *Id.* at 1800.

10. *Id.*

11. *Id.*

12. *Id.* (citing *Boeing N. Am., Inc. v. Ybarra (In re Ybarra)*, 424 F.3d 1018, 1020 (9th Cir. 2005)).

Sherwood approximately \$45,000.00 in attorney's fees.<sup>13</sup>

Taggart next reopened his bankruptcy case before the U.S. Bankruptcy Court for the District of Oregon and moved to hold Sherwood and its two other owners (collectively, Creditors) in contempt of court for violating the discharge injunction under 11 U.S.C. § 524(a).<sup>14</sup> The bankruptcy court disagreed, finding that Taggart had indeed “returned to the fray.”<sup>15</sup> Taggart appealed the bankruptcy court's decision to the U.S. District Court for the District of Oregon.<sup>16</sup> The district court reversed, finding that Taggart had not “returned to the fray” and remanded the matter to the bankruptcy court.<sup>17</sup> On remand, the bankruptcy court determined that the Creditors violated the discharge injunction and awarded sanctions against the Creditors.<sup>18</sup> In doing so, the bankruptcy court applied a standard it likened to “strict liability.”<sup>19</sup>

The Creditors then appealed the bankruptcy court's contempt ruling directly to the Bankruptcy Appellate Panel (BAP), which vacated the sanctions.<sup>20</sup> Taggart next appealed to the Ninth Circuit Court of Appeals, which affirmed.<sup>21</sup> The Ninth Circuit reasoned the Creditors did not “knowingly” violate the discharge injunction because they held a “good faith” belief that the discharge injunction did not apply to their attorney's fees claim.<sup>22</sup> The Supreme Court granted certiorari.<sup>23</sup>

Section 524(a)(2) of the Bankruptcy Code provides, “[a] discharge . . . operates as an injunction against the commencement or continuation of an action . . . or an act, to collect, recover or offset any such debt as a personal liability of the debtor. . . .”<sup>24</sup> Section 105(a) of the Code, in turn, brings the “old soil” of how courts enforce injunctions—namely, civil contempt.<sup>25</sup> The Supreme Court recognized that in cases outside the bankruptcy context, “we have said that civil contempt ‘should not be resorted to where there is [a] fair ground of doubt as to the wrongfulness of the defendant's conduct.’”<sup>26</sup> Expounding upon this reasoning, the Court noted that this is generally an objective standard.<sup>27</sup> In declining to adopt the Ninth Circuit's view, the Supreme Court explained, as it had explained in prior cases, that “a party's subjective belief that she was complying with an order ordinarily will not insulate her from civil contempt if

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13. *Id.*

14. *Id.* at 1800–01.

15. *Id.* at 1800.

16. *Id.*

17. *Id.*

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

22. *Id.* at 1800–01.

23. *Id.* at 1801.

24. 11 U.S.C. § 524(a)(2) (2012).

25. *Taggart*, 139 S. Ct. at 1801 (citing 11 U.S.C. § 105(a) (2012)).

26. *Id.* (citing *Cal. Artificial Stone Paving Co. v. Molitor*, 113 U.S. 609, 618 (1885)).

27. *Id.* at 1802.

that belief was objectively unreasonable.”<sup>28</sup> Despite this, the Court noted that subjective intent is not irrelevant.<sup>29</sup> Whereas contempt sanctions are warranted in instances of bad faith, a party’s good faith belief—though not a bar to civil contempt—could help determine appropriate sanctions.<sup>30</sup>

The Supreme Court also declined to adopt Taggart’s “strict liability” proposal.<sup>31</sup> This standard, the Court analyzed, “may lead risk-averse creditors to seek an advance determination in bankruptcy court even where there is only slight doubt as to whether a debt has been discharged.”<sup>32</sup> This would, in turn, “risk additional federal litigation, additional costs, and additional delays.”<sup>33</sup> But Taggart argued that bankruptcy courts often use a standard similar to strict liability when determining violations of the automatic stay.<sup>34</sup> The Supreme Court rejected this argument, noting that the language of the automatic stay provision, unlike the discharge injunction, includes the word “willful.”<sup>35</sup> Moreover, the purposes of the automatic stay and the discharge injunction differ.<sup>36</sup> Whereas the automatic stay functions to prevent harmful disruptions to the administration of a bankruptcy case in the short term, a discharge order is entered at the conclusion of a bankruptcy case and seeks to bind creditors for a much longer period of time.<sup>37</sup> The Court determined that the proper standard is an objective one—a court may hold a creditor in civil contempt for violating a discharge order where there is no “fair ground of doubt” as to whether the creditor’s conduct may be lawful under the discharge order.<sup>38</sup>

In conclusion, *Taggart* was the case to watch. Prior to this decision, a majority of federal courts, including the U.S. Courts of Appeals for the First, Fourth, and Eleventh Circuits, interpreted the discharge injunction to overcome a good faith belief defense.<sup>39</sup> The Ninth Circuit’s opinion finding that a “good faith” intent precludes civil contempt, was clearly the minority view.<sup>40</sup> While the Supreme Court’s opinion was somewhat unsurprising, it reaffirms that the standard for civil contempt is an objective one.<sup>41</sup> Nevertheless, the case provides some comfort for creditors who may find themselves in violation of a discharge order despite having a

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28. *Id.* (citing *McComb v. Jacksonville Paper Co.*, 336 U.S. 187, 191 (1949)).

29. *Id.*

30. *Id.*

31. *Id.* at 1803.

32. *Id.*

33. *Id.*

34. *Id.*

35. *Id.* at 1804 (citing 11 U.S.C. § 362(k)(1) (2012)).

36. *Id.*

37. *Id.*

38. *Id.*

39. *See, e.g.*, *Internal Revenue Serv. v. Murphy*, 892 F.3d 29 (1st Cir. 2018); *Bradley v. Fina (In re Fina)*, 550 F. App’x 150 (4th Cir. 2014) (per curiam); *Hardy v. United States (In re Hardy)*, 97 F.3d 1384 (11th Cir. 1996).

40. *Taggart*, 139 S. Ct. at 1804.

41. *Id.*

reasonable, good-faith belief for doing so.<sup>42</sup> Overall, the “fair ground of doubt” standard should strike the “careful balance between the interests of creditors and debtors.”<sup>43</sup> Courts going forward can rely on the “old soil” rather than break new ground.

B. FIFTH CIRCUIT DECLINES TO RECONSIDER *GERHARDT*’S “UNDUE HARDSHIP” STANDARD IN *THOMAS V. DEPARTMENT OF EDUCATION* (*IN RE THOMAS*)

In *Thomas v. Department of Education (In re Thomas)*,<sup>44</sup> the U.S. Court of Appeals for the Fifth Circuit held that the bankruptcy court properly denied a debtor a discharge of her student loan debt under 11 U.S.C. § 523(a)(8).<sup>45</sup> Citing its own precedent, the Fifth Circuit declined to overturn the three-prong test for evaluating “undue hardship” it had adopted in *In re Gerhardt*.<sup>46</sup> While both the lower bankruptcy court and district court indicated sympathy for the debtor and the “demanding” nature of the *Gerhardt* standard, the Fifth Circuit remained steadfast in its previous interpretation of the law.<sup>47</sup> “[T]he role of this court,” the Fifth Circuit concluded, “is to interpret the laws passed by Congress, not to set bankruptcy policy.”<sup>48</sup>

Section 523(a)(8) of the Bankruptcy Code enables a debtor to discharge her student loan debt if the debtor can show that the debt, if excepted from discharge, would “impose an ‘undue hardship’ on the debtor and the debtor’s dependents.”<sup>49</sup> While the Bankruptcy Code does not define what amounts to an “undue hardship,” courts in this circuit rely on the three-prong *Brunner* test as construed by the Fifth Circuit in *In re Gerhardt*.<sup>50</sup> That test requires that a debtor establish:

- (1) that the debtor cannot maintain, based on current income and expenses, a “minimal” standard of living for [herself] and [her] dependents if forced to repay the loans;
- (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans;
- and (3) that the debtor has made good faith efforts to repay the loans.<sup>51</sup>

In the Fifth Circuit, the second prong of *Brunner* is especially difficult to

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42. *Id.* at 1802. “On the flip side of the coin, a party’s good faith, even where it does not bar civil contempt, may help to determine an appropriate sanction.” *Id.* (citing *Young v. United States ex rel. Vuitton et Fils S.A.*, 481 U.S. 787, 801 (1987)).

43. *Id.* at 1804 (citing *Clark v. Rameker*, 573 U.S. 122, 129 (2014)).

44. 931 F.3d 449 (5th Cir. 2019).

45. *Id.* at 450.

46. *Id.* at 450–51 (citing *U.S. Dep’t of Educ. v. Gerhardt (In re Gerhardt)*, 348 F.3d 89 (5th Cir. 2003)).

47. *Id.*

48. *Id.* at 455.

49. *Id.* at 451 (citing 11 U.S.C. § 523(a)(8) (2012)).

50. *Id.* (first citing *In re Gerhardt*, 348 F.3d at 91; then citing *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987)).

51. *In re Gerhardt*, 348 F.3d at 91 (quoting *Brunner*, 831 F.2d at 396).

meet.<sup>52</sup> “[A] showing of dire financial” conditions is not enough; rather, a debtor must have a “total incapacity” to pay debts both current and in the future.<sup>53</sup>

In this case, Ms. Vera Frances Thomas (the Debtor) was a single woman over the age of sixty at the time her bankruptcy case was filed in 2017.<sup>54</sup> Prior to filing for Chapter 7 bankruptcy, the Debtor worked for eight years at a call center in Southeastern Virginia earning \$11.40 per hour, including benefits.<sup>55</sup> While employed, she enrolled in community college to improve her career prospects with higher education.<sup>56</sup> The Debtor financed a portion of her college education in 2012 with two loans of \$3,500.00 through the William D. Ford Federal Direct Loan Program with the Department of Education.<sup>57</sup> Her loans went into repayment status in December 2013.<sup>58</sup> The Debtor only made two payments on the loans in the spring of 2014: one in the amount of \$41.24 and another in the amount of \$41.61.<sup>59</sup>

Around this time, the Debtor was diagnosed with a debilitating illness called diabetic neuropathy, for which there is no cure.<sup>60</sup> The effects of that condition caused a loss of circulation in the Debtor’s lower extremities, muscle weakness, and numbness and pain in her legs and feet.<sup>61</sup> Because of this, the Debtor frequently took unpaid leave from work and accrued large amounts of medical expenses.<sup>62</sup> In 2016, the Debtor was terminated for cause at her then-current employment.<sup>63</sup> She retained other work, but each job required her to be on her feet and she was unable to maintain these positions.<sup>64</sup> Shortly thereafter, she filed for bankruptcy protection and later sought to discharge her small amount of student loan debt.<sup>65</sup>

The U.S. Bankruptcy Court for the Northern District of Texas found that the Debtor did not satisfy her burden of showing “undue hardship” under the controlling standard in the Fifth Circuit.<sup>66</sup> The U.S. District Court for the Northern District of Texas affirmed the bankruptcy court’s ruling.<sup>67</sup> On appeal to the Fifth Circuit, the Debtor argued that (1) the *Brunner/Gerhardt* test is inconsistent with the plain meaning of Section

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52. *See In re Thomas*, 931 F.3d at 451.

53. *Id.*

54. *Id.* at 450.

55. *Id.*

56. *Id.*

57. *Id.*

58. *Id.*

59. *See id.*

60. *See id.*

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.* at 451. One of the authors of this Survey was the trial judge in this bankruptcy case.

67. *Id.*



523(a)(8) and the court should instead adopt a “totality of the circumstances” test; and (2) alternatively, the Debtor has satisfied the second and third prongs of *Brunner*.<sup>68</sup>

The Fifth Circuit declined to overturn its precedent, noting that the *Brunner* test reflected the majority view for defining “undue hardship” among the circuit courts.<sup>69</sup> Commenting on the legislative history of Section 523(a)(8), the Fifth Circuit doubled down on its interpretation of the Code’s language.<sup>70</sup> “The plain meaning of the words chosen by Congress,” the Fifth Circuit noted, “is that student loans are not to be discharged unless requiring repayment would impose intolerable difficulties on the debtor.”<sup>71</sup> With respect to the Debtor’s policy-based arguments, the Fifth Circuit did not bite.<sup>72</sup> Instead, “the fact that student loans are now mountainous in quantity poses systemic issues far beyond the capacity or authority of courts, which can only interpret the written law.”<sup>73</sup>

The Fifth Circuit next addressed the question as to whether, in this case and due to external factors, the Debtor’s present inability to pay her student loans and maintain a minimal standard of living would persist throughout a significant portion of the loan repayment period.<sup>74</sup> The court answered this question in the negative, finding that by the Debtor’s own admission, she was capable of employment in sedentary work environments.<sup>75</sup> Because the Debtor did not meet the second prong of the *Brunner* test, the Fifth Circuit declined to opine on the third prong.<sup>76</sup>

In conclusion, the Fifth Circuit affirmed the bankruptcy court’s denial of the Debtor’s discharge in this case. The biggest takeaway, however, is that the “undue hardship” standard articulated by the Fifth Circuit in *In re Gerhardt* remains good law. Accordingly, debtors must wait for a decision from the U.S. Supreme Court if they hope to have better odds at discharging their student loan debts in the Fifth Circuit.

