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Splits and Confounding Issues Destined for the Supreme Court

NCBJ-Trends in Bankruptcy

Friday, October 9, 2026; 11:30 a.m.

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Supreme Court

This Term

The bankruptcy court's independent duty under Espinosa to question confirmation of a plan is in tension with a new Supreme Court opinion barring courts from raising issues not addressed by the parties.

A Supreme Court Nonbankruptcy Opinion Questions Continuing Validity of *Espinosa*

Without holding oral argument, the Supreme Court granted *certiorari* and issued a *per curiam* opinion reversing the Fourth Circuit and raising the question of whether *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010), remains good law.

The decision handed down by the Supreme Court on May 26 was a nonbankruptcy case, *Margolin v. National Association of Immigration Judges*. The Court held that the Fourth Circuit had violated the "party presentation principle" by reversing and remanding "based on an issue the parties had not raised."

Margolin creates tension with *Espinosa* because the Court instructed bankruptcy courts in 2010 to make "an independent determination" on whether a chapter 13 plan was confirmable, "even if the creditor fails to object or appear." *Espinosa*, *supra*, 559 U.S. at 278.

Margolin will require bankruptcy courts to walk a tightrope. In reviewing the propriety of requested relief, how far outside the pleadings may the court go to reach a result authorized by the Bankruptcy Code? Must the bankruptcy court always require further briefing when the court is inclined to rule on an issue not raised by the parties? May the court even ask for further briefing or must it rule on the issues as raised by the parties?

Was the Court issuing *dicta* in *Espinosa* by requiring the court to conduct "an independent determination"? Whether *dicta* or not, courts will be loath to disregard *Espinosa*. After *Margolin*, will *Espinosa* be narrowly construed, often distinguished and applied only to confirmation?

Margolin is suited for ordinary litigation where parties are well represented. However, *Margolin* creates burdens on bankruptcy judges and appellate courts when parties are *pro se* or the issues are not well briefed.

The Facts in *Margolin*

The Executive Office for Immigration Review establishes policies for immigration courts. When the Executive Office issued a rule requiring immigration judges to obtain approval for public speeches, the National Association of Immigration Judges filed suit, asserting violations of First and Fifth Amendment rights.

The district court dismissed the suit, ruling that federal employees must bring work-related grievances to the Merit Systems Protection Board. The judges' association appealed.

The Fourth Circuit vacated and remanded, based on an issue that had not been raised or briefed by the parties.

The *per curiam* Supreme Court faulted the Fourth Circuit for having violated the "party presentation principle," which stands for the rule that "'points not argued will not be considered,'" quoting a concurrence by Justice Antonin Scalia. The court went on to say that "we rely on the parties to 'frame the issues for decision' and decide 'only the questions presented.'"

Quoting the dissent in the Fourth Circuit, the Court said, "The Fourth Circuit violated the party presentation principle when it decided 'a case different from the one [respondent] advanced.'" The decision could also be read to mean that the appeals court also erred by remanding the suit for the district court to consider the broader issue that the Fourth Circuit had raised *sua sponte*.

The Court reversed and remanded "for further proceedings consistent with this opinion."

Joined by Justice Amy Coney Barrett, Justice Clarence Thomas concurred, explaining why, in his view, the circuit was also wrong on the merits.

Espinosa

Espinosa was a chapter 13 case with student loans. Without mounting an adversary proceeding under Section 523(a)(8) for a declaration that the student loans created an "undue hardship," the debtor filed and confirmed a plan where the student loans would be discharge after the principal was paid, but without interest.

The holder of the student loans had notice of the plan but did not object nor appeal confirmation.

After the principal on the student loans was repaid, the lender attempted to collect unpaid interest. The debtor responded by moving in bankruptcy court to enforce discharge and enjoin the lender from attempting to collect interest.

The bankruptcy court ruled in favor of the debtor, but the district court reversed, believing that the lender was denied due process because there had been no adversary proceeding. The Ninth

Circuit reversed the district court, holding that any legal error was not grounds for setting aside a final confirmation order under Rule 60(b).

For the unanimous Court on the lender's next appeal, Justice Clarence Thomas held that the bankruptcy court's failure to follow a procedural rule did not rise to the level of a constitutional violation and did not entitle the lender to relief under Rule 60(b)(4) for a void judgment.

"Although the Bankruptcy Court's failure to find undue hardship was a legal error," Justice Thomas held that "the confirmation order is enforceable and binding on [the lender] because it had actual notice of the error and failed to object or timely appeal." *Espinosa, supra*, 559 U.S. at 275.

Justice Thomas was not finished. After the Ninth Circuit had rejected the lender's appeal based on Rule 60(b), he recited how the appeals court went on to rule that a bankruptcy court must confirm a plan discharging student loans absent lender objection, even when the court has made no ruling on undue hardship.

Justice Thomas disagreed with the Ninth Circuit, saying,

> [T]he Code makes plain that bankruptcy courts have the authority — indeed, the obligation — to direct a debtor to conform his plan to the requirements of § 1328(a)(2) and 523(a)(8). . . . [T]he bankruptcy court must make an independent determination of undue hardship before a plan is confirmed, even if the creditor fails to object or appear in the adversary proceeding.

Justice Thomas upheld the judgment of the Ninth Circuit.

Observations

When does *Espinosa's* duty of "independent determination" end and *Margolin's* "party presentation principle" begin? Does *Espinosa* only apply to confirmation or any time a bankruptcy court rules, even in contested matters? Does *Margolin* only bar courts from granting relief no one requested while *Espinosa* allows courts to deny relief on grounds no one sought?

What about this? The bankruptcy court has a chapter 13 plan with a question in the judge's mind about best interests, but no one has objected. Should the court confirm the plan for lack of objection or call for more briefing? If the judge confirms the plan, has the judge violated *Espinosa*? But if the court denies confirmation, has the court violated *Margolin*? Is a call for further briefing a violation of *Margolin*?

If the court is inclined to rule on an issue not raised by the parties, *Margolin* could mean that the court must somehow notify the parties before making a *sua sponte* ruling. Still, *Margolin* might mean that a party's failure to raise an issue is "tough luck" and the court must rule only on the issues presented. In other words, does the court commit prejudicial error by even raising an issue not briefed by the parties? Must the parties sink or swim on their own?

The opinion is *Margolin v. National Association of Immigration Judges*, 25-767 (Sup. Ct. May 26, 2026).

The opinion by Justice Alito says that a violation of due process in entry of a judgment does mean there's no time limit for moving to set aside a judgment under Rule 60(b)(4).

Supreme Court Holds Void Judgments Must Be Attacked Within a 'Reasonable Time'

Resolving a split of circuits and disagreeing with the leading treatise on federal procedure, the Supreme Court ruled today that a motion under Rule 60(b)(4) to set aside a default judgment for lack of personal jurisdiction must be made within a "reasonable time."

Although the petitioner had not raised due process as grounds for voiding the judgment, Justice Samuel A. Alito, Jr. held for the Court in his January 20 opinion that a due process violation would not set aside a void judgment unless the due process argument was raised within a "reasonable time."

It could now be said that the constitutional guarantee of due process can be overcome by a federal rule of procedure. In other words, a judgment that's "void" will become valid unless a motion under Rule 60(b)(4) is made within a "reasonable time."

Justice Alito did not attempt to define "reasonable time," because the petitioner did not raise the issue.

The Allegedly Void Judgment

A chapter 11 debtor filed an adversary proceeding to recover some $50,000 in unpaid invoices. When the defendant failed to answer the complaint, the bankruptcy court entered a default judgment.

After the case converted to chapter 7, the trustee attempted to collect the judgment over the next six years. Among the attempts was a demand letter sent by the trustee to the defendant's chief executive about a year after the judgment had been entered.

Five years after entry of the default judgment, the chapter 7 trustee attached the defendant's bank account. Six years after the entry of judgment, the defendant moved under Bankruptcy Rule 9024 and Federal Rule 60(b)(4) to set aside the judgment. The defendant contended that the judgment was void, allegedly because the debtor had not properly served the summons and complaint.

The bankruptcy court never reached the question of whether the judgment was void for insufficiency of service of process. The bankruptcy court denied the motion to void the judgment on the grounds that the delay in filing the Rule 60(b)(4) motion was unreasonable.

The defendant appealed, but the district court affirmed, and so did the Sixth Circuit, over a dissent. *Burton v. Coney Island Auto Parts Unlimited Inc. (In re Vista-Pro Automotive LLC)*, 109 F.4th 438 (6th Cir. July 26, 2024). To read ABI's report on the Sixth Circuit decision, click here.

The defendant filed a petition for *certiorari*, which the Court granted in June. To read ABI's story, click here. To read ABI's story about oral argument on November 4, click here.

The Applicable Rules

The outcome turned on the Court's interpretation of Rules 60(b)(4) and 60(c). As Justice Alito said,

> Federal Rule of Civil Procedure 60 permits a court to "relieve a party . . . from a final judgment, order, or proceeding," and subdivision (b)(4) specifically authorizes a court to grant relief from a "void" judgment.

Justice Alito went on to say,

> Rule 60 also imposes a time limit for such motions. Rule 60(c)(1) provides that a "motion under Rule 60(b) must be made within a reasonable time."

Justice Alito then held,

> Because a motion for relief from an allegedly void judgment is a "motion under Rule 60(b)," the reasonable-time limit applies.

The Rule's Plain Language Prevails

Referring to the *Wright, Miller & Kane* treatise, Justice Alito said that "several Courts of Appeals[] and a prominent treatise nonetheless maintain that Rule 60(c)(1)'s reasonable-time limit does not apply to motions alleging voidness." He went on to say that "[t]hese authorities acknowledge that their interpretation clashes with Rule 60's text."

While courts finding no time limit "rely[] on the generally accepted maxim that a 'void judgment is a legal nullity,'" Justice Alito said that those courts believe "that the passage of time cannot turn such a nullity into an enforceable judgment."

Justice Alito said that the argument for no time limit regarding void judgments "cannot bear the weight that [the defendant] and others have placed on it." He went on to say that the defendant "would need to show that some principle of law, such as the Due Process Clause, gives a party the right to allege voidness at any time," because "statutes and rules routinely limit the time during which a party can seek relief from a judgment infected by error."

However, the defendant did not advance a due process argument. Furthermore, "we cannot divine any principle requiring courts to keep their doors perpetually open to allegations of voidness," Justice Alito said.

Justice Alito gave examples explaining why a due process denial should not mean there's no time limit. "[I]f a federal district court erroneously concluded that it possessed subject-matter jurisdiction and proceeded to enter a judgment," he said that "the adversely affected party could wait as long as it wanted before filing a notice of appeal."

"It is hard to accept the proposition that due process requires" having no time limit, Justice Alito said.

Although Justice Alito did not attempt to define "reasonable time," he did say that "it might be reasonable for a defendant not to seek relief before learning about a plaintiff 's attempted enforcement."

Justice Alito ended his opinion by holding that a litigant "seeking relief under Rule 60(b)(4) must comply with Rule 60(c)(1) and file a motion within a reasonable time." Because the defendant had not argued that it acted within a reasonable time, he said that "we need not expound on whether Coney Island's timing was reasonable."

Justice Sotomayor's Concurrence

Not joining the other justices in the opinion of the Court, Justice Sonia Sotomayor concurred in the judgment. She said,

> The Court today rightly holds that a Rule 60(b)(4) motion to set aside a default judgment that is void for lack of personal jurisdiction must be made "within a reasonable time." . . . . Rule 60's text and structure require that conclusion, as the majority explains.

Justice Sotomayor stopped short of adopting the majority's belief that a lack of due process will not avoid the "reasonable time" limitation. She observed that the defendant "did not make this argument below and the Sixth Circuit did not pass upon it." She said,

> This Court does "not generally entertain arguments that were not raised below and are not advanced in this Court by any party." *Burwell v. Hobby Lobby Stores, Inc.*, 573 U.S. 682, 721 (2014). There is no reason to depart from that practice absent unusual circumstances, which certainly are not present here.

In his footnote 3, Justice Alito addressed Justice Sotomayor's concurrence, which he characterized as "contend[ing] that we should abstain from addressing any potential due-process considerations." He said that "the only possible basis for" believing that a due process violation overcomes a time limitation "is a rule of constitutional law that prevents the imposition of the Rule's reasonable-time requirement."

Observation

The majority opinion could be read to mean that "reasonable time" begins to run when the defendant is told about the entry of the allegedly void judgment, given how Justice Alito alluded to the fact that the defendant's CEO had been told in writing about the judgment one year after entry.

Questions

Are the majority's statements about due process *dicta* or holding?

Does the majority's opinion imply that constitutional principles will be applied less rigorously to the federal rules?

The opinion is *Coney Island Auto Parts Unlimited Inc. v. Burton*, 24-808 (Sup. Ct. Jan. 20, 2026).