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68. *See id.* at 452.

69. *Id.* (first citing *Educ. Credit Mgmt. Corp. v. Frushour* (*In re Frushour*), 433 F.3d 393 (4th Cir. 2005); then citing *Oyler v. Educ. Credit Mgmt. Corp.* (*In re Oyler*), 397 F.3d 382 (6th Cir. 2005); then citing *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302 (10th Cir. 2004); then citing *Hemar Ins. Corp. of Am. v. Cox*, (*In re Cox*), 338 F.3d 1238 (11th Cir. 2003); then citing *United Student Aid Funds, Inc. v. Pena* (*In re Pena*), 155 F.3d 1108 (9th Cir. 1998); then citing *Pa. Higher Educ. Assistance Agency v. Farish* (*In re Faish*), 72 F.3d 298 (3d Cir. 1995); and then citing *In re Roberson*, 999 F.2d 1132 (7th Cir. 1993)).

70. *Id.* at 453–54.

71. *Id.* at 454.

72. *See id.* at 455.

73. *Id.*

74. *Id.* at 452.

75. *Id.*

76. *Id.* (“Nor need we opine, despite the government’s urging, on the third *Brunner* prong, which evaluates Ms. Thomas’s good faith efforts to repay the loan.”).

### III. CONTRACT REJECTION

#### A. IN *MISSION PRODUCT HOLDINGS, INC. v. TEMPNOLOGY, LLC*, THE SUPREME COURT RESOLVES CIRCUIT SPLIT ON REJECTION OF TRADEMARK LICENSES IN BANKRUPTCY

##### 1. Background

On September 1, 2015, Tempnology, LLC (the Debtor) filed for protection under Chapter 11 of the Bankruptcy Code.<sup>77</sup> The following day, the Debtor filed a motion to reject an executory contract—specifically, a trademark licensing contract—it had entered into with Mission Products Holdings, Inc. (Mission), the licensee.<sup>78</sup> After the U.S. Bankruptcy Court for the District of New Hampshire approved the Debtor’s rejection of the contract, the Debtor requested that the bankruptcy court terminate Mission’s rights under the contract, and the bankruptcy court granted the Debtor’s request.<sup>79</sup> The BAP for the First Circuit reversed.<sup>80</sup> But the BAP’s decision was subsequently overturned by the First Circuit Court of Appeals.<sup>81</sup>

These rulings centered around whether a trademark falls within the meaning of intellectual property under the Bankruptcy Code.<sup>82</sup> If a trademark is intellectual property, then it would be afforded rights under Section 365(n).<sup>83</sup> If, however, a trademark is not intellectual property, what rights, if any, would the licensee retain when the licensing agreement was rejected during a bankruptcy proceeding?<sup>84</sup>

The extra protection afforded to licensees of intellectual property likely stems from *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*,<sup>85</sup> where the U.S. Court of Appeals for the Fourth Circuit held that a licensee “could not seek to retain its contract rights in the technology by specific performance even if that remedy would ordinarily be available upon breach of this type of contract.”<sup>86</sup> Following this decision, Congress amended the Bankruptcy Code to add Section 365(n),<sup>87</sup> which allows the licensee of intellectual property to treat the contract as terminated or,

to retain its rights (including a right to enforce any exclusivity provision of such contract . . . ) under such contract and under any agreement supplementary to such contract, to such intellectual property . . . , as such rights existed immediately before the case commenced, for (i) the duration of such contract; and (ii) any period for which

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77. *In re* Tempnology, LLC, 541 B.R. 1, 2, 4 (Bankr. D.N.H. 2015).

78. *Id.*

79. *See* *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1658–59 (2019).

80. *Id.* at 1659.

81. *Id.*

82. *See id.* at 1659–60.

83. *See id.* at 1659.

84. *See id.*

85. 756 F.2d 1043, 1048 (4th Cir. 1985).

86. *Id.*

87. *Mission Prod. Holdings*, 139 S. Ct. at 1664.

such contract may be extended by the licensee . . . .<sup>88</sup>

However, trademarks are not included within the meaning of “intellectual property” as defined by the Bankruptcy Code.<sup>89</sup> Section 101(35A) defines intellectual property as a (1) trade secret; (2) invention, process, design, or plant protected under Title 35; (3) patent application; (4) plant variety; (5) work of authorship protected under Title 17; or (6) mask work protected under Chapter 9 of Title 17.<sup>90</sup> Because Congress enacted Sections 365(n) and 101(35A) in response to the Fourth Circuit’s *Lubrizol* decision,<sup>91</sup> it is not surprising that the definition focuses on patent rights and trade secrets, and specifically protects those rights.<sup>92</sup>

## 2. *The Case Before the Supreme Court*

In *Mission Product Holdings, Inc. v. Tempnology, LLC*,<sup>93</sup> the question before the Court was “whether the debtor-licensor’s rejection of [a trademark licensing] contract deprives the licensee of its rights to use the trademark.”<sup>94</sup> The Court granted certiorari to resolve a circuit split between the U.S. Courts of Appeals for the Seventh and First Circuits.<sup>95</sup> The Seventh Circuit held that the rejection of a license agreement would allow the license holder to retain the right to use the license as granted under the original contract.<sup>96</sup> By contrast, the First Circuit held that the rejection of the contract in a bankruptcy proceeding would rescind the contract and thereby void all rights to the use of the trademark granted under the licensing agreement that was rejected.<sup>97</sup> In an 8–1 decision, the Supreme Court sided with the Seventh Circuit’s view, holding that a debtor’s rejection of a trademark license under Section 365 amounts to a breach of the license agreement and the licensee retains the rights to the licensed marks from the remainder of the license term.<sup>98</sup>

The Supreme Court first analyzed 11 U.S.C. § 365(a), which provides that a “trustee [or debtor], subject to the court’s approval, may assume or reject any executory contract.”<sup>99</sup> A contract is executory where “performance remains due to some extent on both sides.”<sup>100</sup> The Court next turned to 11 U.S.C. § 365(g), which provides that the rejection of an executory contract amounts to a breach of such contract.<sup>101</sup> The counterparty to rejection would accordingly receive a pre-petition unsecured damages

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88. 11 U.S.C. § 365(n)(B)(i)–(ii) (2012).

89. *See* 11 U.S.C. § 101(35A) (2012).

90. *Id.*

91. *Mission Prod. Holdings*, 139 S. Ct. at 1664–65.

92. *Lubrizol Enters. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043, 1045 (4th Cir. 1085) (the license agreement at issue related to a metal coating finish process).

93. 139 S. Ct. 1652, 1657–58 (2019).

94. *Id.*

95. *Id.* at 1660.

96. *Id.* at 1659.

97. *Id.*

98. *Id.* at 1657–58.

99. *Id.* at 1658.

100. *Id.*

101. *Id.*

claim.<sup>102</sup>

Further, in Sections 365(h), (i), and (n), the Bankruptcy Code identifies certain types of executory contracts and grants those executory contracts special rights.<sup>103</sup> Section 365(n) gives the license holder of certain types of intellectual property the right to continue to use the license.<sup>104</sup> However, this provision would not have applied to the contract at issue because the license pertained to a trademark, and trademarks are not intellectual property as defined in the Bankruptcy Code.<sup>105</sup> The Court rejected the Debtor's argument that because the Bankruptcy Code does not lay out specific rights pertaining to this type of contract, as it does for real property, timeshares, and certain intellectual property, then no right exists.<sup>106</sup> The Court noted that Sections 365(h), (i), and (n) were added "to reinforce or clarify the general rule that contractual rights survive rejection."<sup>107</sup> These sections were added to address three separate judicial decisions.<sup>108</sup>

The Supreme Court went on to explain that only the Debtor's obligation to perform is relieved in bankruptcy.<sup>109</sup> The Debtor would have no further obligations under the contract, unless otherwise provided for outside of bankruptcy.<sup>110</sup> In this case, that would mean that the Debtor would not be required to maintain or defend the trademark, or perform any other obligation under the agreement.<sup>111</sup> However, "the [D]ebtor cannot rescind the license already conveyed."<sup>112</sup> As a result, any rights conveyed to a license holder outside of bankruptcy will remain with the license holder after the licensor files for bankruptcy.<sup>113</sup> To this point, the Court emphasized the principle that "[t]he estate cannot possess anything more than the debtor itself did outside bankruptcy."<sup>114</sup> A ruling in the Debtor's favor would have transferred the rights held by Mission to the bankruptcy estate.<sup>115</sup> The estate would have then been able to negotiate a better licensing agreement without having to consider its original agreement with Mission.<sup>116</sup>

An additional reason the Court rejected this "rejection-as-rescission" approach was that it would amount to the functional equivalent of avoidance.<sup>117</sup> A trustee or debtor-in-possession may avoid certain types of

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102. *Id.*

103. *Id.* at 1663 (citing 11 U.S.C. §§ 365(h), (i), (n) (2012)).

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.* at 1664.

108. *Id.*

109. *Id.* at 1665.

110. *Id.*

111. *Id.*

112. *Id.* at 1662.

113. *See id.*

114. *Id.* at 1663.

115. *See id.*

116. *See id.*

117. *Id.*

transfers under Sections 544, 545, 546, 547, 548, 549, 550, 551, 552, and 553.<sup>118</sup> Typically, the avoided transfers involve some type of preference or fraud.<sup>119</sup> If an avoidance action is brought, however, the transferee would have the opportunity to defend the transfer, such as, by showing the transfer was for reasonably equivalent value if the trustee alleged fraud.<sup>120</sup> Section 365 has no similar provision related to the rejection of executory contracts.<sup>121</sup> The Court extensively discussed that rejection-as-rescission cannot be allowed as that would effectively be an avoidance without the avoidance restrictions provided in Sections 544 through 553.<sup>122</sup> With this ruling, “[r]ejection is breach, and has only its consequences.”<sup>123</sup>

In conclusion, the Supreme Court’s decision in *Mission Product Holdings, Inc. v. Tempnology, LLC* resolved a longstanding circuit split as to what rights a licensee retains following a debtor’s rejection of a trademark license in bankruptcy.<sup>124</sup> The Court ruled broadly and held that agreements rejected by a debtor in bankruptcy does not amount to rescission.<sup>125</sup> Instead, a non-debtor party will retain whatever rights it would have under applicable non-bankruptcy law following a breach of that agreement.<sup>126</sup> While this decision may appear to limit a debtor’s tools and bargaining power in the context of rejection, that may not always be the case. As Justice Sotomayor observed in her concurrence, applicable non-bankruptcy law may still terminate a license holder’s contractual rights.<sup>127</sup> While parties may continue to litigate about what rights they have, at a minimum, the split between the Seventh and First Circuit Courts of Appeal has been resolved. Hopefully, this will result in a more consistent and predictable application of the Bankruptcy Code.

B. FIFTH CIRCUIT CLARIFIES POST-REJECTION ADMINISTRATIVE  
PRIORITY STATUS IN *NABORS OFFSHORE CORP. V.*  
*WHISTLER ENERGY II, L.L.C.*

In *Nabors Offshore Corporation v. Whistler Energy II, L.L.C.* (*In re Whistler Energy II, L.L.C.*),<sup>128</sup> the U.S. Court of Appeals for the Fifth Circuit clarified when a claimant is entitled to post-rejection administrative priority status under Section 503(b)(1)(A) of the Bankruptcy Code.<sup>129</sup> The question: when can post-rejection damages be allowed as

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118. *Id.*

119. *Id.*

120. *Id.*; see also 11 U.S.C. § 548(c) (2012).

121. *Mission Prod. Holdings*, 139 S. Ct. at 1657–58.

122. *Id.* at 1663.

123. *Id.*

124. See *id.* at 1660, 1663–66.

125. See *id.* at 1666.

126. See *id.*

127. *Id.* at 1666 (J. Sotomayor, concurring).

128. 931 F.3d 432 (5th Cir. 2019).

129. *Id.* at 440; see 11 U.S.C. § 503(b)(1)(A) (2012). This provision grants priority status to certain necessary expenses over most unsecured claims. *In re Whistler Energy II, L.L.C.*, 931 F.3d at 440. In bankruptcy, the court “presume[s] that all ‘creditors are equally inno-

administrative expenses?<sup>130</sup> In affirming in part and reversing in part the decision of the U.S. District Court for the Eastern District of Louisiana, the Fifth Circuit held that a claimant can prove an expense is “actual and necessary” within the meaning of 11 U.S.C. § 503(b)(1)(A), “through evidence of either a direct request from the debtor-in-possession or other inducement via the knowing and voluntary post-petition acceptance of desired goods or services.”<sup>131</sup> Accordingly, “when a debtor-in-possession induces availability and the bankruptcy estate derives a benefit from it, the ordinary cost of ensuring such availability qualifies as an administrative expense.”<sup>132</sup> The underlying facts involve the Chapter 11 bankruptcy proceeding of Whistler Energy II, L.L.C. (Whistler), which owned an oil and gas production platform in the Outer Continental Shelf in the Gulf of Mexico.<sup>133</sup> In February 2014, Whistler entered into a drilling contract with Nabors Offshore Corporation (Nabors) under which Nabors would drill two new wells for Whistler and provide it with related services and equipment.<sup>134</sup> In March 2016, a Nabors employee accidentally died on Whistler’s platform.<sup>135</sup> As a result, the United States Bureau of Safety and Environmental Enforcement (BSEE) ordered Nabors and Whistler to stop drilling activity.<sup>136</sup> At the same time, several of Whistler’s creditors filed an involuntary Chapter 11 bankruptcy petition.<sup>137</sup> Whistler became the debtor-in-possession, and Nabors moved to compel assumption or rejection of the contract with Whistler.<sup>138</sup> Whistler elected to reject the contract.<sup>139</sup> Nabors remained on the platform for several months pending the creation and BSEE approval of a demobilization plan.<sup>140</sup>

Two time periods were at issue in this case: (1) the pre-demobilization period (that is, the four months it took for regulators to approve a demobilization plan immediately following Whistler’s rejection of the Whistler/Nabors contract); and (2) the demobilization period (the two months following that it took for Nabors to remove the drilling rig from the platform).<sup>141</sup> Importantly, both time periods occurred after Whistler rejected the Whistler/Nabors contract.<sup>142</sup> Nabors requested that the U.S. Bankruptcy Court for the Eastern District of Louisiana classify Nabors’s post-rejection expenses from both time periods as administrative expenses

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cent victims.’” *Id.* at 441 (quoting *Total Minatome Corp. v. Jack/Wade Drilling, Inc.* (*In re Jack/Wade Drilling, Inc.*), 258 F.3d 385, 387 (5th Cir. 2001)). Therefore, a bankruptcy court must decide whether the creditor “deserves to get paid at the expense of the debtor’s existing unsecured creditors.” *Id.*

130. *See In re Whistler Energy II, L.L.C.*, 931 F.3d at 438.

131. *Id.* at 443.

132. *Id.* at 444.

133. *Id.* at 438.

134. *Id.* at 438–39.

135. *Id.* at 439.

136. *Id.*

137. *Id.*

138. *Id.*

139. *Id.*

140. *Id.* at 439–40.

141. *See id.* at 438.

142. *Id.*

under 11 U.S.C. § 503(b)(1)(A).<sup>143</sup> Specifically, Nabors requested administrative priority for \$4.32 million in pre-demobilization expenses and \$2.65 million in demobilization costs.<sup>144</sup> Whistler, Whistler's primary secured creditor (Apollo), and the Official Committee of Unsecured Creditors, objected to Nabors's request.<sup>145</sup>

The bankruptcy court held that Nabors was only entitled to administrative priority for the expenses actually used or specifically requested by Whistler during the pre-demobilization time period as the other pre-demobilization services Nabors provided were "'akin to Nabors being available to provide services, as opposed to Nabors actually providing services'" to Whistler.<sup>146</sup> Further, the bankruptcy court denied administrative priority for all of Nabors's demobilization expenses, finding that Nabors was only entitled to a general unsecured damages claim because demobilization was only the consequence of the contract rejection and therefore did not benefit the bankruptcy estate.<sup>147</sup> The U.S. District Court for the Eastern District of Louisiana affirmed, and Nabors appealed.<sup>148</sup>

On appeal to the U.S. Court of Appeals for the Fifth Circuit, the panel found no error in the lower court's denial of Nabors's claim for demobilization expenses.<sup>149</sup> However, the Fifth Circuit reversed and remanded the case to the bankruptcy court for further factfinding on the pre-demobilization expenses in light of the clarified the legal standard set forth in the Fifth Circuit's opinion.<sup>150</sup>

Under Section 503(b)(1)(A) of the Bankruptcy Code, administrative expenses are "the actual, necessary costs and expenses of preserving the estate including . . . wages, salaries, and commissions for services rendered after the commencement of the case."<sup>151</sup> To qualify as an "actual and necessary cost" within the meaning of Section 503(b)(1)(A), the creditor's claim must satisfy two requirements: (1) the claim must have occurred post-petition and result from the debtor-in-possession's actions; and (2) the expenses claimed must have benefitted the estate.<sup>152</sup> The

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143. *Id.* at 440.

144. *Id.*

145. *Id.*

146. *Id.* at 440–41 (quoting *In re Whistler Energy II, LLC*, 571 B.R. 199 (Bankr. E.D. La. 2017) (emphasis in original)).

147. *Id.* at 441.

148. *Id.*

149. *Id.* at 448. In reviewing the applicable BSEE regulations in this case, the Fifth Circuit concluded that demobilization was not necessary to satisfy the bankruptcy estate's legal obligations. *Id.* Granted, "[a] debtor-in-possession must comply with applicable health and safety laws, and services rendered to full these legal requirements are a necessary expense that benefits the bankruptcy estate." *Id.* at 447 (citing *Texas v. Lowe (In re H.L.S. Energy Co., Inc.)*, 151 F.3d 434, 437 (5th Cir. 1998)). But here, "[t]he mere possibility that Whistler could have future regulatory obligations is insufficient to give rise to administrative priority." *Id.* at 448.

150. *Id.* at 446.

151. 11 U.S.C. § 503(b)(1)(A) (2012).

152. *In re Whistler Energy II, L.L.C.*, 931 F.3d at 441 (quoting *Total Minatome Corp. v. Jack/Wade Drilling, Inc. (In re Jack/Wade Drilling, Inc.)*, 258 F.3d 385, 387 (5th Cir. 2001)).

Fifth Circuit elaborated on this standard by explaining that administrative priority claims arise only from transactions with the debtor-in-possession, not from transactions with the pre-petition debtor.<sup>153</sup> Further, “in the context of commercial transactions for goods and services, a creditor must show some inducement by the debtor-in-possession.”<sup>154</sup>

First, the Fifth Circuit considered whether Whistler induced Nabors to provide post-petition services after Whistler rejected the Nabors/Whistler contract.<sup>155</sup> Under the Bankruptcy Code, rejection of pre-petition contracts gives rise to a breach of contract claim rather than an administrative priority claim; however, the creditor can prove inducement by the debtor-in-possession through evidence of a written post-petition agreement.<sup>156</sup> Here, there was no new, written post-petition agreement between Nabors and Whistler.<sup>157</sup> But the Fifth Circuit, joining its sister circuits, held that an explicit written post-petition agreement is not necessary.<sup>158</sup> Instead, “a creditor can establish that its expenses are attributable to the actions of the bankruptcy estate through evidence of either a direct request from the debtor-in-possession or other inducement via the knowing and voluntary post-petition acceptance of desired goods or services.”<sup>159</sup>

Second, the Fifth Circuit analyzed whether Nabors’s administrative expenses benefitted the estate.<sup>160</sup> “This requirement,” the court noted, “is merely a way of testing whether a particular expense was truly “necessary” to the estate . . . .”<sup>161</sup> The Fifth Circuit focused on the fact that benefits to the estate may take different forms and are not narrowly limited to money.<sup>162</sup> Some benefits to the estate such as the ability to continue business as usual are difficult to calculate.<sup>163</sup> Thus, the actual and necessary costs are not limited to costs strictly necessary for rehabilitation, rather it includes the costs that are typically necessary to operate the business.<sup>164</sup> The Fifth Circuit rejected the bankruptcy court’s distinction between services Nabors actually provided and services Nabors was able to provide, finding that conducting business as usual often requires cer-

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153. *Id.* at 442 (citing Preferred Carrier Servs., Inc. v. Phones for All, Inc. (*In re Phones for All, Inc.*), 288 F.3d 730, 732 (5th Cir. 2002)). The court explained the purpose behind administrative priority as one that serves “to encourage third parties to provide necessary goods and services to the debtor-in-possession so that it can continue to conduct its business, thus generating funds from which prepetition creditors can be paid.” *Id.* (quoting Toma Steel Supply, Inc. v. TransAmerican Nat. Gas Corp. (*In re TransAmerican Nat. Gas Corp.*), 978 F.2d 1409, 1420 (5th Cir. 1992)).

154. *Id.* (citing *In re Jartran, Inc.*, 732 F.2d 584, 587 (7th Cir. 1984)).

155. *Id.* at 441.

156. *Id.* at 442.

157. *Id.*

158. *Id.* at 443.

159. *Id.*

160. *Id.*

161. *Id.* (quoting H.L.S. Energy Co., Inc. v. Lowe (*In re H.L.S. Energy Co., Inc.*), 151 F.3d 434, 437 (5th Cir. 1998)).

162. *See id.*

163. *Id.*

164. *Id.* (quoting Reading Co. v. Brown, 391 U.S. 471, 483 (1968)).



tain services to be available, even if they are not ultimately used.<sup>165</sup> Thus, the Fifth Circuit clarified that when the bankruptcy estate derives a benefit from inducing the creditor's availability, the cost of ensuring availability meets the requirements of an administrative expense.<sup>166</sup>

The Fifth Circuit next applied this two-part standard to the pre-demobilization period at issue.<sup>167</sup> The Fifth Circuit first addressed whether Nabors's ongoing presence on the Whistler platform entitled it to administrative priority:

Whereas Nabors would be entitled to administrative priority for the actual and necessary costs of its presence on the platform for the period of time required to satisfy Whistler's logistical and regulatory requirements, Nabors would not be entitled to administrative expenses for the cost of its presence on the platform for any time attributable to its own unnecessary delay, as such delay neither results from actions by the debtor-in-possession nor benefits the estate.<sup>168</sup>

Because the bankruptcy court did not make findings in this regard, the Fifth Circuit remanded the matter for the bankruptcy court to determine: (1) whether Whistler induced Nabors to stay on the platform; (2) the length of time Nabors stayed on the platform due to Whistler's post-petition needs; and (3) the actual and necessary costs of staying on this platform during this time period.<sup>169</sup>

The Fifth Circuit next addressed whether Nabors was entitled to administrative expenses for the cost of providing services to Whistler during the pre-demobilization period.<sup>170</sup> The Fifth Circuit remanded this matter to the bankruptcy court to clarify its own findings as to Nabors's services.<sup>171</sup> The Fifth Circuit again reiterated its holding that Nabors be entitled to administrative priority not only for services explicitly requested by the debtor-in-possession, but also for services "knowingly and voluntarily accepted after the filing of a bankruptcy petition."<sup>172</sup>

In conclusion, this case provides a significant clarification as to when a claimant is entitled to post-rejection administrative expenses under Section 503(b)(1)(A). Notably, the Fifth Circuit held that an explicit written post-petition agreement between a debtor-in-possession and claimant, although "helpful," is not required.<sup>173</sup> Rather, a claimant may show inducement "via the knowing and voluntary post-petition acceptance of desired goods or services."<sup>174</sup> Administrative priority status incentivizes third

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165. *Id.* at 444.

166. *Id.*

167. *See id.*

168. *Id.* at 445-46.

169. *Id.* at 446.

170. *Id.*

171. *Id.*

172. *Id.* at 446-47. The Fifth Circuit further clarified that such costs "should include the full and ordinary costs of providing a service, including overhead costs and other indirect expenses." *Id.* at 447.

173. *Id.* at 442-43.

174. *Id.* at 443.

parties to provide necessary services for the debtor-in-possession to keep operating its business, which in turn creates funds to pay pre-petition creditors.<sup>175</sup> Overall, this case will provide guidance to both creditors and debtors in determining what debtor-in-possession actions may constitute inducement and what actions will benefit the estate giving rise to an administrative priority claim under Section 503(b)(1)(A).

#### IV. FDCPA

##### A. THE SUPREME COURT HOLDS THAT NONJUDICIAL FORECLOSURES FALL OUTSIDE THE FDCPA IN *OBDUSKEY V. MCCARTHY & HOLTHUS LLP*

*Obduskey v. McCarthy & Holthus LLP*<sup>176</sup> was another notable U.S. Supreme Court case centered on an issue of statutory interpretation. The question presented to the Court was whether a business engaged in non-judicial foreclosure proceedings falls under the broad definition of a “debt collector” under the Fair Debt Collection Practices Act (the FDCPA).<sup>177</sup> If so, numerous provisions of the FDCPA would apply.<sup>178</sup> If not, only the limited provision of Section 1692f(6) of the FDCPA, which prohibits unfair or unconscionable debt collection practices, would regulate such conduct.<sup>179</sup> In resolving a circuit split between the U.S. Courts of Appeals for the Fourth, Fifth, and Sixth Circuits (which held the FDCPA applies to nonjudicial foreclosure proceedings) and the U.S. Courts of Appeals for the Ninth and Tenth Circuits (which did not), the Supreme Court followed the minority.<sup>180</sup> Specifically, the Court held that a business whose “principal purpose . . . is the enforcement of security interests” falls outside the scope of the primary “debt collector” definition of the FDCPA.<sup>181</sup>

The underlying facts involve a nonjudicial foreclosure proceeding that occurred in Colorado.<sup>182</sup> In 2007, the petitioner, Dennis Obduskey (Obduskey), bought a home in Colorado and financed the purchase with a \$329,940.00 loan secured by the property.<sup>183</sup> Approximately two years later, Obduskey defaulted.<sup>184</sup> In 2014, Wells Fargo Bank, N.A., the lender, hired a law firm, McCarthy & Holthus, LLP (McCarthy), to act as its agent in conducting a nonjudicial foreclosure proceeding.<sup>185</sup> McCarthy next sent Obduskey a letter that purported to provide notice of the foreclosure in accordance with the FDCPA and Colorado law.<sup>186</sup> Obduskey

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175. *Id.* at 442.