The justices all left the door open for arguments on remand that selling a $175,000 property to collect $2,250 in taxes harbored constitutional violations.

Tax Foreclosures Are Not Required to Realize Fair Market Value, Supreme Court Rules

In real estate tax foreclosures, the Supreme Court held today in *Pung v. Isabella County* that the Takings Clause in the Fifth Amendment does not require the government to sell the property for fair market value. In his holding for the Court, Justice Samuel A. Alito, Jr., said,

> The baseline for measuring just compensation in the tax-sale context is therefore the sale price, not the property's hypothetical fair market value, at least when the sale is fairly conducted in light of our country's history of tax sales.

Joined by Justice Neil M. Gorsuch, Justice Clarence Thomas wrote a concurrence that reads like a dissent. He believes that what the county did was "wrong, and, on my initial view, likely unconstitutional." Because the county was collecting a "small tax debt" of some $2,250, he was of the view that the county should have attached a bank account or personal property, not a home worth around $175,000.

In one paragraph, Justice Sonia Sotomayor concurred, joined by Justices Gorsuch and Ketanji Brown Jackson. She believes that the Court properly remanded to "identify[] the contours of a fair auction."

Tax Sale for a Fraction of Market Value

The Court didn't simply affirm the Sixth Circuit because the facts of the case were disturbing.

The debtor owned a home with an assessed value of $194,000. The county foreclosed the home to recover about $2,250 in one year's unpaid real estate taxes. At foreclosure, the purchaser bought the property for $70,000.

The county paid the homeowner about $68,000, representing the difference between the taxes owing and the price paid at foreclosure. One year after buying the property, the purchaser sold the property for $195,000.

Further complicating the perceived equitable shortcomings of the foreclosure, a state administrative law judge had held that real estate taxes were not owing on the property. However, the county foreclosed for a tax year to which the ALJ's decision did not apply.

In the homeowner's challenge to the foreclosure sale, the district court and the Sixth Circuit only considered the question of whether the homeowner had received the difference between the outstanding taxes and the $70,000 paid at foreclosure. The lower courts believed that no other facts were pertinent to the propriety of the foreclosure.

The 'Baseline' Is the Auction Price

Justice Alito stated the "first question [as being] whether 'just compensation' following a tax sale is measured by the price that the property fetched at auction or its hypothetical fair market value." In other words, "is the constitutional baseline for 'just compensation' the actual tax-sale price or the price that someone would pay for the property in a hypothetical open-market transaction?"

Since the Magna Carta, Justice Alito said that governments have seized property from delinquent taxpayers. "Federal statutes from the early days of the Republic," he said, "required the Federal Government to return to the former property owner any surplus proceeds from a tax sale." Later state and federal statutes "continued to require the Government to refund only the 'surplus of the proceeds of the sale, after satisfying the tax, costs, and charges.'"

In 1884, Justice Alito cited the Supreme Court for holding that taking the surplus away from the property owner would violate the Fifth Amendment. He quoted *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 545 (1994), for interpreting "the Bankruptcy Code to allow foreclosure sales for any 'price in fact received at the foreclosure sale, so long as all the requirements of the State's foreclosure law have been complied with.'" [Note: *BFP* dealt with a regularly conducted mortgage foreclosure.]

Justice Alito read *BFP* as "reject[ing] any suggestion that the owner of a foreclosed property is entitled to recover the fair market value of that property. *Id*., at 538–539." He therefore held that the "baseline for measuring just compensation in the tax-sale context is therefore the sale price, not the property's hypothetical fair market value, at least when the sale is fairly conducted in light of our country's history of tax sales."

History and Precedent

"Neither history nor precedent supports [the debtor's] contrary argument," Justice Alito said. He distinguished cases from state courts and eminent domain cases where "fair market value is the default measure of 'just compensation.'" Unlike eminent domain, Justice Alito said that owners can avoid foreclosure by refinancing or selling the property. Tax sales, on the other hand, "are designed to collect unpaid taxes without undue delay and administrative expense."

Justice Alito said that the debtor's "fair-market-value theory would impose unprecedented burdens on jurisdictions that wish to collect unpaid taxes and might well make tax sales impractical" and "would often produce a net loss," rendering tax sales "infeasible."

"Tax sales," Justice Alito said, "have been an accepted means for governments to collect debts since the earliest days of our Nation."

Troubling Questions Undecided

Justice Alito pointed to contested facts requiring remand, not outright affirmance:

> For one thing, [the debtor] claims that the County seized more property than necessary to satisfy his tax debt. Instead of selling his house, he argues that the County should have seized his money or placed a lien on his property . . . . We will not resolve any of [the debtor's] newfound procedural arguments. On remand, the Sixth Circuit may decide whether they were properly preserved in that court, and, if they were, may entertain [the debtor's] arguments.

No Eighth Amendment Violation

The debtor also challenged the seizure of his property as a violation of the Eighth Amendment's Excessive Fines Clause.

On one page, Justice Alito said that the debtor did "not offer any additional historical evidence suggesting that a tax sale which is fairly conducted in light of our Nation's history would violate the Eighth Amendment." He vacated the judgment of the Sixth Circuit and "remanded for further proceedings consistent with this opinion."

Concurrence #1

Joined by Justices Gorsuch and Jackson, Justice Sotomayor wrote a one-paragraph concurrence.

Justice Sotomayor said that the Court "rightly" rejected the idea that the Takings Clause requires "hypothetical fair market value." She did "not read the Court's opinion as identifying the contours of a fair auction . . . . The Court correctly leaves those issues for remand, should the Sixth Circuit find them preserved."

Concurrence #2 (Dissent?)

In an opinion two pages longer than the Court's opinion, Justice Thomas wrote a concurrence that reads like a dissent. He was joined by Justice Gorsuch and wrote his "preliminary view of the proper resolution of the [debtor's] claims."

Laying out several hundred years of history, Justice Thomas cited *Tyler v. Hennepin County*, 598 U.S. 631, 647 (2023), in saying that "all agree that the government took the [debtor's] property and therefore owed the [debtor] just compensation." He continued, "Just compensation generally requires paying fair market value. Regardless of when exactly the history of tax foreclosure sales can justify a departure from that rule, my initial impression is that it cannot do so in this case."

Although the debtor did not receive fair market value, Justice Thomas said that the Sixth Circuit "reasoned" that the debtor "nonetheless received fair market value because a property is worth less when it is foreclosed upon." The argument, he said, "is mistaken." He explained,

> Because the foreclosure itself does not affect "elements of value that inhere in the property" — such as the land or the building — it cannot affect fair market value in the relevant sense. Likewise, the County may regret its taking and want to avoid losing money, but this Court's precedents also reject the notion that just compensation can take account of the County's interests or its desire to avoid losing money. "It is the owner's loss, not the taker's gain, which is the measure of the value of the property taken." [Citations omitted.]

Justice Thomas said that there are only two exceptions to the rule that just compensation requires fair market value, that neither applied and that the debtor wanted a new exception for tax foreclosures. He "agree[d] that sufficient historical evidence can justify an exception to the fair-market-value rule, and I join the Court's opinion on that basis."

Nonetheless, Justice Thomas said that "any exception based on history can be no broader than what that history justifies. And, on my initial view, any history of tax foreclosure sales reflects a greater respect for principles of just compensation than the County showed the [debtor] here."

Justice Thomas identified two limits on selling a home to pay a "small tax debt." First, the government must try to sell personal property. He quoted a 19th century treatise, saying, "'The power [to sell land] exists only where there are no goods.'" Second, "the government had to pursue only part of the property first" before foreclosing on the entire property.

In the case before the Court, Justice Thomas said that the county's "actions here seem to have departed from that history and tradition." Therefore, he said, "these issues should remain open on remand."

Justice Thomas ended his opinion by rejecting the county's contention that it must be able to collect taxes efficiently. In his view, "the Takings Clause . . . necessarily prioritizes homeowners' property rights over the government's interest in efficiency and public necessity."

In his view, Justice Thomas said that what the county "did to the [debtor] was wrong, and, on my initial view, likely unconstitutional," because the "government exists to protect property; property does not exist to support the government."

Justice Gorsuch joined Justice Thomas's concurrence except for footnote 1. In that footnote, Justice Thomas said he agreed with the Court's opinion, but not the portion saying that the county's foreclosure was in accord with history and tradition. In the footnote, Justice Thomas said,

> I agree that the auction surplus from a tax foreclosure sale can constitute just compensation if it is consistent with historical practice, and because I agree that the parties should have the opportunity to litigate below whether the local government's conduct here was consistent with that practice.

Observations

Remand is a signal that a tax foreclosure does not obviate the possibility that a federal court will find a Takings Clause violation somewhere in the process. All three opinions invite property owners to challenge every step of the process, more so when the amount of the tax is small compared to the property's market value.

The Court's opinion referred to *BFP* as though it applied to all foreclosures, but *BFP* only dealt with regularly conducted mortgage foreclosures. Bankruptcy courts have sometimes found the limitation in *BFP*'s holding to mean that a tax foreclosure can be a fraudulent transfer. Today's citation to *BFP* may be read to mean that tax foreclosures may not be attacked as fraudulent transfers unless there are constitutional flaws in the process.

The opinion is *Pung v. Isabella County*, 25-95 (Sup. Ct. June 23, 2026).

Dissenters argue for overruling Rooker-Feldman while the majority says the issue was not before the Court.

Supreme Court Rules 5/4 that *Rooker-Feldman* Applies to Judgments that Aren't Final

Rooker-Feldman arises habitually in bankruptcy cases. For example, the doctrine can prevent a debtor from asking the bankruptcy court to reach a conclusion at odds with a decision from a state court. Unlike issue preclusion, *Rooker-Feldman* is jurisdictional, so the bankruptcy court must establish its jurisdiction, whether or not the parties raise the question.

Resolving a split of circuits and answering a nagging question, the Supreme Court decided 5/4 on June 18 in *T.M. v. Univ of Maryland Medical System Corp.* that *Rooker-Feldman* eradicates a federal court's subject matter jurisdiction whenever there is a judgment from a state court, even if the judgment is *not* final.

Founded on the notion that the Supreme Court alone has appellate jurisdiction from decisions in state court, Justice Sonia Sotomayor said in her opinion for the majority that "federal district courts lack jurisdiction over 'cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments.' *Exxon Mobil Corp. v. Saudi Basic Industries Corp.*, 544 U. S. 280, 284 (2005)."

Liberal and conservative justices were on both sides. Justice Sotomayor wrote the opinion of the Court for herself and four other justices. Concurring with the majority, Justice Clarence Thomas explored 18th and early 19th century jurisprudence to justify the foundations for *Rooker-Feldman*.

Joined in dissent by Chief Justice John G. Roberts, Jr., and Justices Elena Kagan and Neil M. Gorsuch, Justice Amy Coney Barrett argued that the Court should overrule *Rooker-Feldman*.

As the dissenters pointed out, the facts of the case before the Court did not match those in *Rooker-Feldman* or *Enron*, where the decisions in state court were already final. Arguably, therefore, the new decision is an extension of *Rooker-Feldman*, because the new decision applies *Rooker-Feldman* to judgments that are not final. However, the majority were of the view that the new decision in *T.M.* was "within the narrow doctrine's limits" as they already exist.

As to whether *Rooker* and *Feldman* were wrongly decided, Justice Sotomayor did not reach the question, saying for the majority that the "issue [was] not fairly included in the question presented and was not pressed at the *certiorari* stage."

Same Relief Sought in Two Courts

A woman had been committed to a psychiatric facility against her will and placed on medication against her will. In state court, she filed a petition for judicial review of her commitment.

Her first counsel negotiated a consent order in state court where she was released on conditions, among others, that she obtain a new psychiatrist and take prescribed medications. Ten days later, though, she obtained new counsel and filed a *habeas* petition in federal district court based on the idea that she was deprived of her constitutional rights.

In state court, she appealed from the consent order allowing her release. The appeal in state court was put on ice pending the outcome of her suit in federal court. The district judge raised *Rooker-Feldman sua sponte* and dismissed the federal action for lack of subject matter jurisdiction, based on the idea that she was trying to overturn the non-final state court judgment.

After the Fourth Circuit affirmed dismissal, the Supreme Court granted *certiorari* to resolve a circuit split on whether *Rooker-Feldman* only applies to final judgments from state court. The Fourth and Sixth Circuits have taken the position that the doctrine applies whether or not the judgment is final. Justice Sotomayor described the First, Second, Third, Ninth, Tenth and Eleventh Circuits as declining to invoke the doctrine until the litigation in state court has "ended."

Two Principles Supporting *Rooker-Feldman*

The doctrine was named for two Supreme Court cases: *Rooker*, decided in 1923, and *Feldman*, from 1983. In *Rooker*, the judgment had been upheld in the state supreme court.