176. 139 S. Ct. 1029, 1033 (2019).

177. *See id.*

178. *See id.*

179. *See id.*

180. *See id.* at 1035.

181. *Id.* at 1033.

182. *Id.* at 1034.

183. *Id.*

184. *Id.*

185. *Id.* at 1035.

186. *Id.*

responded to the letter, invoking Section 1692g(b) of the FDCPA, “which provides that if a consumer disputes the amount of a debt, a ‘debt collector’ must ‘cease collection’ until it ‘obtains verification of the debt’ and mails a copy to the debtor.”<sup>187</sup> However, McCarthy allegedly did not comply with this provision, and instead initiated a nonjudicial foreclosure action.<sup>188</sup>

Obduskey next filed a federal lawsuit against McCarthy, alleging that the firm had violated the FDCPA for failing to comply with verification procedure.<sup>189</sup> The U.S. District Court for the District of Colorado dismissed the suit, finding that McCarthy was not a “debt collector” within the meaning of the Act.<sup>190</sup> The U.S. Court of Appeals for the Tenth Circuit affirmed. The Supreme Court granted certiorari.<sup>191</sup>

At issue was whether McCarthy, who undisputedly was in the “business the principal purpose of which is the enforcement of security interests,” was a “debt collector” under the FDCPA, such that all provisions of the Act, not just Section 1692f(6), applied.<sup>192</sup> The Supreme Court first analyzed the FDCPA’s definition of a “debt collector.”<sup>193</sup> The first sentence of the definition says that a “debt collector” is “any person . . . in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or asserted to be owed or due another.”<sup>194</sup> The third sentence of the definition, which the Court coined as the “limited-purpose” definition, provides: “[f]or the purpose of section 1692f(6) [the] term [debt collector] also includes any person . . . in any business the principal purpose of which is the enforcement of security interests.”<sup>195</sup> Section 1692f(6), in turn, prohibits a debt collector from engaging in certain unfair or unconscionable conduct.<sup>196</sup> While no party disputed Section 1692f(6) applied to McCarthy, the question became—do the other provisions, including Section 1692g(b) at issue in this case, apply?<sup>197</sup>

The Supreme Court’s opinion was really one of statutory interpretation.<sup>198</sup> The main canon the Court relied upon was to “generally presum[e] that statutes do not contain surplusage.”<sup>199</sup> Specifically, the word “also” in the limited-purpose definition strongly suggested to the Court that a business who does no more than enforce surety interests

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187. *Id.*

188. *Id.*

189. *Id.*

190. *Id.*

191. *Id.*

192. *Id.*

193. *Id.*

194. *Id.* at 1036 (citing 15 U.S.C. § 1692a(6) (2012)).

195. *Id.* (citing 15 U.S.C. § 1692f(6) (2012)).

196. *Id.*

197. *Id.*

198. *See id.* at 1037.

199. *Id.* (quoting *Arlington Cent. Sch. Dist. Bd. of Educ. v. Murphy*, 548 U.S. 291, 299, n.1 (2006)).

does not fall within the scope of the general definition.<sup>200</sup> The Court conceded that while it is possible Congress included the word “also” to emphasize that a debt collector includes such a business, this reading would render the phrase superfluous.<sup>201</sup>

The Supreme Court gave two other reasons behind its decision.<sup>202</sup> First, the Court reasoned that it was likely Congress chose to treat security-interest enforcement differently than ordinary debt collection in order to avoid conflicts with state nonjudicial foreclosure proceedings.<sup>203</sup> Second, the legislative history of the FDCPA was telling.<sup>204</sup> The Court highlighted that in drafting the FDCPA, Congress considered a version “that would have subjected security-interest enforcers to the full coverage of the Act.”<sup>205</sup> Accordingly, the Supreme Court held that “but for § 1692f(6), those who engage in only nonjudicial foreclosure proceedings are not debt collectors within the meaning of the Act.”<sup>206</sup>

To *Obduskey* and other consumer borrowers, the Supreme Court’s opinion may raise fear that its decision “will open a loophole” and permit creditors “to engage in a host of abusive practices forbidden by the Act.”<sup>207</sup> Justice Sotomayor wrote a concurrence on this point, noting that the case was a “close case” and that it “does not prevent Congress from clarifying this statute if we have gotten it wrong.”<sup>208</sup> Until then, however, the Supreme Court “must enforce the statute that Congress enacted.”<sup>209</sup>

## V. JURISDICTION

### A. FIFTH CIRCUIT HOLDS THE TIME-OF-FILING RULE APPLIES TO “RELATED-TO” BANKRUPTCY JURISDICTION IN *DOUBLE EAGLE ENERGY SERVICES, L.L.C. v. MARKWEST UTICA EMG, L.L.C.*

Under the long-standing time-of-filing rule, “the jurisdiction of the Court depends upon the state of things at the time the action brought.”<sup>210</sup> In *Double Eagle Energy Services, L.L.C. v. Markwest Utica Emg, L.L.C.*,<sup>211</sup> the U.S. Court of Appeals for the Fifth Circuit clarified that, although courts apply the time-of-filing rule more frequently to the context of diversity or federal question jurisdiction contexts, the rule is equally applicable to bankruptcy jurisdiction.<sup>212</sup> In this case, it meant that that the district court’s “related-to” bankruptcy jurisdiction was deter-

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200. *Id.*

201. *Id.*

202. *See id.*

203. *Id.*

204. *Id.*

205. *Id.*

206. *Id.* at 1038.

207. *Id.* at 1040.

208. *Id.*

209. *Id.*

210. *Grupo Dataflux v. Atlas Glob. Grp., L.P.*, 541 U.S. 567, 570 (2004).

211. 936 F.3d 260 (5th Cir. 2019).

212. *Id.* at 263–64.

mined at the time the case was filed, even following the debtor's later assignment of claims it brought against third parties to one of its creditors.<sup>213</sup>

Double Eagle Energy Services, L.L.C. (the Debtor) filed for Chapter 11 bankruptcy and later sued Markwest Utica Emg, L.L.C. and Ohio Gathering Company, L.L.C. (collectively, the Defendants) on a contract claim in the U.S. District Court for the Western District of Louisiana.<sup>214</sup> The district court established subject matter jurisdiction under 28 U.S.C. § 1334(b) insofar as the Debtor's contract suit was a "'civil proceeding[ ] . . . related to' a bankruptcy."<sup>215</sup> The Debtor then assigned its claim against the Defendants to one of its creditors.<sup>216</sup> The Defendants moved to dismiss the case, arguing that (1) the assignment eliminated bankruptcy subject matter jurisdiction and accordingly, (2) the Louisiana federal court lacked personal jurisdiction over the Defendants.<sup>217</sup> The magistrate judge agreed with the Defendants and the district court adopted the magistrate's recommendation over the Debtor's objection.<sup>218</sup> The Debtor next appealed to the Fifth Circuit.<sup>219</sup>

The U.S. Court of Appeals for the Fifth Circuit addressed three issues on appeal.<sup>220</sup> First, the Fifth Circuit held that the district court erred because it did not consider the time-of-filing rule in its analysis.<sup>221</sup> Second, because the lower court retained bankruptcy jurisdiction over the lawsuit, it also had personal jurisdiction over the Defendants by way of Bankruptcy Rule 7004(d), which permits nationwide service of process.<sup>222</sup> Third, the Fifth Circuit addressed discretionary dismissal and venue transfer; ultimately, the Fifth Circuit vacated and remanded the case back to the district court to consider those two issues.<sup>223</sup>

The Fifth Circuit first analyzed the application of the time-of-filing rule.<sup>224</sup> "Although courts have not often considered the time-of-filing rule for cases related to bankruptcy, it applies to bankruptcy jurisdiction no less than it applies to diversity or federal question jurisdiction."<sup>225</sup> The Fifth Circuit correctly acknowledged that even the closing of a bankruptcy case does not divest courts of Section 1334(b) jurisdiction over

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213. *See id.*

214. *Id.* at 263.

215. *Id.*

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.*

220. *See id.* at 263–65.

221. *See id.* at 263–64.

222. *See id.* at 264.

223. *See id.* at 264–65.

224. *See id.* at 263.

225. *Id.* (first citing *Randall & Blake, Inc. v. Evans (In re Canion)*, 196 F.3d 579, 586 n.29 (5th Cir. 1999); then citing *Owens-Ill., Inc. v. Rapid Am. Corp. (In re Celotex Corp.)*, 124 F.3d 619, 626 (4th Cir. 1997); and then citing *In re Worldcom, Inc. Sec. Litig.*, 294 B.R. 553, 556 (S.D.N.Y. 2003)).

cases that, when filed, were related to the bankruptcy.<sup>226</sup> However, the Fifth Circuit explained that there is a general rule that strongly favors dismissal under such circumstances.<sup>227</sup>

Second, the district court's failure to apply the time-of-filing rule also meant that its personal jurisdiction analysis was flawed.<sup>228</sup> Personal jurisdiction has two requirements: (1) authorization for service of summons; and (2) a "constitutionally sufficient relationship" between the defendant and the forum (also known as the "minimum contacts" test).<sup>229</sup> The Fifth Circuit noted that if the present case involved a contract claim in federal court on the basis of diversity jurisdiction, the only authority to serve the Defendants would be through Federal Rule of Civil Procedure 4.<sup>230</sup> Under Rule 4 in this instance, the Defendants must be subject to personal jurisdiction in Louisiana courts.<sup>231</sup> Furthermore, Fourteenth Amendment due process would require that the Defendants have sufficient contacts with the state of Louisiana.<sup>232</sup> Relying on Rule 4, the district court determined that Defendants' contacts with Louisiana were insufficient.<sup>233</sup>

But the lower court did not consider Bankruptcy Rule 7004.<sup>234</sup> Rule 7004 permits bankruptcy courts to serve defendants throughout the United States.<sup>235</sup> Therefore, with respect to the Defendants' "constitutionally sufficient relationship" with the forum, nationwide service means that the forum is the United States.<sup>236</sup> As U.S. residents, the Defendants have sufficient contact with the forum such that it would not "offend traditional notions of fair play and substantial justice" to hail them into federal court.<sup>237</sup> Relying on Bankruptcy Rule 7004, the Fifth Circuit concluded that the Louisiana federal court had personal jurisdiction over the Defendants.<sup>238</sup>

Third, the Defendants argued that there were alternative grounds to affirm the district court's dismissal; namely, the general rule favoring discretionary dismissal involving facts such as the facts of this case.<sup>239</sup> However, the Fifth Circuit's "ordinary practice for discretionary decisions is remanding to 'allow the district court to exercise [its discretion] in the

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226. *Id.* at 263–64.

227. *Id.* (first citing *Porges v. Gruntal & Co. (In re Porges)*, 44 F.3d 159, 162 (2d Cir. 1995); then citing *In re Querner*, 7 F.3d 1199, 1201 (5th Cir. 1993)).

228. *Id.* at 264.

229. *Id.*

230. *Id.*; see FED. R. CIV. P. 4(k)(1)(A).

231. *Double Eagle Energy Servs., L.L.C.*, 936 F.3d at 264.

232. *Id.*

233. *Id.*

234. *Id.*

235. *Id.*; see FED. R. BANKR. P. 7004(d).

236. *Double Eagle Energy Servs., L.L.C.*, 936 F.3d at 264.

237. *Id.* (citing *Busch v. Buchman, Buchman & O'Brien, Law Firm*, 11 F.3d 1255, 1258 (5th Cir. 1994)).

238. *Id.*

239. *Id.*

first instance.’”<sup>240</sup> It did so here.<sup>241</sup> Moreover, the Fifth Circuit charged the district court with considering the forum selection clause in the parties’ contract to determine whether it permitted a venue change on remand.<sup>242</sup>

In conclusion, *Double Eagle Energy Services, L.L.C. v. Markwest Utica Emg, L.L.C.* is significant because the Fifth Circuit confirmed the applicability of the time-of-filing rule to the bankruptcy context. When a case falls within a federal court’s related-to-bankruptcy jurisdiction and post-filing actions dissolve the bankruptcy connection, the time-of-filing rule means that a federal court retains both Section 1334(b) and personal jurisdiction over the case. However, district courts still have discretion to dismiss under such facts. This is important for parties to remember whenever litigating related-to bankruptcy actions in federal court.