Justice Sotomayor described *Rooker* as holding that federal courts, as courts of original jurisdiction under 28 U.S.C. § 1331, lack jurisdiction to review decisions from state courts. Rather, *Rooker* said that only the Supreme Court has appellate jurisdiction over final decisions from state supreme courts under 28 U.S.C. § 1257(a).

Sixty years later in *Feldman*, the Supreme Court held there was no jurisdiction for a district court to review a decision by the highest court in the District of Columbia.

Citing *Exxon*, Justice Sotomayor said that the doctrine is based on two principles. First, federal courts are courts of original jurisdiction and may not exercise appellate jurisdiction over state judgments. Second, appellate jurisdiction over state judgments is lodged exclusively in the U.S. Supreme Court.

Quoting *Exxon*, Justice Sotomayor said that the case at hand "falls within 'the narrow ground occupied by *Rooker-Feldman*'" because the woman was "plainly" seeking review of the state consent order.

No Room for a 'New' Rule on *Rooker-Feldman*

Rather than confront the doctrine's applicability, Justice Sotomayor said that the woman wanted the Court to add a "new rule" that *Rooker-Feldman* only applies to final judgments. She declined to adopt the new rule because it would be "inconsistent with the Court's precedents, risks producing anomalous results, and undermines federalism interests."

The proposed theory, Justice Sotomayor said, "cannot be squared with this Court's precedents, which plainly adopted a different, more functional view of original and appellate jurisdiction." In *Rooker*, she found "nothing in this Court's reasoning suggest[ing] that the outcome would have been different had the judgment still been on appeal."

Citing *Exxon* for the idea that federal courts don't have appellate jurisdiction, Justice Sotomayor said, "None of these cases suggests that district courts have jurisdiction to review state-court judgments, and declare them void, so long as the judgments are not yet within this Court's §1257 jurisdiction." In fact, she said, "*Feldman* explicitly rejected that notion."

"If more is necessary," Justice Sotomayor said, "[T]he Court also declines to distort the *Rooker-Feldman* doctrine in service of a rule that would create anomalous outcomes and undermine the federalism principles upon which the doctrine rests." Allowing federal courts to review state court judgments while they are on appeal, she said, "would undermine the '[c]ooperation and comity' on which our federal system is built." She added,

> Such a rule would only encourage parties to file earlier in federal court, duplicating their efforts even though the state process may well resolve the dispute in their favor.

On the last page of her opinion, Justice Sotomayor said that "the animating force behind many of [the petitioner's] and the dissent's arguments appears to be the belief that *Rooker* and *Feldman* were wrongly decided and so should be cabined whenever possible, if not outright overruled." The issue, she said, "is not fairly included in the question presented and was not pressed at the *certiorari* stage."

Affirming the Fourth Circuit, Justice Sotomayor said that the decision "neither expands nor constrains *Rooker-Feldman*."

The Concurrence

Concurring with Justice Sotomayor's 18-page opinion, Justice Thomas wrote 14 pages concurring "in full" with the majority while explaining the historical underpinnings of *Rooker-Feldman*. Surveying cases and commentators from the 18th and early 19th centuries, his opinion reads like a brief if the Supreme Court ever grants *certiorari* to question *Rooker-Feldman* outright.

Justice Thomas credited the "Founders" for having "accepted this straightforward account of appellate jurisdiction without reservation," and he saw Congress as having "never purported to give inferior federal courts general revising power over state-court judgments for errors of federal law" and for "giving them only original jurisdiction in federal-question cases." He joined the majority in full.

The Dissent

Penning the opinion for the four dissenters, Justice Barrett quoted *Exxon* and said that the Court "emphasized [that] the federal action was brought 'after the state proceedings ended.'" She added "that seven Courts of Appeals took us at our word, refusing to apply *Rooker-Feldman* when the underlying state action remained pending."

Justice Barrett "respectfully" dissented because those seven courts "were right to hold the line." "Because *Rooker-Feldman* stands on shaky ground," she said that the Court has "consciously kept its footprint small."

The primary justification for the rule, Justice Barrett said, is "a negative inference from 28 U.S.C. §1257: Because Congress gave this [Supreme] Court appellate jurisdiction over certain state-court judgments, district courts must lack original jurisdiction to entertain a collateral attack against those judgments." In her view, however, "[a] collateral attack is not functionally equivalent to an appeal." Reliance on Section 1331, she said, "adds nothing."

Justice Barrett saw *Rooker-Feldman* as being "in tension" with parts of the U.S. Code, for instance, the grant of original jurisdiction over "all civil actions" presenting a federal question. She also saw the doctrine as in conflict with the Full Faith and Credit Act. She did not see what the doctrine "brings to the table" because "[p]reclusion already bars parties from relitigating issues and claims that were decided in state court."

"Faithfully read," Justice Barrett saw "*Exxon* [as] requir[ing] us to reject the application of *Rooker-Feldman*." Quoting *Exxon*, she said that "the losing party sued in federal court [in *Rooker* and *Feldman*] 'after the state proceedings ended.'" To her reading, "*Exxon* compels the opposite conclusion," because it only applies to state court judgments and "does not bar district courts from reviewing state court interlocutory orders."

Justice Barrett noted that "federalism" appears in neither *Rooker* nor *Feldman* and that the state's own rules of preclusion would not have barred a second suit in state court just like the one in federal court. She also found the doctrine "at odds with our abstention doctrines," which are "purposefully" kept "narrow."

For Justice Barrett, the "news it not all bad. Although the Court expands *Rooker-Feldman* beyond *Exxon*'s line, it repeatedly emphasizes that the doctrine is 'narrow.'"

Observations

It only takes four justices to grant *certiorari.* If the issue is presented to the Court, the four dissenters by themselves could grant review to decide whether *Rooker-Feldman* should be overturned. *Rooker-Feldman* would be reversed if only one justice from the majority were to switch sides.

In a sense, the majority opinion is a blessing for bankruptcy judges because the decision maps a shorter route for finding a lack of subject matter jurisdiction and obviates any need for deciding whether a state court decision is final.

But what about this: Federal courts typically follow state court rules on issue preclusion. What if issue preclusion is not applicable to a state court judgment? Must the bankruptcy court nonetheless dismiss under *Rooker-Feldman*? It is possible that the latest iteration of *Rooker-Feldman* might bar suits that issue preclusion would permit.

The majority opinion could cause a race to the courthouse by putting a premium on quickly gaining a nonfinal judgment in state court. And what if a judgment hasn't been entered, only an order on a motion for summary judgment, for example? Does the doctrine apply?

The opinion is *T.M. v. Univ. of Maryland Medical System Corp.*, 25-197 (Sup. Ct. June 18, 2026).

In Keathley, the Supreme Court reversed the Fifth Circuit by holding that 'potential' motive to conceal does not justify application of judicial estoppel.

Supreme Court May Have Killed Judicial Estoppel in Bankruptcy and Everywhere Else

Today, the Supreme Court reversed the Fifth Circuit, holding that the doctrine of judicial estoppel arising from a bankruptcy case should not be applied rigidly or broadly but may be invoked only when the court "look[s] to the totality of the circumstances surrounding the omission."

Significantly, all of the justices "assume[d] without deciding that judicial estoppel can apply in the bankruptcy context." Indeed, the unanimous opinion for the Court and the two concurrences together imply that judicial estoppel is a doctrine having no place at all in federal practice. More narrowly, the opinions more than imply that judicial estoppel is inapplicable in bankruptcy cases.

Assuming there is a rule to preclude a litigant from taking inconsistent positions, the opinions suggest that federal courts should apply the doctrine of equitable estoppel, never judicial estoppel.

This writer reads the opinions to mean that federal courts in any context are walking on thin ice by applying judicial estoppel. The opinions are in line with Supreme Court authority that federal courts may employ only those equitable remedies exercised by the High Court of Chancery in England at the time of the adoption of the Constitution and the enactment of the Judiciary Act in 1789. *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 318 (1999).

The Facts and the Circuit Decision

The debtor filed a chapter 13 petition and confirmed a five-year plan with 100% payment for unsecured creditors, without interest. More than a year after confirmation, the debtor was injured when the truck he was driving collided with another truck. Immediately after the injury, the debtor retained personal injury counsel.

The debtor informed his bankruptcy lawyer about the accident, but bankruptcy counsel did not inform the court or amend the schedules. Later, bankruptcy counsel filed an amended chapter 13 plan but did not disclose the personal injury claim on that occasion, either.

While the chapter 13 case was still proceeding, the debtor filed a personal injury suit in federal district court. The defendant responded with a motion for summary judgment based on judicial estoppel for the debtor's failure to disclose the personal injury claim in bankruptcy court. The debtor then amended his bankruptcy schedules to disclose the claim.

Granting the defendant's summary judgment motion, the district court dismissed the suit, holding that the failure to disclose was not inadvertent. The Fifth Circuit affirmed in a *per curiam*, nonprecedential opinion. *Keathley v. Buddy Ayers Construction Inc.*, 24-60025, 2025 WL 673434 (5th Cir. March 3, 2025). The Fifth Circuit upheld invocation of judicial estoppel because the debtor had potential motive to conceal.

Under its case law, the Fifth Circuit applies judicial estoppel whenever the debtor has a "plausible" motive for failure to disclose a personal injury claim. The Tenth Circuit follows the same rule.

In her opinion for the unanimous court, Justice Ketanji Brown Jackson said that the Fourth, Sixth, Seventh, Ninth and Tenth Circuits "conduct a more fact-specific inquiry and do not so stringently limit the analysis." The Supreme Court granted *certiorari* in October to resolve the circuit split and heard argument on March 24. The question presented was:

> Whether the doctrine of judicial estoppel can be invoked to bar a plaintiff who fails to disclose a civil claim in bankruptcy filings from pursuing that claim simply because there is a potential motive for nondisclosure, regardless of whether there is evidence that the plaintiff in fact acted in bad faith.

The Assumption that Judicial Estoppel Exists as a Valid Doctrine

Citing the Supreme Court's only opinion on judicial estoppel, Justice Jackson said that the doctrine is "intended 'to protect the integrity of the judicial process,' both by 'prohibiting parties from deliberately changing positions according to the exigencies of the moment,' and by preventing the 'risk of inconsistent court determinations.'" *New Hampshire v. Maine*, 532 U. S. 742, 749-51 (2001).

When a debtor has not scheduled a claim but later files a lawsuit, she said that some lower courts "apply judicial estoppel to bar such lawsuits, reasoning that application of the doctrine 'raises the cost of lying' and 'induces debtors to be truthful in their bankruptcy filings.'"

"While this Court has never applied judicial estoppel in the bankruptcy context," Justice Jackson again referenced *New Hampshire*, where, "in a different context[,] we left open whether it 'may be appropriate to resist application of judicial estoppel' when the party's prior inconsistent position was due to 'inadvertence or mistake.'"

Then, Justice Jackson stated an assumption that might lead some readers to believe that the Court will not find judicial estoppel to be a valid federal doctrine should the issue be presented to the Court. She said,

> For purposes of this opinion, we assume without deciding that judicial estoppel can apply in the bankruptcy context and that "inadvertence or mistake" can function as an exception to that application.

'All Relevant Factors'

"Operating under those assumptions," Justice Jackson held, "the Fifth Circuit's understanding of 'inadvertence or mistake' is simultaneously too rigid and too broad," because judicial estoppel is an equitable remedy and equity "'eschews mechanical rules,'" citing Supreme Court precedent. Citing other Court authority, she said that equity requires a court to "act 'on a case-by-case basis,' considering all relevant facts and circumstances."

In other words, the Fifth Circuit's "rigidity is out of step with equity," Justice Jackson said. "[T]he Fifth Circuit instead should have examined the totality of the circumstances surrounding [the debtor's] failure to report his personal-injury claims earlier."

The Fifth Circuit's rule was not only too rigid, it was also too broad, Justice Jackson said, because "a debtor will almost always hypothetically benefit from not revealing such a claim to his creditors."

Finding error, Justice Jackson reversed and remanded, holding that the "Fifth Circuit artificially narrowed its inquiry into whether [the debtor's] bankruptcy-schedule omission was the result of inadvertence or mistake by assessing *only* whether he had knowledge of the underlying facts or a potential motive to conceal his personal-injury suit." [Emphasis in original.]

There were concurrences by justices at both ends of the political spectrum. Combined with the Court's unanimous opinion, the concurrences suggest that judicial estoppel might not withstand scrutiny.

Concurrence by Justices Thomas and Gorsuch

Justice Clarence Thomas wrote a concurrence joined by Justice Neil M. Gorsuch. They joined the opinion by Justice Jackson "in full" but wrote "separately to express doubt about the foundation of the doctrine of judicial estoppel."

"Lower federal courts," Justice Thomas said, "have applied this doctrine broadly without clear authority to do so, and with only limited support from this Court's precedents. In a future case, we should reexamine it."

Having stated his skepticism, Justice Thomas went on to say that judicial estoppel "entered the mainstream in the federal courts only in the past few decades." In 1980, he said that "the D. C. Circuit declined to apply judicial estoppel because it 'ha[d] not been followed by anything approaching a majority of jurisdictions, nor [was] there a discernible modern trend in that direction.'"

Nonetheless, Justice Thomas said that "judicial estoppel has now become commonplace in the Courts of Appeals" and "reaches much further than the older doctrine of 'equitable estoppel,' which requires the party invoking the doctrine to prove that it was itself the object of a previous representation, that it relied on the previous representation, and that it was prejudiced by the change in positions."

In the case on appeal, Justice Thomas observed that "the defendant was relieved of all liability for injuring the plaintiff, regardless of whether his conduct was tortious and regardless of whether he was in any manner affected by the plaintiff 's other proceedings."

Saying that the doctrine "appears" to lack "general equitable authority," Justice Thomas explained why the "foundation" for equitable estoppel "remains questionable."

> It is unclear what gives federal courts the authority to bar suits based on judicial estoppel. Often, . . . federal courts treat judicial estoppel as a matter of federal law and feel free to craft their own standards and extend the doctrine to new contexts. But, the doctrine appears to have no basis in any statute, any Federal Rule of Civil Procedure, or any traditional inherent power of federal courts. Although the doctrine purports to punish litigants to "protect the integrity of the judicial process," the courts of appeals have not justified it as an exercise of the traditional sanctioning power that courts have been held to have in other contexts. [Citations omitted.]

Citing *New Hampshire*, where the "Court has apparently enforced judicial estoppel only a single time," Justice Thomas said that the Court's own "precedents do not justify the current state of [the] judicial-estoppel doctrine." He noted that *New Hampshire* was an original jurisdiction case where "the Court applied the doctrine based on prior litigation between the same two parties. It estopped New Hampshire from adopting a new position after it had taken the opposite position in a previous suit against the same party before the same Court."

Justice Thomas said, "[I]t is difficult to see how application of this doctrine in cases such as this one serves any equitable purpose, or how an interest in 'the integrity of the judicial process' could justify it." He ended his concurrence by saying that "this doctrine merits a closer look" because "[j]udicial estoppel has secured widespread acceptance in the Courts of Appeals without any clear authority in statutes, rules of procedure, or this Court's precedents."

Concurrence by Justice Sotomayor

Where Justices Thomas and Gorsuch questioned the validity of judicial estoppel across the board, Justice Sonia Sotomayor explained why the doctrine makes no sense in bankruptcy cases.

"[A]ssuming judicial estoppel applies in the bankruptcy context," Justice Sotomayor agreed that "the Fifth Circuit's exceedingly narrow test for determining whether an inconsistent position was based on inadvertence or mistake is erroneous." She wrote "to address why it may not ever make sense to apply judicial estoppel when bankruptcy proceedings are pending . . . ."

Justice Sotomayor recognized how "the 'unfair advantage' a dishonest debtor gains by failing to disclose assets comes at the creditors' expense and deprives them of potential recovery." In reality, she said, "the party most likely to benefit is the potential tortfeasor in the separate proceeding: someone who is not prejudiced by the debtor's earlier, inconsistent position, but whom judicial estoppel permits to escape liability."

Had the lawsuit not been dismissed, Justice Sotomayor said that "any judgment [the debtor] received could have been used in turn to pay creditors interest or shorten the repayment period or both." On the other hand, the doctrine gave "the alleged tortfeasor a windfall even though it was not involved in the bankruptcy and thus was neither misled nor impacted by the delayed disclosure."

Justice Sotomayor listed the "more equitable options" that the bankruptcy court could have applied, like imposing sanctions under Rule 11, converting the case to chapter 7, revoking confirmation, denying discharge or referring the matter to the U.S. Attorney for perjury.

When a bankruptcy case remains open, Justice Sotomayor said it is "doubtful that equity ever demands the application of judicial estoppel to a claim asserted by a debtor in a different proceeding, even when that claim relies on a deliberately inconsistent position." She added, however, that "the judicial estoppel calculus may look different if the debtor takes an inconsistent position long after discharge."

The opinion is *Keathley v. Buddy Ayres Construction Inc.*, 25-6 (Sup. Ct. June 11, 2026).

On remand from the Supreme Court, the district judge comes within an inch of deciding that failure to schedule a tort claim as an asset was no ground for dismissal under judicial estoppel.

District Judge Interprets What *Keathley* Means Regarding Judicial Estoppel

At the end of the term, the Supreme Court handed down *Keathley v. Buddy Ayres* to resolve a split of circuits by reversing the Fifth Circuit for dismissing a chapter 13 debtor's tort action because the debtor had not amended his schedules to list the tort suit as an asset.

The Supreme Court remanded, saying that the Fifth Circuit "should have examined the totality of the circumstances surrounding [the debtor's] failure to report his personal-injury claims earlier." *Keathley v. Buddy Ayres Construction Inc.*, 146 S. Ct. 1532, 225 L. Ed. 2d 214, 222 (Sup. Ct. June 11, 2026).

In her opinion for the Court on June 11, Justice Ketanji Brown Jackson said that the "Fifth Circuit artificially narrowed its inquiry into whether [the debtor's] bankruptcy-schedule omission was the result of inadvertence or mistake by assessing *only* whether he had knowledge of the underlying facts or a potential motive to conceal his personal-injury suit." [Emphasis in original.] *Id*. at 223. To read ABI's report, click here.

Today, we report on how District Judge Michael P. Mills of Oxford, Miss., reacted when the lawsuit fell into his lap once again on remand. His opinion is not good news for the defendant in the tort action.

The July 20 opinion by Judge Mills is the first example of what other courts may be reading into *Keathley*.

Bankruptcy in One Circuit; Tort Suit in Another Circuit

A year after confirming his chapter 13 plan in Arkansas, the debtor was injured in an accident with a truck. He immediately informed his bankruptcy counsel about the accident, but the lawyer did not amend the debtor's schedules, perhaps believing there was no requirement to do so. Later, the debtor amended his chapter 13 plan, but the tort claim was not disclosed once again.

After filing a tort action in federal district court in Mississippi, the debtor amended his schedules when the tort defendant filed a motion to dismiss based on judicial estoppel. Reluctantly, Judge Mills dismissed the suit to comport with Fifth Circuit authority requiring dismissal under judicial estoppel if the debtor has a "plausible" motive for failing to disclose.

The Fifth Circuit affirmed dismissal in a *per curiam* opinion. Circuit Judge Catharina Haynes concurred in an opinion that reads like a dissent. She agreed with the result because a three-judge panel had no right to differ from established circuit precedent without sitting *en banc*.

After the Supreme Court's reversal and remand, the Fifth Circuit quickly remanded the case to Judge Mills. The circuit court "express[ed] no view as to what proceedings the district court should conduct on remand or what decisions it should make."

Keathley Had 'Vague Guidelines'

Sua sponte, Judge Mills made "certain observations and set[] case management guidelines following the U.S. Supreme Court's ruling on the judicial estoppel issues in this case." He began by noting how "the Supreme Court 'assum[ed] without deciding' that 'judicial estoppel can apply in the bankruptcy context' and 'that "inadvertence or mistake" can function as an exception to that application.' *Keathley*, 146 S. Ct. at 1539."

Before delving into the details of the case before him, Judge Mills stated his overall view of *Keathley* as follows:

> This court personally believes that the Supreme Court arrived at a reasonable middle ground in this case which permits federal courts to incentivize the timely disclosure of claims in bankruptcy through the application of judicial estoppel, but which tempers the harshness of this approach by requiring the recognition of equitable exceptions in cases of "inadvertence," "mistake" or, most likely, other contexts as well in which equity so requires.

Judge Mills read the Supreme Court's opinion as providing "rather vague guidelines which, it seems likely, will leave the various federal circuits considerable discretion to decide how stringent or lenient an approach they wish to adopt in the judicial estoppel context." He was left "to essentially guess what positions the Fifth Circuit will choose to stake out in this context." It is "more likely," he said, "that the Fifth Circuit will alter its approach only to the extent required by the Supreme Court's ruling in this case."

Judge Mills said it "should be unsurprising" that he "chooses to adopt the reasoning of [the] concurrence [by Circuit Judge Haynes] in deciding how best to proceed on remand."

New Law Applied to the Old Case

In her concurrence, Judge Haynes observed that the bankruptcy was in Arkansas, where the Eighth Circuit "adopted a more lenient approach to judicial estoppel in bankruptcy cases." Judge Mills therefore "conclude[d] that the fact that plaintiff filed for bankruptcy in the much more permissive (in this context) Eighth Circuit makes his failure to timely disclose his claim more excusable than if he had filed for bankruptcy in this circuit."

Judge Mills went on to recognize the realities of bankruptcy practice and the debtor's attorney's nondisclosure.

> Moreover, bankruptcy counsel are generally paid a rather limited fee to perform one particular ask: to file and litigate the bankruptcy. That being the case, it seems to be asking quite a lot of such counsel to not only litigate the bankruptcy issues before them, but to also anticipate and research the impact of the bankruptcy filings upon the litigation of a completely separate tort lawsuit in a different jurisdiction, which lawsuit will generally be handled by a different counsel.

Judge Mills added, "[T]he argument against a district court finding judicial estoppel is even stronger in cases where the bankruptcy case is not only pending in another district, but also in a different judicial circuit." The argument, he said, is "even stronger still when the two circuits in question have adopted starkly different approaches to judicial estoppel in the bankruptcy context, as is the case here."

Also following Judge Haynes, Judge Mills said that the "defendant is essentially seeking a windfall by arguing in favor of judicial estoppel based on representations made in Arkansas bankruptcy proceedings in which it was not a creditor." Therefore, he said "it should be difficult for defendant to summon a sense of righteous indignation that it is (potentially) being held accountable for the negligence of its employees, just like any other civil defendant."

The Conclusion by Judge Mills

Judge Mills saw "very real equitable downsides, and a very real societal price to be paid, for applying judicial estoppel to this case and other cases like it." As a matter of "public policy," he saw the question as whether the failure to disclose "was sufficiently *reprehensible and damaging* to the judicial process that federal courts should be willing to accept the harm which will be caused by punishing the debtor's behavior." [Emphasis added.]

Judge Mills said he "does not believe that it would be equitable and appropriate, under the totality of the circumstances of this case, to accept the harms and downside which would result from applying judicial estoppel here." He saw "multiple potential approaches to rejecting the application of judicial estoppel in this case, and it is strongly inclined to conclude that at least one of them is applicable here."

Nonetheless, Judge Mills stopped short of denying the tort defendant's motion for summary judgment on judicial estoppel. Because the case has been pending since 2021, he directed the case to go forward in discovery as a matter of docket management.

Judge Mills therefore directed "that any renewed summary judgment motion based on judicial estoppel should only be filed after discovery has been completed regarding the tort issues in this case. This will allow the tort and judicial estoppel issues to be addressed in the same order and thereby promote considerations of judicial economy."

Observation

Judge Mills abjured the opportunity for him to discuss the question of whether judicial estoppel has any place in federal practice.

The Court's opinion only assumed that judicial estoppel is a valid doctrine in federal practice. After all, the only Supreme Court cases on judicial estoppel, *New Hampshire v. Maine*, 532 U. S. 742, 749-51 (2001), involved one state suing another under the Supreme Court's original jurisdiction. The contrary position was taken by one state against the other in the very same lawsuit in the Supreme Court.

In a concurrence, Justices Clarence Thomas and Neil M. Gorsuch wrote "separately to express doubt about the foundation of the doctrine of judicial estoppel."

The Court's opinion was far from a ringing endorsement of judicial estoppel, and the concurrence lays out a theory for saying that judicial estoppel has no place in federal practice.

Because the Fifth Circuit was so fervently in favor of judicial estoppel, Judge Mills properly avoided questioning whether the doctrine deserves a dignified funeral.

The opinion is *Keathley v. Buddy Ayres Construction Inc.*, 21- 261 (N.D. Miss. July 20, 2026).

Reorganization

Solvent Companies and Bad Faith

The concurring opinion in Bestwall could be read to suggest that Circuit Judge G. Steven Agee might have an open mind if a confirmed plan comes to the Fourth Circuit on appeal.

Bestwall Concurrence Believes in 'Liberalization' of Bankruptcy Powers

In our previous two reports, we covered *Bestwall's* majority and dissenting opinions. The majority did not see insolvency as a condition to federal bankruptcy jurisdiction under Section 1334. The dissenter believes that the Constitution's Bankruptcy Clause demands insolvency to invoke bankruptcy jurisdiction.