#### B. IT MEANS WHAT IT SAYS: THE FIFTH CIRCUIT EXPANDS BANKRUPTCY JURISDICTION TO SOCIAL SECURITY CLAIMS

In *Benjamin v. United States of America, Social Security Administration (In re Benjamin)*,<sup>243</sup> the U.S. Court of Appeals for the Fifth Circuit held that a bankruptcy court has subject-matter jurisdiction to hear a dispute concerning overpayment of social security benefits to a Chapter 7 debtor.<sup>244</sup> Specifically, the Fifth Circuit held that 42 U.S.C. § 405(h), which provides that no claim arising under the Social Security Act can be brought under 28 U.S.C. §§ 1331 or 1346, does not bar bankruptcy courts from exercising their jurisdiction under 28 U.S.C. § 1334 to hear social security claims.<sup>245</sup> The Fifth Circuit’s holding is at odds with the view held by the U.S. Courts of Appeals for the Third, Seventh, Eighth, and Eleventh Circuits.<sup>246</sup> Consequently, the Fifth Circuit’s ruling has reenergized the debate over whether bankruptcy courts have the statutory authority to adjudicate social security claims. Given the level of bankruptcy filings in the health care industry, *In re Benjamin* highlights a circuit split of critical significance to insolvent health care providers and debtors alike.

The controversy in *In re Benjamin* concerns a debtor, Kenneth Benjamin (Benjamin), who sought recovery from the U.S. government for amounts withheld from his social security payments.<sup>247</sup> Benjamin was the

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240. *Id.* (citing *Al Rashaid v. Nat’l Oilwell Varco, Inc.*, 757 F.3d 416, 424–25 (5th Cir. 2014)).

241. *Id.*

242. *Id.* at 264–65.

243. 932 F.3d 293 (5th Cir. 2019).

244. *Id.* at 300.

245. *Id.*

246. See *Fla. Agency for Health Care Admin. v. Bayou Shores SNF, LLC (In re Bayou Shores SNF, LLC)*, 828 F.3d 1297, 1314 (11th Cir. 2016); *Nichole Med. Equip. & Supply, Inc. v. TriCenturion, Inc.*, 694 F.3d 340, 346–47 (3d Cir. 2012); *Midland Psychiatric Assocs., Inc. v. United States*, 145 F.3d 1000, 1004 (8th Cir. 1998); *Bodimetric Health Servs. v. Aetna Life & Cas.*, 903 F.2d 480, 488–90 (7th Cir. 1990).

247. *In re Benjamin*, 932 F.3d at 295.

designated beneficiary of his sister's disability benefits.<sup>248</sup> In September 2013, the Social Security Administration (SSA) informed Benjamin that his sister's benefits had expired in April 2012 because she had returned to work, resulting in an overpayment of \$19,286.90.<sup>249</sup> Benjamin and his sister requested reconsideration of the overpayment determination and a waiver of overpayment.<sup>250</sup> Although the SSA did not immediately consider the waiver request, it started withholding a portion of Benjamin's social security payments in September 2014 to make up for the alleged overpayment.<sup>251</sup> After the SSA collected approximately \$6,000.00 from Benjamin, it abruptly stopped withholding the money from his monthly social security checks.<sup>252</sup> Eventually, the SSA denied Benjamin's waiver request in July 2016 and resumed withholding payments. After the SSA ruled against Benjamin, he appealed to an administrative law judge.<sup>253</sup> The appeal has yet to be decided.

In May 2017, Benjamin filed for Chapter 7 relief in the U.S. Bankruptcy Court for the Southern District of Texas after the SSA resumed withholding funds from his social security checks.<sup>254</sup> Notably, Benjamin initiated an adversary proceeding against the SSA in bankruptcy court asserting that the SSA collected \$6,000.00 from him illegally and in violation of its own regulations.<sup>255</sup> The SSA moved to dismiss Benjamin's claims for lack of subject-matter jurisdiction, asserting that Benjamin alleged violations that first needed to be exhausted through the administrative-appeal process.<sup>256</sup> The bankruptcy court agreed and granted the SSA's motion to dismiss.<sup>257</sup> Benjamin appealed to the district court, which affirmed the bankruptcy court's dismissal on jurisdictional grounds.<sup>258</sup> Accordingly, Benjamin appealed to the Fifth Circuit.

On appeal, the sole issue before the Fifth Circuit was whether the bankruptcy court had jurisdiction to hear Benjamin's social security claims.<sup>259</sup> Indeed, the primary issue hinged on the interpretation of Section 405(h) of the Social Security Act.<sup>260</sup> Section 405(h) of the Social Security Act provides, in relevant part,

No findings of fact or decision of the Commissioner of Social Security shall be reviewed by any person, tribunal, or governmental agency except as [provided in § 405(g)]. *No action against the United States, the Commissioner of Social Security, or any officer or employee thereof shall be brought under section 1331 or 1346 of title 28[ ]*

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248. *Id.* at 294.

249. *Id.* at 294–95.

250. *Id.* at 295.

251. *Id.*

252. *Id.*

253. *Id.*

254. *Id.*

255. *Id.*

256. *Id.*

257. *Id.*

258. *Id.*

259. *Id.*

260. *See generally id.*



to recover on any claim arising under [Title II of the Social Security Act].<sup>261</sup>

As originally enacted in 1939, Section 405(h) barred *all* jurisdictional grants to the federal courts, meaning only the SSA had authority to adjudicate social security claims.<sup>262</sup> In 1984, however, Congress revised Section 405(h) to its current form, which in its plain text deprives federal courts of jurisdiction over Social Security, Medicare, and Medicaid disputes under Sections 1331 and 1346 *only*.<sup>263</sup> Consequently, circuit courts disagree as to whether Congress intended its amendments to substantially change the scope of Section 405(h).<sup>264</sup>

Here, the SSA relied on the legislative history of Section 405(h) to assert that the Social Security Act bars Section 1334 jurisdiction.<sup>265</sup> The Third, Seventh, and Eighth Circuits have previously considered similar arguments. Indeed, these circuit courts have held that Congress intended for the current form of Section 405(h) to set forth a bar to *all* cases in which administrative remedies have not been exhausted, not only those in which Sections 1331 or 1346 might otherwise provide jurisdiction.<sup>266</sup> Specifically, the Third, Seventh, and Eighth Circuits agree that the 1984 amendments to Section 405(h) did not substantively change the scope or purpose of the original statute. Recently, the Eleventh Circuit expanded this body of law and based its holding on the recodification canon, which states that “when legislatures codify the law, courts should presume that no substantive change was intended absent a clear indication otherwise.”<sup>267</sup> In applying this canon, the Eleventh Circuit reasoned that the Office of Law Revision Counsel must have made an error by not including in the 1984 amendments the full range of jurisdictional grants listed under the prior version of Section 405(h).<sup>268</sup>

In contrast, Benjamin argued to the Fifth Circuit that the plain language of Section 405(h) *only* bars jurisdiction under Sections 1331 and 1346—but not under Section 1334. Accordingly, Benjamin relied on the Ninth Circuit’s decision in *Sullivan v. Town & Country Home Nursing Services, Inc. (In re Town & Country Home Nursing Services Inc.)*.<sup>269</sup> There, the Ninth Circuit held that the language of Section 405(h) only bars actions under Sections 1331 and 1346 and in no way prohibits an

261. 42 U.S.C. § 405(h) (2012).

262. *In re Benjamin*, 932 F.3d at 296 (emphasis added).

263. *Id.* at 297 (emphasis added).

264. *Id.*

265. *Id.* at 296–97.

266. See generally *Nichole Med. Equip. & Supply, Inc. v. TriCenturion, Inc.*, 694 F.3d 340, 346–47 (3d Cir. 2012); *Midland Psychiatric Assocs., Inc. v. United States*, 145 F.3d 1000, 1004 (8th Cir. 1998); *Bodimetric Health Servs. v. Aetna Life & Cas.*, 903 F.2d 480, 488–90 (7th Cir. 1990) (holding Section 405(h) of the Social Security Act includes a “hidden jurisdictional bar”).

267. *Fla. Agency for Health Care Admin. v. Bayou Shores SNF, LLC (In re Bayou Shores SNF, LLC)*, 828 F.3d 1297, 1314 (11th Cir. 2016).

268. *Id.* at 1319.

269. 963 F.2d 1146 (9th Cir. 1991).

assertion of jurisdiction under Section 1334.<sup>270</sup> Notably, the Ninth Circuit emphasized that Congress intended for bankruptcy courts to have jurisdiction over all matters “conceivably having an effect on the bankruptcy estate.”<sup>271</sup>

In the instant case, the Fifth Circuit rejected the majority approach and joined the Ninth Circuit in applying the plain meaning of Section 405(h).<sup>272</sup> Acknowledging the recodification canon’s usefulness in certain instances, the Fifth Circuit found it applicable only “in the absence of a clear indication from Congress that it intended to change the law’s substance.”<sup>273</sup> Finding the “most obvious source of congressional intent” to be the clear statutory text, the Fifth Circuit held that “[section 405(h)] mean[s] what it says. And it says nothing about section 1334.”<sup>274</sup> Consequently, the Fifth Circuit reversed the district court’s ruling and remanded the case.

Debtor Benjamin did not win outright, however. The second sentence in Section 405(h) provides, “[n]o findings of fact or decision of the Commissioner of Social Security shall be reviewed by any person, tribunal, or governmental agency except as [provided in section 405(g)].”<sup>275</sup> The Fifth Circuit noted that on remand “the bankruptcy court should examine Benjamin’s claims and determine whether they are primarily about his entitlement to benefits . . . or claim for money because the SSA failed to comply with its own regulations in recouping the overpayment.”<sup>276</sup> According to the Fifth Circuit, the bankruptcy court would have jurisdiction under the latter because his claim would not be channeled by Section 405(h)’s second sentence into Section 405(g).<sup>277</sup>

*In re Benjamin* highlights an important circuit split that has implications on health care providers, debtors, and creditors. While debtors in the Ninth and Fifth Circuit courts may adjudicate their social security claims in a speedy hearing in front of a bankruptcy court, debtors in the Third, Seventh, Eighth, and Eleventh Circuits must resolve their social security claims through an administrative appeals process. Moreover, bankruptcy jurisdiction over Medicare and Medicaid claims is also derived from Section 405(h). Certainly, Medicare and Medicaid issues are often tangled with other factors that lead to a debtor’s bankruptcy filing. Curtailing a bankruptcy court’s authority to hear such issues could significantly impair a healthcare provider’s bankruptcy case.<sup>278</sup> Until the U.S.

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270. *Id.* at 1155.

271. *Id.*

272. *See Benjamin v. U.S. Soc. Sec. Admin. (In re Benjamin)*, 932 F.3d 293, 298 (5th Cir. 2019).

273. *Id.*

274. *Id.* at 298, 300.

275. 42 U.S.C. § 405(h) (2012).

276. *In re Benjamin*, 932 F.3d at 302.

277. *Id.*

278. *See, e.g., Fla. Agency for Health Care Admin. v. Bayou Shores SNF, LLC (In re Bayou Shores SNF, LLC)*, 828 F.3d 1297 (11th Cir. 2016). There, the Eleventh Circuit held

Supreme Court addresses the circuit split, health care providers may seek greater refuge under Ninth and Fifth Circuit's interpretation of the law.

C. FIFTH CIRCUIT RULES THE SEVEN SEAS: COURT REAFFIRMS  
DISTINCTION BETWEEN DIRECT AND DERIVATIVE INJURIES

In *Meridian Capital CIS Fund v. Burton (In re Buccaneer Resources, L.L.C.)*,<sup>279</sup> the U.S. Court of Appeals for the Fifth Circuit affirmed the decisions of the U.S. District Court and the U.S. Bankruptcy Court for the Southern District of Texas in holding that a creditor's tortious interference claim against a non-debtor third party was not property of the estate.<sup>280</sup> Because the tortious interference claim alleged a direct injury to the creditor, and was not dependent on an injury to the bankruptcy estate, the court lacked bankruptcy jurisdiction over the claim.<sup>281</sup> Accordingly, the Fifth Circuit affirmed the bankruptcy court's order remanding the case to state court.<sup>282</sup> The Fifth Circuit's holding provides guidance to judges and attorneys on the distinction between direct and derivative injuries, an issue which arises frequently in litigation in bankruptcy courts.

Curtis Burton (Burton) was the Chief Operating Officer of *Buccaneer Resources, L.L.C.* (the Debtor), an oil exploration and production company, until his termination in 2014.<sup>283</sup> The Debtor's business began to falter and in January 2014, *Meridian Capital CIS Fund* (*Meridian*) purchased all of the Debtor's senior debt.<sup>284</sup> While the aid from *Meridian* prevented the Debtor from immediate insolvency, the Debtor's business continued to decline and it subsequently filed for Chapter 11 in May 2014.<sup>285</sup> But just prior to its bankruptcy filing, the Debtor fired Burton.<sup>286</sup> Burton alleged that the termination violated the terms of his employment contract and that *Meridian* was involved in the Debtor's decision.<sup>287</sup> Burton filed a claim in the bankruptcy case but later withdrew it.<sup>288</sup> Ultimately, the Debtor and *Meridian* reached a settlement in which the Debtor agreed to release *Meridian* from any potential claims the Debtor may have had against it in exchange for \$10 million.<sup>289</sup> The agreement was incorporated into the Debtor's bankruptcy plan.<sup>290</sup>

Burton next instituted a suit against *Meridian* in state court alleging tortious interference with contract.<sup>291</sup> *Meridian* sought to remove the

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that bankruptcy courts lack jurisdiction under Section 405(h) to hear claims under the Social Security Act. *Id.*

279. 912 F.3d 291, 292 (5th Cir. 2019).