Today, we cover the seven-page concurring opinion by Circuit Judge G. Steven Agee, who refuted the dissent's belief that the 18th century understanding of "bankruptcy" connotes insolvency in modern times.

Judge Agee began by saying that he "completely agree[d]" with the majority's holding that "'federal courts have subject-matter jurisdiction over bankruptcy cases filed by debtors who may be able to pay their obligations.'" He characterized the dissenter, Circuit Judge Robert Bruce King, as believing that "Congress exceeded its authority under the Bankruptcy Clause in crafting Section 1334" to permit filings by solvent entities.

Judge Agee cited the Supreme Court in 1935 as having said that the power of Congress under the Bankruptcy Clause is not limited by English or colonial law in effect at the time of the adoption of the Constitution. *Cont'l Ill. Nat. Bank & Tr. Co. of Chi. v. Chi., Rock Island & P. Ry. Co.*, 294 U.S. 648, 669 (1935). He quoted the Court for having said that "'the tendency of legislation and of judicial interpretation has been uniformly in the direction of progressive liberalization in respect of the operation of the bankruptcy power.'" *Id*. at 668.

More recently, Judge Agee said that the Supreme Court "reiterated that bankruptcy is difficult to define and includes 'nothing less than "the subject of the relations between [a] debtor and his creditors."'" *Siegel v. Fitzgerald*, 596 U.S. 464, 473–74 (2022).

Judge Agee said that the dissenter "fails to identify any historical precedent that — as a *jurisdictional* matter, lest we forget the question presented — applies to support its position." [Emphasis in original.] After 235 years, he thought "there would be at least one case supporting the dissent's vague view; but there are none."

Although chapter 9 requires insolvency, Judge Agee observed that "neither Chapter 7, Chapter 11, nor Chapter 13 includes such a requirement." Given the million cases under chapters 11 and 13 that have been filed in the last five years, he said that "all of these would be unconstitutional and therefore void" if the dissenter's analysis were to prevail.

Judge Agee read the dissent as "simply disagree[ing] with what has colloquially become known as the Texas Two-Step, which it characterizes as 'a corporate sleight-of-hand maneuver.'" He said that "the Texas Two-Step's validity is irrelevant in evaluating whether federal courts have subject-matter jurisdiction over bankruptcy cases filed by debtors who may be able to pay their obligations."

Judge Agee "fully concur[red]" with the majority opinion.

Observation

Among the three opinions, the concurrence by Judge Agee could be read as being most hospitable toward the debtor. Regarding the merits of the Texas Two-Step, he said, "that is a matter within the province of the Congress, not the judiciary."

Was Judge Agee suggesting that a Texas divisional merger gives rise to no offense requiring dismissal and no intentional fraudulent transfer?

In a footnote, he said that "the Committee has filed multiple challenges that have impeded progression to a plan and confirmation hearing." He criticized the committee, "in the eleventh hour," for having moved "to dismiss for lack of subject-matter jurisdiction."

In the same footnote, Judge Agee asked whether delay occasioned by the committee was calculated to raise "valid claims" or reflected a "desire for perceived higher attorneys' fees should the claims be removed and be adjudicated outside of bankruptcy." "Perhaps future review will answer that question," he said.

This writer lauds Judge Agee for not hinting at how he might rule on issues not yet before the court.

The opinion is *Official Committee of Asbestos Claimants of Bestwall LLC v. Bestwall LLC (In re Bestwall LLC)*, 24-1493 (4th Cir. Aug. 1, 2025).

ROCHELLE'S DAILY WIRE

Building on LTL Management (a/k/a Johnson & Johnson), a chapter 11 case was dismissed because the newly formed debtor was designed to rid the larger enterprise of 'toxic' leases for the benefit of equity holders.

Chapter 11 by a Newly Created Debtor Dismissed in Delaware for a Bad Faith Filing

Building on the Third Circuit's landmark decisions in *LTL Management (*a/k/a Johnson & Johnson*)* and *SGL Carbon*, Bankruptcy Judge J. Kate Stickles of Delaware dismissed a chapter 11 case as a bad faith filing when the debtor was created six days before bankruptcy "to take advantage of the provisions of the Bankruptcy Code" by capping lease-rejection damages "for the benefit of its shareholders, not to maximize the value for the Debtor's creditors."

The debtor's parent was formed in 2020 to purchase and lease sites to be used for manufacturing plants or laboratories. The original $2 billion in equity proved insufficient, but alternative financings did not come to pass. When new long-term financing was out of reach by mid-March 2025, the company was left with $100 million in cash, maybe three months of liquidity.

At that point, the company had two options: a chapter 11 reorganization for the entire enterprise, or a divisive merger under Section 18-217 of the Delaware LLC Act. A divisive merger would split the business into two parts, creating a good company and a bad company.

Deciding on a divisive merger, the bad company was given seven "toxic" leases plus $41.4 million in cash and receivables, among other assets. The bad company filed a chapter 11 petition in Delaware six days after formation. At the time, there were no defaults on the leases.

Immediately after filing, the debtor filed a chapter 11 plan where equity holders and all creditors would be unimpaired. There were no secured creditors. The plan would have reinstated equity holdings and paid landlords the full amount of their lease-rejection claims that aggregated about $32 million after being capped under Section 502(b)(6).

The U.S. Trustee and several landlords filed motions to dismiss the case for "cause" as a bad faith filing under Section 1112(b). Judge Stickles granted the dismissal motions for reasons explained in her 42-page opinion on August 29.

Third Circuit Law on Good Faith Filings

Citing and quoting *LTL Mgmt., LLC v. Those Parties Listed on Appendix A to Complaint (In re LTL Mgmt., LLC)*, 64 F.4th 84, 100 (3d Cir. 2023), Judge Stickles said that the "Third Circuit recognizes that a 'lack of good faith' constitutes cause for dismissal of a chapter 11 petition," and that the two factors "relevant to the good faith inquiry [are]: '(1) whether the petition serves a valid bankruptcy purpose' and '(2) whether [the petition] is filed merely to obtain a tactical litigation advantage.'" Of greatest renown, she quoted *LTL*, where the Third Circuit said, "A valid bankruptcy purpose 'assumes the debtor is in financial distress.'" To read ABI's report on *LTL*, click here.

LTL was a development from *Off. Comm. of Unsecured Creditors v. Nucor Corp. (In re SGL Carbon Corp.)*, 200 F.3d 154, 161–62 (3d Cir. 1999), where Judge Stickles cited the Third Circuit for holding that a "valid bankruptcy purpose includes preserving a going concern or maximizing the value of the estate."

Synthesizing *LTL* and *SGL*, Judges Stickles said, "A debtor who is not in financial distress cannot establish that its petition serves a valid bankruptcy purpose supporting good faith."

Newly Created Just for Bankruptcy

The debtor contended there was financial distress because the total lease liability before the cap was $372 million, vastly more than the assets. The debtor also argued that full payment of the capped lease claims would be a better outcome for landlords than a bankruptcy by the entire enterprise.

To the contrary, Judge Stickles found "that although the Debtor may have been allocated greater liabilities than assets, the financial health of the Debtor was not authentic, but rather structured, by design, by the [affiliates and equity holders] in conjunction with the [divisive merger] to facilitate the bankruptcy filing and jettison lease liabilities." More specifically, she found that the "toxic" leases and related guaranties were removed from the nondebtor affiliates and allocated to the debtor for "the benefit of its shareholders[,] not to maximize the value for the Debtor's creditors."

Judge Stickles pointed out that financing for the chapter 11 case was provided by shareholders "to take advantage of the Bankruptcy Code's redistributive provisions." She was unwilling to give "the benefits of the Bankruptcy Code provisions absent [a] bankruptcy filing" by all of the related companies. She therefore held that the "Debtor has failed to establish that this Chapter 11 Case serves a valid bankruptcy purpose."

Because the "Debtor was formed solely to file bankruptcy and rid the Enterprise of liabilities for the benefit of the Enterprise's shareholders," Judge Stickles also concluded that the filing was designed for a "tactical advantage."

Since a bankruptcy by the entire enterprise might entail a worse outcome, the debtor contended that dismissal was improper because Section 1112(b)(2) bars conversion "if the court finds and specifically identifies unusual circumstances establishing that . . . dismissing the case is not in the best interests of creditors and the estate . . . ."

Finding "no unusual circumstance [to] overcome the manufactured financial distress," Judge Stickles granted the motions to dismiss.

Question

Would bankruptcy courts in other circuits reach the same result?

The opinion is *In re Bedmar LLC*, 25-11027 (Bankr. D. Del. Aug. 29, 2025).

Executory Contracts & Leases

The 'lowest point in the zone of reasonableness' brought into question as the standard for approving settlements.

Judge Goldblatt Examines the 'Reasonableness' Standard for Claim Objection Settlements

It's sometimes taken as gospel that the bankruptcy court will approve a settlement if it does not "fall below the lowest point in the zone of reasonableness."

In an opinion that reads like a law review article, Bankruptcy Judge Craig T. Goldblatt of Delaware said he was "rejecting the extreme levels of deference that might be suggested by the 'lowest point in the range of reasonable' language" when the court is being asked to approve the settlement of a claim under objection by a creditor.

We recommend that our readers find time to read all 74 pages of Judge Goldblatt's April 2 opinion.

Proposed Settlements of ERISA Claims

One of the country's largest truckers, Yellow Corp., filed a chapter 11 petition and quickly halted operations. Eventually, the debtor confirmed a liquidating chapter 11 plan.

Halting operations meant that the debtor was withdrawing from no less than 20 multiemployer pension plans. As a consequence of the resulting withdrawal liability, the multiemployer plans filed claims for almost $8 billion in liability arising under the Multiemployer Pension Plan Amendments Act of 1980, as amended under the Employee Retirement Security Act, or ERISA.

The debtor and the pension plans have been litigating the claims for years. Along the road, Judge Goldblatt issued opinions resolving several areas of dispute and developing a methodology for calculating the amounts in which the claims would ultimately be allowed. However, Judge Goldblatt's decisions did not give rise to final orders subject to appeal.

With no final orders, the debtor and the pension plans decided to settle rather than continue years more in litigating and appealing. Suffice it to say that the settlements proposed allowing the claims for more than the amounts indicated by Judge Goldblatt's prior rulings.

Here's the rub: An entity that was both a creditor and an equity holder was objecting to the pension plans' claims and to the proposed settlements. The creditor had standing because a reduction in the claims would increase the creditor's recovery and might even result in a distribution to equity.

Invoking Section 502(b), the creditor took the position that Judge Goldblatt was required to rule on the allowance of the claims and could not approve the settlements. When there is a claim objection outstanding, the subsection provides, in pertinent part, that the court "*shall determine* the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount . . . ." [Emphasis added. Note the word "shall."]

The creditor's objection obliged Judge Goldblatt to decide whether he could even entertain the settlements. If settlements were possible, he needed to decide what standard to apply in approving settlements that were more than what they would be under his prior, nonfinal opinions.

We won't hold you in suspense. Judge Goldblatt approved most of the settlements and constructed an approval standard for application in the case at hand.

Deference, but How Much?

Judge Goldblatt said "that some cases talk about a settlement being just one rung above the very bottom of the ladder of what is reasonable." However, he said it "bears emphasis that the case for deferring to the debtors' 'business judgment' necessarily operates differently in different contexts." He elaborated,

> The paradigmatic articulation of the "business judgment rule" arises when a shareholder seeks to bring a derivative action against a corporate director after some business decision turns out poorly for the corporation, thus reducing the value of the shareholder's investment. In that context, courts are appropriately concerned about discouraging businesses from taking appropriate risks.

"The questions presented to a bankruptcy court are different," Judge Goldblatt said, because "the question is asked in advance, rather than after things have gone sideways." Nonetheless, he said "there are logical reasons why bankruptcy courts in that context have largely drawn on the 'business judgment' principle that comes out of the fiduciary duty caselaw." He noted that judges do not have trained management teams like corporate debtors in chapter 11.

"Accordingly," Judge Goldblatt said, "it is widely accepted that a bankruptcy court reviews the trustee's business judgments deferentially, asking whether there is a 'sound business purpose' or 'good business reason' for the decision."

The Traditional Settlement Standard

Judge Goldblatt described the derivation of the business judgment rule. The genesis, he said, was "*TMT Trailer Ferry*, a pre-Code case [where] the Supreme Court explained that settlements that form the basis for a plan of reorganization must be 'fair and equitable.'"

Then came *In re Martin*, 91 F.3d 389 (3d Cir. 1996), where Judge Goldblatt said that the Third Circuit, "relying on *TMT Trailer Ferry*, found that a bankruptcy court reviewing a trustee's decision to resolve an estate claim should consider '(1) the probability of success in litigation; (2) the likely difficulties in collection; (3) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it; and (4) the paramount interest of the creditors.'"