280. *Id.*

281. *Id.* at 296–97.

282. *Id.* at 297.

283. *Id.* at 292.

284. *Id.* at 293.

285. *Id.*

286. *Id.*

287. *Id.*

288. *Id.*

289. *Id.*

290. *Id.*

291. *Id.*

case to the U.S. Bankruptcy Court for the Southern District of Texas, arguing that the claims alleged by Burton belonged to the Debtor's estate and were thus released by the agreement between Meridian and the Debtor.<sup>292</sup> The bankruptcy court disagreed with Meridian and concluded that the tortious interference claim belonged to Burton and should be litigated in state court.<sup>293</sup> The district court agreed with the bankruptcy court and remanded all of Burton's claims to state court. An appeal to the Fifth Circuit followed.<sup>294</sup>

On appeal to the Fifth Circuit, the question for the court centered on whether the tortious interference claim belonged to Burton or to the Debtor.<sup>295</sup> If it belonged solely to Burton, there would be no basis for bankruptcy jurisdiction and the claim should be heard in state court.<sup>296</sup> If it belonged to the Debtor, the bankruptcy court would be the proper forum because the claim would be property of the estate.<sup>297</sup>

The Fifth Circuit relied on its decision in *Highland Capital Management LP v. Chesapeake Energy Corporation (In re Seven Seas Petroleum, Inc.)*<sup>298</sup> in its analysis of the issue.<sup>299</sup> In *In re Seven Seas Petroleum, Inc.*, the Fifth Circuit held that when determining whether the bankruptcy estate or a creditor could pursue a claim against non-debtor third parties, the bankruptcy court must focus on whether the creditor has suffered a direct injury or one that is derivative of an injury to the debtor.<sup>300</sup> For claims that belong to a particular creditor or group of creditors and do not involve any harm to the debtor, the claim is a direct injury and cannot be part of the estate.<sup>301</sup> The Fifth Circuit used *In re Seven Seas Petroleum, Inc.* as an example of a direct injury.<sup>302</sup> In that case, unsecured bondholders had relied on false oil reserve estimates when deciding whether to invest in the debtor.<sup>303</sup> There, the Fifth Circuit held that the induced reliance did not injure the debtor, only the bondholders, so the injury was direct and belonged to the creditors.<sup>304</sup> If, however, the harm to a creditor comes about only due to harm to the debtor, then its injury is derivative, and the claim is property of the bankruptcy estate.<sup>305</sup> In its analysis of derivative injuries, the Fifth Circuit provided numerous cases where the injury was a derivative one.<sup>306</sup>

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292. *Id.*

293. *Id.*

294. *Id.*

295. *Id.*

296. *Id.*

297. *Id.*; see also 11 U.S.C. § 541(a)(1) (2012).

298. 522 F.3d 575 (5th Cir. 2008).

299. *In re Buccaneer Res., L.L.C.*, 912 F.3d at 293–94; see also *In re Seven Seas Petroleum, Inc.*, 522 F.3d 575.

300. *In re Buccaneer Res., L.L.C.*, 912 F.3d at 294.

301. *Id.* at 293.

302. *Id.* at 293–94.

303. *Id.* at 294.

304. *Id.*

305. *Id.*

306. See *id.* (citing *Grossman v. Belridge Grp. (In re Lothian Oil, Inc.)*, 531 F. App'x 428, 439–40 (5th Cir. 2013) (“The creditors’ injury (reduced bankruptcy recovery) derived

In this case, Meridian argued that Burton's tortious interference cause of action was really one for lender liability in disguise.<sup>307</sup> Meridian asserted that the injury was its improper control of the Debtor and that the improper control led to Burton's termination, making it the derivative harm.<sup>308</sup> The Fifth Circuit was not persuaded by Meridian's argument.<sup>309</sup> "As long as the injury a creditor is pursuing against a third party does not stem from the depletion of estate assets," the court noted, "the injury is a direct one that does not belong to the estate."<sup>310</sup>

The Fifth Circuit concluded that the harm to Burton from his termination without severance did not depend on any harm to the Debtor.<sup>311</sup> The Fifth Circuit reasoned that the injury to Burton flowed through the Debtor's action, namely, the request of Meridian to terminate Burton in attempt to save the Debtor money, but not because of an injury to the Debtor.<sup>312</sup> The Fifth Circuit went on to find that there is no reason why the estate should recover for a third party's tortious conduct when it did not injure the bankrupt company.<sup>313</sup> In sum, the injury to Burton was a direct one and thus, it belonged to him.<sup>314</sup>

Overall, jurisdiction can often be a complicated issue in bankruptcy cases and proceedings. The holding in *In re Buccaneer Resources, L.L.C.* reiterates the Fifth Circuit's *In re Seven Seas Petroleum, Inc.* framework, while providing guidance as to how the Fifth Circuit distinguishes direct and derivative injuries.

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from injury to the debtor (the loss of estate assets), so only the estate could sue the third parties.")); see also *Schimmelpenninck v. Byrne* (*In re Schimmelpenninck*), 183 F.3d 347, 358 (5th Cir. 1999) ("[A]n alter ego suit that attempted to pierce the corporate veil and recover assets improperly moved through the corporate structure belonged only to the estate."); *Wells Fargo Capital Fin., LLC v. Noble* (*In re R.E. Loans*), No. 3:12-CV-3515-D, 2013 WL 1265205, at \*5 (N.D. Tex. Mar. 28, 2013) ("[T]he plaintiff's injury of a reduced bankruptcy recovery derived from harm to the debtor—that caused by the liens—so the estate owned the claim.").

307. *In re Buccaneer Res., L.L.C.*, 912 F.3d at 295.

308. *Id.*

309. *Id.*

310. *Id.*

311. *Id.* at 294.

312. *Id.*

313. *Id.* (first citing *Feld v. Zale Corp.* (*In re Zale Corp.*), 62 F.3d 746, 755 (5th Cir. 1995) (holding that the bankruptcy court did not have jurisdiction over bad-faith claims third parties brought against a debtor's insurer because "the claims are not property of the estate and they have no effect on the estate"); then citing *Steinberg v. Buczynski*, 40 F.3d 890, 893 (7th Cir. 1994) ("When a third party has injured not the bankrupt corporation itself but a creditor of that corporation, the trustee in bankruptcy cannot bring suit against the third party.")).

314. *Id.* at 295.

## VI. CHAPTER 11

A. FIFTH CIRCUIT WITHDRAWS CONTROVERSIAL RULING ON SOLVENT-DEBTOR EXCEPTION IN *IN RE ULTRA PETROLEUM CORP.*, BUT ITS PRIOR HOLDING ON IMPAIRMENT REMAINS

In *Keystone Gas Gathering, L.L.C. v. Ad Hoc Committee (In re Ultra Petroleum Corp.)*,<sup>315</sup> the U.S. Court of Appeals for the Fifth Circuit sided with the debtors and held that the creditors were unimpaired—thus ineligible to vote on the plan of reorganization—where the plan paid the creditors everything allowed by the Bankruptcy Code.<sup>316</sup> This meant that although the creditors would be entitled to a make-whole premium and post-petition interest under state law, the Bankruptcy Code freed the debtors of this obligation under Section 502(b)(2).<sup>317</sup> In its now withdrawn opinion, however, the Fifth Circuit went a step further and expressed doubt as to whether the solvent-debtor exception survived the enactment of Section 502(b)(2) of the Bankruptcy Code.<sup>318</sup> On petition for rehearing en banc, the Fifth Circuit replaced its earlier 2019 opinion and removed its controversial discussion on the solvent-debtor exception.<sup>319</sup>

The facts of the case are extremely rare.<sup>320</sup> The debtors entered Chapter 11 bankruptcy insolvent, but later became solvent “by virtue of a lottery-like rise in commodity prices.”<sup>321</sup> Accordingly, the debtors proposed a Chapter 11 plan of reorganization that they claimed would pay the creditors in full.<sup>322</sup> The Class 4 Creditors<sup>323</sup> objected, claiming that they were impaired (and thus entitled to vote on the plan) because the plan did not require the debtors to pay the contractual make-whole premium and additional post-petition interest at contractual default rates.<sup>324</sup> This additional amount totaled \$387 million.<sup>325</sup>

Under 11 U.S.C. § 502(b)(2), the debtors argued that the make-whole premium qualified as unmatured interest and should be disallowed.<sup>326</sup> In addition, the debtors argued that 11 U.S.C. § 726(a)(5) entitled the creditors to, at most, the post-petition interest at a “legal rate,” not the contract rate.<sup>327</sup> However, the U.S. Bankruptcy Court for the Southern

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315. 943 F.3d 758, 760 (5th Cir. 2019).

316. *Id.* at 760–61.

317. *See id.* at 760–62.

318. *See* *Ultra Petroleum Corp. v. Ad Hoc Comm. of Unsecured Creditors of Ultra Res., Inc. (In re Ultra Petroleum Corp.)*, 913 F.3d 533, 547 (5th Cir. 2019) (withdrawn).

319. *In re Ultra Petroleum Corp.*, 943 F.3d at 765–66.

320. *Id.* at 760.

321. *Id.*

322. *Id.* at 761.

323. The Class 4 Creditors were creditors with claims under the Note Agreement and Revolving Creditor Facility. *Id.*

324. *Id.*

325. *Id.*

326. *Id.* at 762.

327. *Id.*

District of Texas sided with the creditors and held that the creditors receive all that they were entitled to receive under state law in order to be unimpaired.<sup>328</sup> The debtors sought a direct appeal to the Fifth Circuit.<sup>329</sup>

On appeal, the Fifth Circuit reversed the bankruptcy court's opinion and held that a creditor is not impaired by a plan of reorganization that incorporates the Bankruptcy Code's disallowance provisions.<sup>330</sup> In doing so, it sided with a majority of courts that have addressed the issue, noting that "[w]here a plan refuses to pay funds disallowed by the Code, the Code—not the plan—is doing the impairing."<sup>331</sup> Most significant, however, the Fifth Circuit withdrew its previous discussion as to whether the solvent-debtor exception survived the enactment of Section 502(b)(2).<sup>332</sup> Instead, the Fifth Circuit held that the bankruptcy court is best able to consider the post-petition interest question because whether such premiums are in fact unmatured interest, "much depends on the dynamics of the individual case."<sup>333</sup> The Fifth Circuit went on to comment that "the record reveals no reasons why the solvent-debtor exception could not apply."<sup>334</sup> Overall, the Fifth Circuit was "mindful that [it] [is] a court of review, not of first view."<sup>335</sup>

## VII. EQUITABLE MOOTNESS

### A. FIFTH CIRCUIT DECLINES TO EXPAND APPLICATION OF THE EQUITABLE MOOTNESS DOCTRINE IN *IN RE SNEED SHIPBUILDING, INC.*

In *New Industries Inc. v. Byman (In re Sneed Shipbuilding, Inc.)*,<sup>336</sup> the U.S. Court of Appeals for the Fifth Circuit held that an appeal of a bankruptcy court's approval of a settlement agreement and sale of estate assets was not equitably moot where (1) the sale and settlement were not sufficiently complex; and (2) the appeal was already statutorily moot under Section 363(m) of the Bankruptcy Code.<sup>337</sup> In doing so, the Fifth Circuit declined to expand the equitable mootness beyond appeals of

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328. *Id.*

329. *Id.*

330. *Id.* at 760, 762.

331. *Id.* at 763 (first citing *In re Tree of Life Church*, 522 B.R. 849, 861–62 (Bankr. D.S.C. 2015); then citing *In re RAMZ Real Estate Co.*, 510 B.R. 712, 717 (Bankr. S.D.N.Y. 2014); then citing *In re K Lunde, LLC*, 513 B.R. 587, 595–96 (Bankr. D. Colo. 2014); then citing *In re Mirant Corp.*, No. 03-46590-DML-11, 2005 WL 6440372, at \*3 (Bankr. N.D. Tex. May 24, 2005); then citing *In re Coram Healthcare Corp.*, 315 B.R. 321, 351 (Bankr. D. Del. 2004); then citing *In re Monclova Care Ctr., Inc.*, 254 B.R. 167, 177 (Bankr. N.D. Ohio 2000), *rev'd on other grounds*, 266 B.R. 792 (N.D. Ohio 2001); and then citing *In re Am. Solar King Corp.*, 90 B.R. 808, 819–22 (Bankr. W.D. Tex. 1988)).

332. *See id.* at 765–66.

333. *Id.* at 765.

334. *Id.*

335. *Id.* at 766.

336. 914 F.3d 1000, 1001 (5th Cir. 2019).

337. *See* 11 U.S.C. § 363(m) (2012); *In re Sneed Shipbuilding, Inc.*, 914 F.3d at 1001.

“substantially consummated” Chapter 11 plans of reorganization.<sup>338</sup> The decision reiterates the Fifth Circuit’s hesitancy to invoke the equitable mootness doctrine as compared alongside its sister circuits, opting instead to treat it “as a ‘scalpel rather than an axe.’”<sup>339</sup>

As background, Sneed Shipbuilding, Inc. (the Debtor) owned two shipyards in Texas, including one in Channelview.<sup>340</sup> In 2016, it filed for Chapter 11 bankruptcy.<sup>341</sup> After reorganization proved “tumultuous,” the U.S. Bankruptcy Court for the Southern District of Texas appointed a Chapter 11 trustee.<sup>342</sup> The trustee filed an adversary proceeding against the probate estate of the Debtor’s principal, Martin Sneed (Mr. Sneed), and several of his family members for “attempt[ing] to fraudulently transfer ownership of the Channelview shipyard to himself, among other fraudulent activities.”<sup>343</sup> The trustee asked the bankruptcy court to determine that the Debtor, not Mr. Sneed, was the titleholder of the Channelview shipyard.<sup>344</sup> Before the bankruptcy court could resolve the issue, however, the trustee and Mr. Sneed’s probate estate reached a settlement agreement so that the shipyard could be sold to a third-party buyer with clear title.<sup>345</sup>

The settlement and sale agreements were executed together under the following terms: (1) the buyer paid the Debtor \$15 million for the shipyard, which the trustee used to ensure title to the property was free of all encumbrances;<sup>346</sup> and (2) Mr. Sneed’s probate estate agreed to forego any claim to the Channelview shipyard and all other claims in the bankruptcy estate in return for \$8 million and an agreement from the trustee to drop any outstanding avoidance actions.<sup>347</sup> New Industries, Inc. (New Industries), an unsecured creditor of the Debtor, objected to the proposal and took specific issue with the provision authorizing the \$8 million deposit to the probate estate.<sup>348</sup> But the bankruptcy court overruled the objection and approved the sale and settlement agreement, declaring them as “non-severable and mutually dependent.”<sup>349</sup> New Industries appealed, but did not request a stay of the bankruptcy court’s ruling.<sup>350</sup>

On appeal to the U.S. District Court for the Southern District of Texas, the trustee requested that the case be dismissed as equitably moot, or

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338. *Id.* at 1003 (quoting *Hilal v. Chapter 11 Tr. Randy W. Williams (In re Hilal)*, 534 F.3d 498, 500 (5th Cir. 2008)).

339. *Id.* (quoting *Bank of N.Y. Tr. Co., NA v. Official Unsecured Creditors’ Comm. (In re Pacific Lumber Co.)*, 584 F.3d 229, 240 (5th Cir. 2009)).

340. *Id.* at 1001.

341. *Id.*

342. *Id.* at 1002.

343. *Id.*

344. *Id.*

345. *Id.*

346. *Id.* These encumbrances included liens of a secured creditor, the debtor in possession’s lender, and property taxes. *See id.*

347. *Id.*

348. *Id.*

349. *Id.*

350. *Id.*



alternatively, as statutorily moot under 11 U.S.C. § 363(m).<sup>351</sup> The district court granted the dismissal but failed to indicate under which theory dismissal was proper.<sup>352</sup>

New Industries subsequently appealed the district court's ruling to the Fifth Circuit.<sup>353</sup> The Fifth Circuit held that while equitable mootness was not applicable in this case, Section 363(m) of the Bankruptcy Code rendered the appeal moot because New Industries failed to seek a stay of the bankruptcy court's order approving the sale.<sup>354</sup>

In reaching its decision, the Fifth Circuit first addressed whether the appeal was equitably moot.<sup>355</sup> Equitable mootness is a judicial abstention doctrine that appellate courts use to decline review of certain plan confirmation orders in favor of letting a bankruptcy court's decision stand.<sup>356</sup> It gives courts discretion to determine when a confirmed plan is so complicated that reversal or amendment of the plan would be immensely difficult or inequitable to implement.<sup>357</sup> The Fifth Circuit is, self-admittedly, more reluctant to apply equitable mootness than its sister circuits.<sup>358</sup> Quoting the standard articulated in *Hilal v. Chapter 11 Trustee Randy W. Williams (In re Hilal)*,<sup>359</sup> the Fifth Circuit explained that equitable mootness is properly applied when a reorganization plan has been "so substantially consummated that a court cannot order effective relief even though a live dispute remains among some parties to the bankruptcy case."<sup>360</sup>

Applying this standard to the case at bar, the Fifth Circuit determined that equitable mootness did not bar review because this was an appeal of a sale and settlement agreement, not a confirmed plan of reorganization.<sup>361</sup> While other circuits have applied the equitable mootness doctrine in cases involving settlement agreements, these cases involved particularly complex transactions.<sup>362</sup> In comparing the facts of this case with those in *Aurelius Capital Management, L.P. v. Deutsche Bank Trust Company Americas (In re Tribune Media Co.)*,<sup>363</sup> the Fifth Circuit noted that the sale and settlement agreements here were relatively simple and only

351. *Id.*

352. *Id.*

353. *See id.*

354. *See id.* at 1004.

355. *Id.* at 1002.

356. *Id.*

357. *Id.* at 1003. "[T]he concern of equitable mootness is that an appellate reversal might undermine the plan and the parties' reliance on it." *Id.* (citing *Wooley v. Faulkner (In re SI Restructuring, Inc.)*, 542 F.3d 131, 135–36 (5th Cir. 2008)).

358. *Id.* "We are more hesitant to invoke equitable mootness than many circuits, treating it as a 'scalpel rather than an axe.'" *Id.* (quoting *Bank of N.Y. Tr. Co., NA v. Official Unsecured Creditors' Comm. (In re Pacific Lumber Co.)*, 584 F.3d 229, 240 (5th Cir. 2009)).

359. 534 F.3d 498, 500 (5th Cir. 2008).

360. *Id.*

361. *In re Sneed Shipbuilding, Inc.*, 914 F.3d at 1003.

362. *Id.*

363. 799 F.3d 272, 274 (3d Cir. 2015). In *In re Tribune Media Co.*, the Third Circuit applied equitable mootness to an appeal of a multi-billion-dollar reorganization plan which affected several hundred classes of creditors. *See id.*

involved a handful of parties, all of whom were directly involved with the case.<sup>364</sup> The Fifth Circuit found that the transaction in this case was insufficiently complex to warrant an expansion of the doctrine.<sup>365</sup>

While the Fifth Circuit declined to rule that the present appeal was equitably moot, it did find that it was statutorily moot under Section 363(m).<sup>366</sup> Mootness under Section 363(m) of the Bankruptcy Code exists to “encourage parties to bid for estate property” by allowing buyers to rely on the validity of the transaction.<sup>367</sup> In effect, the statute limits the review of a sale of estate property to the judgment of the bankruptcy court, unless a stay preventing the sale is issued before the case is reviewed on appeal.<sup>368</sup> Despite New Industries’s argument that it was not appealing the sale (and only the distribution of funds to the probate estate), the Fifth Circuit determined that the two agreements were inseparable from one another.<sup>369</sup> The sale of the shipyard was contingent upon the probate estate relinquishing all claims to the property, which would not have occurred but for the payment to the probate estate.<sup>370</sup> Since the sale agreement and the settlement agreement were interdependent, the Fifth Circuit could not review one without also reviewing the other.<sup>371</sup> Therefore, Section 363(m) prevented appellate review of the settlement agreement.<sup>372</sup>

This case illustrates the Fifth Circuit’s reluctance to deviate from the status quo. In acknowledging the willingness of other circuits to more readily apply equitable mootness, the court demonstrated a self-awareness of its own narrow view of the doctrine.<sup>373</sup> However, the Fifth Circuit’s discussion and comparison of this case with more complex cases where courts applied equitable mootness outside of the confirmation plan context, suggests that the court may be open to expanding its view of this doctrine should the right case arise. It is also worth bearing in mind that the Fifth Circuit was able to deny appellate review of the sale agreement here without deviating from its own precedent. Under a different set of facts, it is possible that the Fifth Circuit may have ruled differently on the equitable mootness argument in order to achieve an equitable result.

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364. *In re Sneed Shipbuilding, Inc.*, 914 F.3d at 1003 (“Our ability to produce a single graphic to illustrate the Channelview transaction demonstrates that this case does not rise to that level of complexity.”).

365. *See id.*

366. *Id.* at 1004 (citing 11 U.S.C. § 363(m) (2012)).

367. *Id.* at 1003 (citing *Bleaufontaine, Inc. v. Roland Int’l (In re Bleaufontaine, Inc.)*, 634 F.2d 1383, 1389 n.10 (5th Cir. 1981) (“If deference were not paid to the policy of speedy and final bankruptcy sales, potential buyers would not even consider purchasing any bankrupt’s property.”)).

368. *Id.*

369. *Id.* at 1004.

370. *Id.*

371. *Id.*

372. *Id.*

373. *See id.*

## VIII. ATTORNEY'S FEES

## A. NO SOUP FOR YOU! THE FIFTH CIRCUIT AFFIRMS BANKRUPTCY COURT'S DENIAL TO REIMBURSE COUNSEL FOR PRE-PETITION COSTS AND FEES MADE ON BEHALF OF THE DEBTOR

In *McBride v. Riley (In re Riley)*,<sup>374</sup> the U.S. Court of Appeals for the Fifth Circuit considered whether the Western District of Louisiana's no-look fee order permits the reimbursement of advanced fees outside of, and in addition to, the no-look fee amount. Ultimately, the Fifth Circuit affirmed the bankruptcy court's decision, which denied the reimbursement of three pre-petition fees debtor's counsel made on the debtor's behalf, including filing fees, credit counseling fees, and a credit report fee.<sup>375</sup> However, the court vacated the lower court's additional finding that bankruptcy courts lack discretion to award the payment of such fees under 11 U.S.C. §§ 503(b) and 330(a).<sup>376</sup>

The straight-forward facts of the case are as follows: a Chapter 13 debtor's attorney in the Western District of Louisiana (the Appellant) sought reimbursement of certain pre-petition fees.<sup>377</sup> Prior to the filing of the debtor's Chapter 13 petition in 2017, the Appellant and his client (the Debtor) made a "no-money-down agreement" to pay the Appellant \$2,150.00 for his legal services in addition to \$367.00 for advanced payments, including credit counseling fees, filing fees, and a credit report fee.<sup>378</sup> The bankruptcy court ultimately held that its standing order did not permit separate reimbursement of the \$367.00 in fees. The district court affirmed.

On appeal to the Fifth Circuit, the Appellant argued three points.<sup>379</sup> First, that the fees were reimbursable under the Western District of Louisiana's February 2017 no-look fee standing order.<sup>380</sup> Second, that the fees are necessary "administrative expense[s] of the bankrupt estate under 11 U.S.C. § 503."<sup>381</sup> And third, that bankruptcy courts do not lack authority to reimburse counsel for pre-petition costs under Section 503(b)(2) and Section 330(a).<sup>382</sup>

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374. 923 F.3d 433 (5th Cir. 2019).

375. *See id.* at 435.

376. *Id.* at 444.

377. *Id.* at 435.

378. *Id.* at 436.

379. *Id.* at 437–38.

380. *Id.* at 437. The standing order is specific to the Western District of Louisiana and governs no-look fees in Chapter 13 cases. The "no-look fee" option is a common local rule applied by many bankruptcy courts to quicken the payment of attorney's fees in routine cases. *Id.* at 346 ("[T]he no-look fee option generally says that if debtor's counsel charges no more than a given amount for a given case, the attorney fee will be treated as presumptively reasonable under § 330(a), with no need to provide a detailed accounting unless the request is challenged.").

381. *Id.* at 435 (internal quotations omitted).

382. *Id.* at 437–38.

The Fifth Circuit held that under the February 2017 standing order, the bankruptcy court correctly denied the separate reimbursement of advanced payments, alleviating confusion about its omission on whether “advances . . . were not separately reimbursable.”<sup>383</sup> The pre-February order “stated that any advances made by debtor’s counsel for filing fees or other pre-filing expenses were not separately reimbursable.”<sup>384</sup> However, the February 2017 standing order removed the language and did not explicitly address whether advanced payments were reimbursable, bringing its new meaning into question.<sup>385</sup> Despite the absence of such language, the bankruptcy court still interpreted the February 2017 standing order to state, “that any advances made by the debtor’s counsel (with one explicit exception) remained accounted for under the pre-approved no-look fee amount and were not separately reimbursable.”<sup>386</sup> The Fifth Circuit agreed and reasoned that because of the expediting purpose of no-look fees “it seems intuitive that silence on a given expense (particularly a routine expense) means the expense is supposed to be accounted for under the pre-approved no-look fee amount.”<sup>387</sup> The Fifth Circuit also highlighted that the February 2017 standing order only stated one exception for when reimbursement could exceed the no-look fee amount, suggesting the advanced fees fell outside of the scope of reimbursement.<sup>388</sup>

Second, the Fifth Circuit affirmed the bankruptcy court’s holding that the advanced fees paid by counsel were not reimbursable as “administrative expenses necessary for preserving the estate under 11 U.S.C. § 503(b)(1).”<sup>389</sup> The Fifth Circuit used a two-prong test to help categorize what debt constitutes as an administrative expense.<sup>390</sup> To satisfy the first prong, “the debt must arise from a post-petition transaction with the estate, rather than a transaction with the debtor personally.”<sup>391</sup> Likewise, to pass the second prong, “the goods or services received in exchange for the debt must directly benefit the estate.”<sup>392</sup> On review, the Fifth Circuit held that the three advanced payments made by counsel did not satisfy either of the two prongs mentioned above.<sup>393</sup> The Fifth Circuit determined that the filing fee and credit counseling fee were “pre-petition obli-

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383. *Id.* at 438.