Subsequently, Judge Goldblatt said that some bankruptcy court decisions "could be read to suggest that so long as any sober debtor could possibly have agreed to a settlement, a bankruptcy court is duty-bound to rubber stamp it," resulting in "some heightened level of extreme deference."

When there is an objection to a proposed claim settlement, Judge Goldblatt surveyed authority and held that the "bankruptcy court is duty bound to give that party a fair hearing and satisfy itself that the trustee has formed a reasoned judgment about what is best for the estate, in light of the factors the Third Circuit identified in *Martin*."

Harmonizing *Martin* and Section 502(b)

To harmonize "the statutory command of § 502(b) with the long history of trustees undertaking to resolve claims allowance disputes as part of their role in managing the bankruptcy estate," Judge Goldblatt said he was "persuaded [by] the approach taken by the court in" *In re DVR LLC*, 582 B.R. 507 (Bankr. D. Colo. 2018)), by retired Bankruptcy Judge Elizabeth E. Brown of Denver.

Judge Brown said that the command in Section 502(b) may not be ignored, but Judge Goldblatt understood *DVR* to stand for the proposition that the section "need not be read to mean that the court is statutorily required to conduct a full claims allowance process." Understanding the section to mean there must be a final decision on every claim objection "would provide an objector with the very ability to extract holdout value."

Judge Goldblatt said he "would be disinclined to adopt such a construction unless it were compelled by the statutory text." Furthermore, he said that "such a reading is not, in any event, compelled by the text of § 502(b)."

Agreeing with *DVR*, Judge Goldblatt held "that one can reconcile § 502(b)'s right of a party in interest to object to the allowance of a claim with the trustee's historical authority to settle claims allowance disputes by giving the objecting party a full and fair opportunity to be heard in opposition to the motion to approve a settlement."

More particularly, Judge Goldblatt said that "the court must engage in a searching inquiry into the reasonableness of the proposed settlement with the full participation of the objecting party."

As further support for the idea that a full hearing on claim allowance is not required, Judge Goldblatt pointed to Section 502(c), which, he said, "expressly permits a court to 'estimate' a claim." Although the court should give "full and fair" attention to the objector's arguments, he said "there remains some room for deference to the trustee's judgment."

Applying the Standard to the Proposed Settlements

Recognizing that the proposed settlements would allow the claims for more than his prior decisions indicated, Judge Goldblatt said he had "no quarrel at all with the proposition that the debtors would rationally pay something to the pension plans to eliminate the risk associated with the plans' pursuit of appeals." He was therefore required "to assess the likelihood that an appellate court might conclude that this Court's earlier decisions were wrong."

Judge Goldblatt framed the "question [as] whether, viewed objectively, the debtors' decision to settle the potential appeals, by paying amounts that are greater than the estate would owe if the decisions were all affirmed, was the exercise of reasoned business judgment."

Examining one of the proposed settlements, Judge Goldblatt said it "effectively ascribes a 60 percent likelihood to the possibility this Court's ruling will be affirmed and a 40 percent likelihood to the possibility it will be reversed." Although he saw a smaller chance of reversal, he did "not believe that the decision to resolve this by ascribing a 40 percent likelihood of success to the pension plans is outside the range of reasonable."

Applying the same standard, Judge Goldblatt approved most of the settlements, but not those ascribing a 100% likelihood to reversal.

The opinion is *In re Yellow Corp*., 23-11069 (Bankr. D. Del. April 2, 2026).

Venue, Jurisdiction & Power

Sixth Circuit finds no appellate standing to challenge nondebtor releases when the appellant has opted out of nondebtor releases.

Eighth Circuit Concurrence Finds Reasons for Survival of 'Person Aggrieved'

For failure to satisfy the "person aggrieved" test, the Eighth Circuit predictably dismissed an appeal challenging nondebtor releases in a chapter 11 plan because the appellant had opted out of nondebtor releases and wouldn't be affected one way or the other.

Readers may be intrigued by reading the concurring opinion by Circuit Judge David Stras, who questioned whether the "person aggrieved" standard for appellate standing survived adoption of the Bankruptcy Code. However, he proposed an idea to account for the endurance of "person aggrieved" under traditional concepts of standing.

Appellant Opted Out of Releases

A Catholic hospital sold the assets and confirmed a chapter 11 plan with two categories of nondebtor releases. In the first category, the debtor and creditors released the major players in the reorganization, such as official committees and their members, bondholder representatives and a related order of nuns.

The second category of releases ran in favor of the major players' current and former officers, directors, affiliates, employees, agents, financial advisors and consultants. We shall refer to the second group as the remote released parties.

The plan enabled creditors to opt out of releases by checking a box on the ballot. Creditors who voted in favor of the plan or who did not vote would grant the releases, including the remote released parties.

The hospital's former corporate manager had a general unsecured claim for more than $30,000. The former manager opted out and opposed confirmation, contending that the Supreme Court's *Purdue* decision precluded releases in favor of the remote released parties. The bankruptcy judge decided that the former manager lacked standing to object because he had already opted out of the releases. The bankruptcy judge overruled the objection and confirmed the plan.

The former manager appealed and was denied stays pending appeal. On appeal, the former manager only challenged the releases in favor of the remote released parties.

On appeal, the district judge agreed with the bankruptcy judge and dismissed the appeal for lack of standing. If the circuit were to find standing, the district judge affirmed on the merits. *See Mercy Health Network Inc. v. Mercy Hospital, Iowa City, Iowa*, 671 B.R. 499 (N.D. Iowa March 3, 2025). To read ABI's report, click here.

No Injury, No Standing

Citing Eighth Circuit authority, Circuit Judge Bobby E. Shepherd began from the proposition that only a "person aggrieved" has standing to appeal in a bankruptcy case. The circuit went on to say that a "person aggrieved" is someone who is directly and adversely affected in a pecuniary sense.

Paraphrasing the circuit, Judge Shepherd said, "A party does not have standing to appeal a bankruptcy court's order if it cannot materially benefit from the relief it is seeking." He said that the former manager "would not gain anything from a reversal of the bankruptcy court's order" because he had "already opted out of the Third-Party Releases [and] . . . is not bound by them regardless of whether they are held to be enforceable."

Again adverting to Eighth Circuit authority, Judge Shepherd said that the plan did not increase the former manager's burdens or diminish his rights but merely maintained the *status quo*. Quoting the Sixth Circuit, he said,

> "[A party] may not assert merely the 'vindication of the rule of law' as its basis for harm without alleging an actual injury . . . . [because the] 'psychic satisfaction' that the bankruptcy 'laws are faithfully enforced' 'is not an acceptable Article III remedy[.]'"

The former manager contended that he had standing because the releases granted by the debtor would reduce the recovery by creditors like him. Judge Shepherd rejected the idea, saying that "this theory of harm [is] completely speculative" because the former manager had not identified any claims that might increase creditors' recoveries.

Judge Shepherd affirmed dismissal of the appeal, saying,

> [W]e agree with our sister circuits who have held that unsecured creditors do not have standing to appeal a bankruptcy court order when it is only "'theoretically possible' that [they] would benefit" from their appeal.

The Concurrence

In "Observations" at the conclusion of ABI's report on the district court opinion, we asked, "As a matter of constitutional law under Article III, may courts contrive prudential notions of standing to narrow the scope of who may appeal?"

Circuit Judge Stras addressed precisely that question in his concurrence. Although he agreed that the former manager lacked standing under the circuit's precedent, he asked,

> The mystery is why we still have a restrictive test for "bankruptcy [appellate] standing" at all.

Citing the Tenth Circuit, Judge Stras said that the "person aggrieved" standard "cannot come from the Bankruptcy Code, which dropped the 'person aggrieved' language nearly five decades ago." It persists, he said, as "'essentially prudential,'" citing the Third Circuit. He continued,

> [T]hat label can be "misleading" and "inapt," *Lexmark Int'l, Inc. v. Static Control Components, Inc.*, 572 U.S. 118, 125, 127 n.3 (2014).

Judge Stras said that the zone-of-interests test "is a poor fit because the statute does not say anything about who can appeal," again citing *Lexmark*. "If anything," he said, "Congress has left us guessing since 1978."

Citing the Supreme Court, Judge Stras said,

> The closer match, at least in my view, is the prohibition on third-party standing. It requires parties to "generally . . . assert [their] own legal rights and interests," not those belonging to "others." *Warth v. Seldin*, 422 U.S. 490, 499 (1975).

Again quoting the Supreme Court, Judge Stras said, "'the litigants themselves still must have . . . a sufficiently concrete interest in the outcome.' *FDA v. All. for Hippocratic Med.*, 602 U.S. 367, 393 n.5 (2024) (citation omitted)."

Applying Supreme Court authority to the case at hand, Judge Stras noted that the former manager had opted out of nondebtor releases and observed that "this scenario is common in bankruptcy." However, what "the 'person aggrieved' standard really does is filter out parties who lack 'the appropriate incentive' to litigate the issues they are raising," citing *Kowalski v. Tesmer*, 543 U.S. 125, 129 (2004).

Judge Stras concluded by saying that "bankruptcy standing may have a sturdier foundation than we think. Unlike other 'prudential' justiciability doctrines, this one is 'closely related to Art[icle] III concerns,' if not partially rooted in its 'case-or-controversy requirement.'"

Saying that the reasons "for its survival may well lie there," Judge Stras said, "they can await another day."

The opinion is *Mercy Health Network v. Mercy Hospital*, 25-1654 (8th Cir. June 12, 2026).

Although substantive consolidation should have been sought by adversary proceeding, the Eleventh Circuit holds that using a motion instead was harmless error.

Substantive Consolidation by Motion, Not Adversary Proceeding, Was Harmless Error

Affirming the lower courts in a short but precedential opinion, the Eleventh Circuit held that ordering substantive consolidation by motion rather than by adversary proceeding was harmless error.

A company filed a petition under Subchapter V of chapter 11, commencing a case that was later converted to chapter 7. The chapter 7 trustee filed a motion for substantive consolidation of the debtor with four other entities that were subject to common control by the individual who controlled the debtor.

In granting conversion to chapter 7, the bankruptcy court found that the debtor had commingled assets with the other four entities and had committed misconduct in dealings with the other entities. The bankruptcy judge granted the motion for substantive consolidation, deciding that findings from the conversion order supplied the elements required for substantive consolidation by application of the doctrine of issue preclusion.

The District Court's Holding

The debtor's owner and the four entities appealed, but the district court affirmed in a 56-page opinion.

The appellants argued primarily in district court that the bankruptcy court erred because substantive consolidation was not sought in an adversary proceeding under Bankruptcy Rule 7001(7). With exceptions that do not apply, the rule requires an adversary proceeding in "a proceeding to obtain an injunction or other equitable relief."

"Although this is admittedly a close call," the district court said, "the Eleventh Circuit has suggested (albeit in *dicta*) that a trustee *need not* seek substantive consolidation *only* through adversary proceedings." [Emphasis in original.] *Smith v. Slott*, 754 F. Supp. 3d 1271, 1282 (S.D. Fla. Oct. 17, 2024). To read ABI's report on the district court affirmance, click here.

Even if substantive consolidation should have proceeded through an adversary proceeding, the district court said that the "error was unambiguously harmless, since the Appellants received all the due process they were owed." *Id.* at 1294. The district court upheld the bankruptcy court's order granting the motion for substantive consolidation.

The nondebtor entities appealed to the Eleventh Circuit.

Again, Harmless Error

In his June 1 opinion, Circuit Judge William Pryor noted that the appellants didn't challenge the factual basis for substantive consolidation but "only made procedural arguments" insisting "that substantive consolidation requires an adversary proceeding." He nonetheless held that the bankruptcy court did not err in identifying grounds for substantive consolidation, because the bankruptcy court properly applied the factors required by the Eleventh Circuit in *Eastgroup Properties v. Southern Motel Ass'n*, 935 F.2d 245 (11th Cir. 1991).

Addressing procedure, Judge Pryor said that the appellants "failed to prove how granting substantive consolidation by motion affected their substantial rights." Of significance, he said, "Each entity received adequate notice and an opportunity to be heard before the motion was granted."

Regarding adequacy of notice, Judge Pryor said,

> [The trustee] served a copy of the substantive consolidation motion and notice of the hearing on each non-debtor entity by first-class mail, the same manner of personal service required for an adversary proceeding. See Bankruptcy Rule 7004(b).

Regarding the lack of service of a summons, Judge Pryor said,

> The non-debtor entities object only that the filing was styled as a motion instead of a complaint and was served without a summons. Even so, the non-debtor entities all objected to the motion represented by the same counsel at the substantive consolidation hearings.

Judge Pryor said that the appellants could tell neither the bankruptcy court nor the circuit court "how those errors would change the [substantive consolidation] analysis." He affirmed the bankruptcy court's substantive consolidation order.

The opinion is *Smith v. Slott (In re No Rust Rebar Inc.)*, 24-13383 (11th Cir. June 1, 2026).

The first-filed debtor, an inactive subsidiary with no operations, employes or tangible assets, established venue in New Jersey for a family of companies by opening a $1 million bank account 16 days before filing.

Bank Account Opened 16 Days Before Filing Made Venue for a Mega Chapter 11 Case

At least when it comes to confirming a prepackaged chapter 11 plan that's been accepted by more than 70% of the holders of debt in the only impaired classes, venue for a family of companies can be created by having an inactive subsidiary open a $1 million bank account in the city to be home for the reorganization, for reasons explained by Bankruptcy Judge Michael B. Kaplan of Trenton, N.J.

The first-filed debtor was a subsidiary that had no employees or customers on the filing date. It did, however, have a $1 million account at a bank opened in Trenton 16 days before filing.

The first-filed debtor had been "formed solely as an acquisition vehicle for the Debtors' purchase of a manufacturing facility located in Norwood, Ohio," Judge Kaplan said in his March 16 opinion. The plant eventually closed and was sold in 2023. Judge Kaplan added, "There have been no operations since."

Including the parent corporation, more than 50 other related debtors subsequently filed their chapter 11 petitions in Trenton. The parent and the other affiliates were entitled to venue their petitions in Trenton under 28 U.S.C. § 1408(2). The objective of the prepackaged plan was to reduce debt by $3.9 billion in two classes of funded debt. All other classes were unimpaired.

Contending that venue in New Jersey was improper under 28 U.S.C. §§ 1406, 1408 and 1412, the U.S. Trustee and several creditors filed motions to dismiss or transfer the cases to another district. After a hearing with witnesses, Judge Kaplan denied the motions to dismiss or transfer.

The Asset-Based Approach

The propriety of venue for the first-filed debtor's chapter 11 case in New Jersey was governed by Section 1408(1), which provides that a petition may be filed in the district

> in which the domicile, residence, [or] principal place of business . . . of the person or entity that is the subject of such case ha[s] been located for the one hundred and eighty days immediately preceding such commencement, or for a longer portion of such one-hundred-and-eighty-day period than the domicile, residence, or principal place of business . . . [i]f such person were located in any other district.

Applying the statute, Judge Kaplan said there were two questions: (1) What are the first-filed debtor's principal assets; and (2) where were they located for the longer portion of the 180-day period before filing?

To answer the question, Judge Kaplan said there were two approaches: the "time-based approach" and the "asset-based approach." Giving examples, he said that "both approaches have flaws and can lead to absurd or unintended results." He conceded that the asset-based approach, "to some degree, makes venue subject to manipulation" because "many assets can be relocated." He added, "[S]ome parties might develop creative workarounds to the protections built into the statute."

Judge Kaplan ultimately decided that the asset-based approach "is the appropriate approach for determining venue based on principal assets" because it "produces more logical results and construes the statute in a way that is more consistent with the functional concerns of the administration of the bankruptcy estate."

Finding no caselaw "directly on point," Judge Kaplan said that Congress "seemingly intentionally . . . left the venue statute broad and has not provided explicit guidance for its application." He held that venue was proper in the district because the first-filed debtor's $1 million bank account was the principal asset and was "located longer in this district than in any other during the Venue Period."

Intangible Assets Have Their Own Situs

Drilling down into arguments for and against venue in New Jersey, Judge Kaplan rejected the idea that intangible assets follow the venue of the parent. He found support in the Uniform Commercial Code, which, he said, "assigns situs to deposit accounts based on factors which do not consider the depositor's domicile."

Judge Kaplan described the objectors as contending "that permitting venue to rest on recently opened bank accounts would render § 1408 meaningless and allow debtors to file 'anywhere.'" He disagreed, because the "statute does not require longevity of ownership, historical nexus, operational activity, or a qualitative business purpose."

Judge Kaplan said he was "unpersuaded by the 'file anywhere' parade of horribles." If the debtor were to have "truly operating facilities," he said that "venue properly would lie there and/or could be transferred there under § 1412." He once again held that venue was "proper in this district under § 1408(1)."

Fact-Intensive Factors

Judge Kaplan devoted half of his 28-page opinion to dealing with the fact-specific argument by the objectors. He rejected the contention that several patents held by the first-filed debtor had sufficient value to be the principal assets. He was likewise persuaded by the debtor's evidence that intercompany receivables in favor of the first-filed debtor should have been written off years before.

Even if receivables owing by the parent had value, Judge Kaplan said they were subject to liens securing $5.5 billion in funded debt. He saw "no scenario" in which the first-filed debtor could "make use of these intercompany payables as part of its reorganization."

No Bad Faith, No Venue Transfer

Citing *In re LTL Management, LLC*, 64 F.4th 84 (3d Cir. 2023), the U.S. Trustee argued for dismissal as a bad-faith filing. Judge Kaplan dismissed the *LTL* analogy, noting that the first-filed debtor was not a "newly created bankruptcy vehicle."

Furthermore, the first-filed debtor was "in genuine financial distress" as a guarantor of $5.5 billion in debt.

Even when venue is proper, venue still can be transferred under Section 1412, which provides that a court may transfer a bankruptcy case "to a district court for another district, in the interest of justice or for the convenience of the parties."

Judge Kaplan saw "no basis to conclude that transfer would serve the interest of justice or be more convenient for the parties." Focusing on the first-filed debtor, he said that the assets were all intangible and that it had no employees or customers. He said, "[N]othing in the record establishes that a different district would provide greater proximity to its creditors, assets, or witnesses — or would otherwise be more convenient for those involved."

Although saying he "appreciates that the manner in which the Debtors have employed the venue statute strikes many as being inconsistent with the 'interest of justice,'" Judge Kaplan cited courts that "consistently hold that a primary consideration 'under the interest-of-justice prong is whether transfer would promote the economic and efficient administration of the bankruptcy estate.'"

If the case were transferred to another district, Judge Kaplan said that the transfer would occasion increased costs and delay and "imperil[] the Debtors' reorganization and could give rise to uncertainty among lenders, vendors, the market and thousands of employees." In addition, he gave "deference" to the debtors' "choice of forum."

Judge Kaplan said there was no evidence that the choice of venue was designed to hinder creditors or "take advantage of any favorable caselaw." In addition, he said that holders "of more than 83% of Debtors' prepetition funded debt support venue in this district."

Judge Kaplan conceded that the bank account was opened to establish venue in New Jersey, but he said it was "likely that venue would have been appropriate in multiple districts." He noted that Congress had failed to act several times when legislation was introduced to reform bankruptcy venue rules.

The case at hand, Judge Kaplan said, was a "situation intentionally created by Congress when it elected to broadly draft — and decline[d] to tailor — the venue statute." Denying the motion s to dismiss, he said it was "not this Court's place to 'close loopholes in legislation[,]'" citing *In re Patriot Coal Corp.*, 482 B.R. 718, 745 (Bankr. S.D.N.Y. 2012).

Observations

If one were to disagree with Judge Kaplan, on what grounds would one do so? Even though the small, inactive subsidiary's venue was proper in New Jersey, was the filing in bad faith? Is it bad faith for an inactive subsidiary to file first, rather than its parent company? How can the filing be in bad faith if the facts line up with the statute? How can it be bad faith if the statute does not require judging venue based on the parent?

Prof. Bruce A. Markell provided ABI with the following commentary:

> While I respect and like Judge Kaplan, he privileged form over substance and blinked at harm to the judiciary's essential commitment to non-partisanship in a case of clear venue-shopping. By contorting the "interests of justice" to justify the costs and time imposed by a debtor's choice of venue while downplaying the perfidy inherent in venue- or judge-shopping, he validated the shenanigans debtor's counsel employed, thereby encouraging further shenanigans by others.
>
> We might as well just toss the venue statutes, and let parties pick and choose what locations and what judges they want. To adopt Judge Kaplan's logic, it would save time and speed administration. It would also add to the growing perception that courts, and justice, are for sale to the highest bidder.

Prof. Robert M. Lawless authored a piece two years ago in *U.S. Law Week* that reads as though it was written in response to Judge Kaplan's opinion. Among other things, he said,

> [P]eople must perceive the judge as motivated only by a desire to be fair and not by motives extraneous to the issues at hand.
>
> Chapter 11 forum-shopping violates most of these criteria. Some bankruptcy judges have openly admitted [to] wanting to attract large Chapter 11 cases. Procedural justice is about perception. It is telling that most other countries don't tolerate forum-shopping the way the US legal system does . . . .
>
> Given the ease with which it can be manufactured, Chapter 11 today is venue by declaration. And for particularly large companies, venue rules have become functionally nonexistent.
>
> Corporations have cited law firm retainers, office leases, or PO boxes as their "principal assets" in a preferred venue . . . .
>
> It was the courts' job to consider the bigger picture to say "no." They abdicated their responsibility for reasons that are well-rehearsed: national fame, professional accolades, and appreciation of the local bankruptcy bar . . . .
>
> The legal system's overriding goal isn't efficiency. In a democratic society, the judicial system needs the citizenry to have faith in the courts' legitimacy.

Prof. Robert M. Lawless, "Bankruptcy Venue Shopping Breaks Perceptions of Judicial Fairness," *U.S. Law Week*, June 26, 2024.

Prof. Markell is the Professor of Bankruptcy Law and Practice at the Northwestern University Pritzker School of Law. Prof. Lawless is the Max L. Rowe Professor of Law and co-director of the Program on Law, Behavior & Social Science at the University of Illinois College of Law.

The opinion is *In re Multi-Color Corp.*, 26-10910 (Bankr. D.N.J. March 16, 2026).

Fourth Circuit needs to sit en banc before deciding whether Carolin and Robbins apply when the debtor is not in financial distress.

Over Dissent Again, Fourth Circuit Allows Mass Tort Reorgs Without Financial Distress

For the fourth time, Circuit Judge Robert Bruce King has filed a vigorous dissent imploring his colleagues on the Fourth Circuit to sit *en banc* and reconsider whether the circuit's *Carolin* and *Robbins* decisions permit chapter 11 reorganization by solvent debtors able to pay tort claims in full.

As he had done twice last year in *Bestwall* dissents, Judge King said that "our Circuit has become the 'safe haven' for ultra-wealthy corporations seeking to evade asbestos-related civil tort liability under the guise of the Bankruptcy Code."

Bound by *Carolin* and *Robbins*, the majority affirmed denial of a motion to modify the automatic stay in a mass tort case involving CertainTeed Corp. Declining to reach the issues raised by the dissenter, the February 11 majority opinion by Circuit Judge Paul V. Niemeyer explained the narrow scope of the majority's opinion:

> [W]e do not have before us any motion to dismiss the Chapter 11 petition so as to challenge whether Chapter 11's § 524(g) reorganization procedure has been appropriately invoked in this case. Nor do we have the question before us [of] whether the pre-bankruptcy Texas Two-Step process is appropriate or legal. Indeed, we also do not have before us the more fundamental question of whether Congress had constitutional authority to enact § 524(g) without requiring a showing of "insolvency." Thus, in this *presumptively* viable Chapter 11 proceeding, we address only the standard for lifting a § 362(a) stay and whether the district court correctly applied that standard.

The Divisional Merger

Owned by a French corporate parent, CertainTeed manufactured products containing asbestos. As Judge Niemeyer said in his majority opinion, the company spent some $3.5 billion until 2019 litigating and settling lawsuits, exhausting insurance in the process.

In 2019, the company underwent a so-called divisional merger under Texas corporate law, creating two companies. One was to become the debtor.

The debtor assumed all liability for asbestos and was given a business with an estimated $150 million market value. The second company, which we shall refer to as New CertainTeed, had the profitable businesses and no asbestos liability.

New CertainTeed gave the debtor an uncapped funding agreement promising to pay all expenses under chapter 11 together with an undertaking to pay all asbestos-related claims through a trust to be created at plan confirmation under Section 524(g).

In early 2020, the debtor filed a chapter 11 petition in North Carolina.

After a lengthy trial in 2021, the bankruptcy court denied a motion to modify the automatic stay that would have allowed tort claims to proceed. In the same order, the bankruptcy court extended a preliminary injunction barring suits against nondebtor third parties. There was no appeal, nor did anyone file a motion to dismiss the chapter 11 case, Judge Niemeyer said.

In early 2024, two asbestos claimants filed a motion to lift the automatic stay. The motion argued that the chapter 11 filing was in subjective bad faith because the debtor had the capacity to pay all claims in full. The bankruptcy court denied the motion, ruling that the claimants had not shown evidence of bad faith. The district court affirmed, prompting an appeal to the Fourth Circuit.