384. *Id.* The pre-February standing order did not apply because the agreement regarding payment between the debtor and counsel occurred on February 2, 2017, after the standing order’s February revision and implementation. *Id.* at 436.

385. *Id.* at 437.

386. *Id.* at 438.

387. *Id.*

388. *Id.* The February standing order only stated one cost that “could be reimbursed above and beyond the no-look fee amount—the postage costs for service of the motion to modify the plan.” *Id.*

389. *Id.* at 440.

390. *Id.* at 439; *see* Total Minatome Corp. v. Jack/Wade Drilling, Inc. (*In re* Jack/Wade Drilling, Inc.), 258 F.3d 385, 387 (5th Cir. 2001); *In re* TransAmerica Nat. Gas Corp., 978 F.2d 1409, 1416 (5th Cir. 1992).

391. *In re* Riley, 923 F.3d at 439.

392. *Id.*

393. *See id.* (“We agree with the bankruptcy court and the district court that the advances of the filing fee, credit counseling fee, and credit report fee by the debtor’s counsel

gations owed by [the debtor] in her personal capacity . . . .” The Fifth Circuit also held the credit report fee was not a “necessary expense” because credit reports are not statutorily required to file a Chapter 13 petition.<sup>394</sup>

Last, the Fifth Circuit rejected and vacated the lower courts’ finding that bankruptcy courts lack discretion to reimburse debtors’ attorneys for pre-petition fees made on behalf of the debtor.<sup>395</sup> In the Western District of Louisiana, the bankruptcy court reasoned that pre-petition fees are not reimbursable and should not be categorized as an “administrative expenses” necessary to preserving the estate under Section 503(b)(1).<sup>396</sup> The bankruptcy court came to the same conclusion about reimbursement regarding Section 330(a).<sup>397</sup> The Fifth Circuit determined that the lower courts’ interpretation of Section 330(a) inaccurately applied the reasoning used to interpret Section 503(b)(1).<sup>398</sup> The Fifth Circuit noted that Section 330(a) did not deal with administrative expenses under Section 503(b)(1) and in fact, stated that “courts *may allow* compensation ‘for representing the interest of the debtor in connection with the bankruptcy case.’”<sup>399</sup> Basing its decision on the discretionary nature of Section 330(a), the Fifth Circuit held that bankruptcy courts have discretion to award “compensation and reimbursement . . . under section 330(a) of this title.”<sup>400</sup>

*In re Riley* provides a necessary clarification on the reimbursement of certain fees and expenses in Chapter 13 cases. The Fifth Circuit affirmed the bankruptcy court’s finding that the February 2017 standing order did not permit the reimbursement of pre-petition fees, and that the pre-petition fees should not be considered administrative expenses necessary to the preservation of the estate. Most impactful, the Fifth Circuit vacated the bankruptcy court’s finding that bankruptcy courts always lack authority to award such reimbursements. In doing so, the Fifth Circuit effectively recognized the discretion of bankruptcy courts in determining whether to reimburse debtors’ attorneys for certain pre-petition expenses in Chapter 13 cases.<sup>401</sup>

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in this case were not necessary expenses to preserve the estate under 11 U.S.C. § 503(b)(1).”).

394. *Id.*

395. *Id.* at 441.

396. *Id.* The lower courts relied on this interpretation as a way to avoid pre-petition costs from falling upon creditors. See *In re Riley*, 577 B.R. 497, 510 (Bankr. W.D. La. 2017) (quoting *In re Frazier*, 569 B.R. 361, 367 (Bankr. S.D. Ga. 2017)).

397. *In re Riley*, 923 F.3d at 442.

398. *Id.* (“[The] reasoning appears to be derived from the analysis conducted to determine whether the filing fee was a necessary expense for preserving the estate under § 503(b)(1).”).

399. *Id.* at 443 (quoting Section 330(a)(4)(B)) (emphasis added).

400. 11 U.S.C. § 503(b) (2012). Section 330(a) provides that in Chapter 12 or Chapter 13 cases, courts “*may allow* reasonable compensation to the debtor’s attorney for representing the interests of the debtor . . . .” 11 U.S.C. § 330(a)(4)(B) (2012) (emphasis added).

401. *In re Riley*, 923 F.3d at 443 (“11 U.S.C. §§ 503(b) and 330 provide bankruptcy courts with discretion to compensate debtor’s counsel for advancing the cost of filing fees, credit card counseling fees, and credit card report fees if they chose to do so. . . .”).

## IX. LEGISLATIVE UPDATE

On August 23, 2019, President Trump signed into law three pieces of bankruptcy legislation. The first bill is the Small Business Reorganization Act of 2019 (the SBRA), which creates a new option for bankruptcy relief for small business debtors. The second bill is the Honoring American Veterans in Extreme Need Act of 2019 (the HAVEN Act), which revises the definition of exempt income for debtors who receive certain veterans' benefits. The third bankruptcy amendment is the Family Farmer Relief Act of 2019, which increases the debt limit for farmers eligible to file for relief under Chapter 12 of the Bankruptcy Code.

## A. SMALL BUSINESS REORGANIZATION ACT OF 2019

The SBRA arguably contains the most drastic changes to current bankruptcy practice. The SBRA will go into effect in February 2020 and creates a new subchapter V under Chapter 11 of the Bankruptcy Code.<sup>402</sup> The Act is designed to streamline bankruptcy procedures and increase the success of small business reorganizations by making the process quicker and less expensive.<sup>403</sup>

There are some key provisions of the SBRA that are important to highlight. First, only debtors with non-contingent, liquidated debts totaling not more than \$2,725,625.00 may opt for relief under subchapter V.<sup>404</sup> Second, the SBRA provides for the appointment of a standing trustee for a small business's bankruptcy estate.<sup>405</sup> Like a Chapter 13 trustee, the trustee in a case under subchapter V shall perform a number of duties, such as "ensur[ing] that the debtor commences making timely payments required by a plan confirmed under this subchapter."<sup>406</sup> In addition, the trustee is responsible for "appear[ing] and be[ing] heard at [a] status conference" concerning the value of property subject to a lien, plan confirmation, plan modification, and sale of estate property.<sup>407</sup> Notably, the trustee is to also "facilitate the development of a consensual plan of reorganization."<sup>408</sup>

Third, the plan process is designed to be more streamlined under the SBRA. On this point, only the debtor can propose a plan of reorganization, and the debtor need not submit a disclosure statement or even so-

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402. See Small Business Reorganization Act of 2019, 116 P.L. 54, 2019, Enacted H.R. 3311, 116 Enacted H.R. 3311, 133 Stat. 1079.

403. See *id.*

404. *Id.* (to be codified at 11 U.S.C. § 101(51D)(A)) (The statutory cap was raised to \$7.5 million as part of the CARES Act passed in response to the COVID-19 health crisis. As of the time that this article was edited, the cap will return to \$2,725,625.00 after one year).

405. See *id.* (to be codified at 11 U.S.C. § 1183(a)).

406. *Id.* (to be codified at 11 U.S.C. § 1183(b)(4)).

407. *Id.* (to be codified at 11 U.S.C. § 1183(b)(3)). Further, section 1188(a) provides that a bankruptcy court shall hold a status conference not later than sixty days after the entry of the order for relief "to further the expeditious and economical resolution of a case under this subchapter." *Id.* (to be codified at 11 U.S.C. § 1188(a)).

408. *Id.* (to be codified at 11 U.S.C. § 1183(b)(7)).

licit votes to confirm a plan.<sup>409</sup> A plan is confirmed so long as it “does not discriminate unfairly, and is fair and equitable,” with respect to non-consenting, impaired creditor classes under the plan.<sup>410</sup> The debtor must, however, file its plan within ninety days of the petition date.<sup>411</sup> The plan length must be at least three years and no more than five years, and all disposable income is dedicated to the plan.<sup>412</sup> Further, a creditors’ committee is not appointed, “[u]nless the court for cause orders otherwise.”<sup>413</sup> And a debtor may now modify the rights of a secured lender with a lien on a principal residence, “if the new value received in connection with the granting of the security interest was not used primarily to acquire the real property; and used primarily in connection with the small business of the debtor.”<sup>414</sup>

Fourth, a discharge is not granted to a debtor under subchapter V until the debtor completes all plan payments.<sup>415</sup> The discharge applies to all debts addressed by the plan except for any debt “on which the last payment is due after the first 3 years of the plan, or such other time not to exceed 5 years . . .” or debts that are otherwise nondischargeable under Section 523(a).<sup>416</sup> Last, the SBRA removes the requirement that a debtor pay administrative expenses on the effective date of the plan.<sup>417</sup> A debtor under subchapter V may now stretch out the payment of administrative expense claims over the life of the plan.<sup>418</sup>

The SBRA has implemented some important changes to current small business Chapter 11 bankruptcy practice. At first blush, the Act serves as a hybrid between Chapter 11 and Chapter 13 procedures. While the SBRA does not raise the debt limit for small business debtors, it seems likely that Congress is testing whether the Act is truly successful for a smaller pool of debtors who qualify before considering a debt limit raise. Until then, bankruptcy practitioners should hope that the SBRA provides some meaningful relief to small business debtors.

#### B. HONORING AMERICAN VETERANS IN EXTREME NEED ACT OF 2019

The HAVEN Act revises Section 101(10A) of the Bankruptcy Code to exclude from the definition of current monthly income:

any monthly compensation, pension, pay, annuity, or allowance paid under title 10, 37, or 38 in connection with a disability, combat-related injury or disability, or death of a member of the uniformed

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409. *Id.* (to be codified at 11 U.S.C. § 1189(a)).

410. *Id.* (to be codified at 11 U.S.C. § 1191(b)).

411. *Id.* (to be codified at 11 U.S.C. § 1189(b)).

412. *Id.* (to be codified at 11 U.S.C. § 1191(c)(2)(A)).

413. *Id.* (to be codified at 11 U.S.C. § 1181(b)).

414. *Id.* (to be codified at 11 U.S.C. § 1190(3)).

415. *Id.* (to be codified at 11 U.S.C. § 1192).

416. *Id.*

417. *Id.* (to be codified at 11 U.S.C. § 1191(e)).

418. *Id.*

services, except that any retired pay excluded under this subclause shall include retired pay paid under chapter 61 of title 10 only to the extent that such retired pay exceeds the amount of retired pay to which the debtor would otherwise be entitled if retired under any provision of title 10 other than chapter 61 of that title.<sup>419</sup>

Unlike the SBRA, the HAVEN Act became immediately effective when it was signed into law on August 23, 2019.<sup>420</sup> The purpose of the Act is to exclude certain disability and death-related veterans' benefits from the definition of "current monthly income," like the Code's treatment of certain social security benefits, and to expand bankruptcy relief to veterans.<sup>421</sup>

### C. FAMILY FARMER RELIEF ACT OF 2019

Similar to the HAVEN Act, the Family Farmer Relief Act revises another definitional provision of the Bankruptcy Code.<sup>422</sup> Specifically, it amends Section 101(18) of the Bankruptcy Code to raise the debt limit for a "family farmer" from \$3,237,000.00 to \$10,000,000.00.<sup>423</sup> As with the HAVEN Act, this amendment became effective on August 23, 2019, and should hopefully provide some meaningful relief to struggling farmers.

## X. CONCLUSION

This Survey period was an important one for bankruptcy specialists. Courts at all levels addressed a number of challenging bankruptcy issues in areas of jurisdiction, impairment, discharge, contract rejection, equitable mootness, and attorney's fees. The U.S. Supreme Court issued three decisions, one of which addressed the applicability of the FDCPA to non-judicial foreclosures. The other two opinions focused on Bankruptcy Code-specific issues. In *Taggart*, the Supreme Court clarified that good faith does not bar a finding of civil contempt. And in *Mission Product Holdings*, the Supreme Court held that a debtor's rejection of a trademark license under Section 365 amounts to a breach of the license agreement, not rescission. Likewise, the U.S. Court of Appeals for the Fifth Circuit also addressed some interesting topics. *In re Thomas* was a much-anticipated decision, but in it the Fifth Circuit declined to overturn the stringent standard it articulated in *In re Gerhardt* concerning the dischargeability of student loan debt. As with the new amendments to the Bankruptcy Code that became law in 2019, the Fifth Circuit signaled that it will be up to Congress to address the student loan debt crisis. Until then, at least at the bankruptcy court level, this next year will be a year to watch with the SBRA taking effect in February 2020.

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419. See Haven Act, 116 P.L. 52, 2019 Enacted H.R. 2938, 116 Enacted H.R. 2938, 133 Stat. 1076, (to be codified at 11 U.S.C. § 101(10A)(B)(ii)(IV)).

420. See *id.*

421. See *id.*

422. See Family Farmer Relief Act of 2019, 116 P.L. 51, 2019 Enacted H.R. 2336, 116 Enacted H.R. 2336, 133 Stat. 1075.

423. See *id.* (to be codified at 11 U.S.C. § 101(18)).