Robbins and *Carolin*

On the merits, Judge Niemeyer said that the "narrow question" was whether the bankruptcy court properly denied the lift-stay motion. For "decades," he said, *In re Robbins*, 964 F.2d 342 (4th Cir. 1992), and its three-factor test has been the "controlling authority" in the Fourth Circuit.

Judge Niemeyer said that the bankruptcy court had "correctly" applied the *Robbins* factors and went on to provide "extensive explanation as to why those factors suggest that granting the motion to lift the stay would undermine the entire bankruptcy proceeding."

Judge Niemeyer characterized the claimants as contending that "*Robbins* is not dispositive because it did not address its argument that [the debtor] acted in bad faith in filing the Chapter 11 petition to obtain a stay" when it was profitable and not financially distressed. He agreed "that *Robbins* did not address whether a showing of bad faith would justify lifting the stay," because that question was not presented to the appeals court. Citing *Carolin Corp. v. Miller*, 886 F.2d 693 (4th Cir. 1989), he also agreed that "good faith is an *implied* requirement for obtaining an automatic stay." [Emphasis in original.]

Turning to *Carolin*, Judge Niemeyer said that bad faith as grounds for dismissal or stay modification "is not without boundaries." The movant must show both "subjective bad faith and objective futility," as *Carolin* requires.

In the case on appeal, Judge Niemeyer said that the bankruptcy court found a lack of evidence about bad faith and failure to meet the objective futility requirement.

On bad faith, Judge Niemeyer said that the debtor "was legitimately seeking to invoke the § 524(g) process authorized by Congress to address the circumstances in which it faced 60,000 pending asbestos-related claims and expected to receive a continuous flow of such lawsuits for decades to come."

Regarding the debtor's ability to pay claims in full without chapter 11, Judge Niemeyer said that the "statutory authority for a company to pursue a § 524(g) plan in a Chapter 11 reorganization does not require a showing of 'insolvency.'"

Addressing the inadequacy of the country's tort system, Judge Niemeyer said that the "§ 524(g) process is quicker, more efficient, and fairer than can be provided by continuing with widely dispersed litigation in various federal and state courts."

Finding no fact that was clearly erroneous, the majority affirmed, holding that the bankruptcy court had not abused its discretion.

The Dissent

The majority opinion was 20 pages. Judge King "wholeheartedly" dissented in a 38-page opinion. He saw

> ample evidence in this record that the Debtor . . . and its non-debtor parent . . . have engaged in pervasive, well-documented, and systematic bad faith by subverting the Bankruptcy Code to evade asbestos-related civil tort liability and deprive tens of thousands of dead and dying Americans of their constitutionally protected day in court before a jury of their peers.

"In my view," Judge King said, "the majority's decision is not only inexplicable as a matter of law and fact, it is unacceptable." He referred to the debtor's "sham Chapter 11 bankruptcy" and the "corporate sleight-of-hand called the 'Texas Two-Step.'" He said that *Robbins* was "inapposite" and that *Carolin* was "wholly inapplicable."

Judge King had three reasons for differing with the majority. First, lack of good faith is grounds for modifying the stay, citing the Supreme Court and three circuits. Second, *Robbins* "merely articulates the test for ascertaining what constitutes the statutory 'cause' in the context of a good faith bankruptcy." Third, "It makes no sense to conclude that the Debtor has been acting within the contours of a legitimate Chapter 11 bankruptcy . . . without first addressing the 'bad faith' that already infects its Chapter 11 bankruptcy petition."

Harkening to the Third Circuit's ground for twice dismissing chapter 11 filings by a Johnson & Johnson subsidiary, he said that CertainTeed "was not, and never will be, in any financial distress, [and] is not seeking to reorganize for a legitimate purpose." He went on to say "that § 524(g) is a remedy within Chapter 11 and made available to an entity 'in financial distress.'"

Judge King accused the majority of being "engage[d] in a rather alarming type of extra-legislative judicial 'tort reform,'" based on a belief that "§ 524(g) is 'quicker, more efficient, and fairer than can be provided by continuing with widely dispersed litigation in various federal and state courts.'"

Judge King "wholeheartedly" dissented.

Commentary # 1

Prof. Ralph Brubaker provided ABI with the following commentary:

"After declining to take up the issue on multiple previous occasions, the Fourth Circuit has now squarely held that a Texas Two-Step filing, by a debtor with the admitted ability to fully and timely pay all of its mass-tort obligations, is not a bad-faith filing.

"Given the Third Circuit's contrary ruling in the Johnson & Johnson/*LTL Management* case, there is now a clear circuit split that will hopefully convince the Supreme Court to step in.

"These Texas Two-Step cases raise profound issues regarding whether it is appropriate to use the Chapter 11 process *solely* as a means of displacing the nonbankruptcy tort system. The good-faith inquiry in such a case also implicates fundamental constitutional issues regarding the scope of the Bankruptcy Power, the Due Process and Seventh Amendment rights of individual tort claimants, and states' sovereignty over the development and administration of state-law tort claims, embedded in Article III's limitations on federal courts' jurisdiction over state-law claims."

Professor Brubaker is the James H.M. Sprayregen Professor of Law at the University of Illinois College of Law. He is a consultant to counsel for one of the participants in a pending Texas Two-Step mass-tort bankruptcy case. The views expressed here are solely his own.

To read one of Prof. Brubaker's writings on the constitutional issues, click here.

Commentary # 2

Prof. Robert M. Lawless provided ABI with the following commentary:

"The issue is not going away anytime soon, and it has the feel that we are setting up for a Supreme Court decision in the coming years.

"The dissent implies the problem is with the divisive merger. Would the dissent have ruled differently if the case had involved putting the original company into bankruptcy? With the backstop, isn't the entire corporate group equally solvent (or insolvent) before and after the divisive merger?

"If so, what is it about a divisive merger specifically that causes concern? The dissent nods at an answer. The backstop from the 'GoodCo' replaces the assets of 'OldCo' with a promise to pay the value of the assets. If there is anything bankruptcy lawyers understand, it is that a promise to pay is not the same as the payment itself."

Prof. Lawless is the Max L. Rowe Professor of Law and co-director of the Program on Law, Behavior & Social Science at the University of Illinois College of Law.

Note

To read ABI's reports on the Fourth Circuit's three recent *Bestwall* opinions and Judge King's dissents, click here, here and here.

The opinion is *Herlihy v. DBMP LLC*, 24-2109 (4th Cir. Feb. 11, 2026).

By a vote of 8/6, the Fourth Circuit denied rehearing en banc on the question of whether federal courts only have subject matter jurisdiction over insolvent debtors.

Fourth Circuit May Prompt *Cert* to Decide Whether Bankruptcy Requires Insolvency

Over a dissent, the Fourth Circuit held on August 1 that the bankruptcy court has subject matter jurisdiction under 28 U.S.C. § 1334(a) to entertain a bankruptcy reorganization of a solvent company.

Circuit Judge Robert Bruce King dissented vigorously but "respectfully" in August, believing that the Bankruptcy Clause in Article I of the Constitution only permits bankruptcies by insolvent entities or those that cannot or will not pay their debts as they mature.

The official asbestos claimants' committee filed a petition for rehearing *en banc*. By a vote of 8/6, the Fourth Circuit denied the rehearing petition on October 30. Circuit Judge King "regrettably" but "respectfully" dissented. None of the other five circuit judges who voted for rehearing joined Judge King's dissent.

Judge King's dissent merits reading in full text at first opportunity. At times, his language is remarkable.

'Manufactured Sham Bankruptcy'

As we explained when reporting the August 1 opinion, the debtor, Bestwall, was created by a Texas divisional merger. Asbestos liability went to Bestwall, while the solvent parent, Georgia-Pacific, took most of the assets and gave Bestwall an undertaking to pay the expenses of Bestwall's chapter 11 case and to fund an asbestos trust to be created under a plan confirmed in accord with Section 524(g). *In re Bestwall LLC*, 71 F.4th 168 (4th Cir. 2023). To read ABI's reports on the majority decision, the dissent and the concurrence, click here, here and here.

Dissenting from the denial of rehearing and believing that the bankruptcy court had no subject matter jurisdiction over a solvent debtor, Judge King called the divisional merger "a novel and provocative corporate sleight-of-hand maneuver" that created Bestwall, a debtor "not at all . . . in distress." He said that the "sacred right of the . . . Bestwall asbestos claimants to pursue justice through the tort system of America's civil courts . . . has been placed on hold by a solvent profitable enterprise called Bestwall, acting through a *manufactured sham bankruptcy*." [Emphasis added.]

According to Judge King, the chapter 11 case was designed to "extract more favorable settlement terms from their suffering and dying victims through litigation delay." He described the effect as follows:

> [A] financially-healthy and fully-solvent corporation (that is, [the Georgia-Pacific parent]) has placed its asbestos-related tort liabilities involving thousands of American workers behind the firewall of bankruptcy protection. Yet critically, [the Georgia Pacific parent] is not undergoing the scrutiny, transparency, and risk that a Chapter 11 bankruptcy petition should entail.

Here's how Judge King characterized the result sought by debtor Bestwall and its parent:

> Such an *obscene* — and . . . unconstitutional — result is far from the fundamental proposition that "[b]ankruptcy offers individuals and businesses in financial distress a fresh start to reorganize, discharge their debts, and maximize the property available to creditors." *See Truck Ins. Co. v. Kaiser Gypsum Co., Inc.*, 602 U.S. 268, 272 (2024). [Emphasis added.]

A *Cert* Petition?

This writer presumes there will be a petition for *certiorari*, bolstered by the 8/6 split in the Fourth Circuit on rehearing *en banc*. This writer doubts there will be a grant of *certiorari*, because there is no circuit split. Furthermore, granting *certiorari* and dismissing the case based on an Article I constitutional violation would engender a crisis equal to that resulting from *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), and its proclamation that the bankruptcy court's jurisdiction was unconstitutional.

If the equivalent of insolvency were required before federal courts could have subject matter jurisdiction for a case under any chapter of title 11, solvency would become a threshold issue in many cases, perhaps requiring appraisals of individual and corporate debtors' assets, a time-consuming and expensive process. Reorganization might not be available for solvent entities that need time to cure defaults but have illiquid equities in their assets.

We will not delve into Judge King's discussion of the merits, except to say that his view of the history and tradition of Article I leads him to believe that the definition of "bankruptcy" today must be the same as it was in 1789 and that bankruptcy should be "available only to a debtor who [is] truly and actually bankrupt — that is, a financially distressed debtor unable or unwilling to pay its debts."

Judge King's views prompt consideration of the issues that could arise from originalist constitutional theory in the bankruptcy sphere. If the Supreme Court were to adopt an originalist interpretation of the word "bankruptcy," there could be problems in bankruptcy beyond subject matter jurisdiction. We might see challenges to substantive provisions of the Bankruptcy Code based on the idea that the relief accorded to debtors in the eighteenth century should limit the relief available today.

Eventually, originalist thinking about bankruptcy might require a constitutional amendment before we have bankruptcy and reorganization laws as functional as they are today.

We urge reading Judge King's dissent, because he likely is not the only judge or scholar to hold the same opinion.

Observations

The Fourth Circuit became a haven for large company bankruptcies given the circuit's unique standard governing dismissal for a bad faith filing. In the Fourth Circuit, creditors are required to prove both subjective and objective bad faith to dismiss a chapter 11 case. In part, the Bestwall reorganization has persisted for eight years, since dismissal for bad faith was not available.

This writer is seeing a pattern in circuit courts regarding large company bankruptcies that stretch the rubber band. Note the Third Circuit's dismissal in *LTL Management* - Johnson & Johnson based on the lack of "financial distress," as well as the Fifth Circuit's narrowing of the doctrine of equitable mootness and its aversion to "lender-on-lender violence," as shown in *Serta Simmons*. Similarly, the Fifth Circuit narrowed exculpations and releases and trimmed the power of bankruptcy courts in two *Highland Capital* decisions. And let's not forget *Purdue*, where the Supreme Court knocked down nonconsensual, nondebtor releases that had been used widely around the country for decades.

Were it before the Third Circuit, the Philadelphia-based appeals court could have dismissed the Bestwall reorganization for lack of financial distress. With the same recourse not available, the Fourth Circuit found itself in a box, with several of the circuit judges showing antipathy for the reorganization but finding themselves procedurally unable to dismiss the case without sitting *en banc* and setting aside circuit precedent governing bad faith dismissals.

The doctrine of equitable mootness and the inability to appeal interlocutory decisions restricts the capacity of circuit courts to reach pivotal issues emerging in bankruptcy courts, sometimes for decades. This writer believes we are now seeing some Article III judges question bankruptcy's legitimacy in providing relief for large companies facing mass tort liability.

It would be best if Congress were to deal with mass torts generally in a manner similar to asbestos bankruptcies under Section 524(g). Were there another statute to salvage big companies without infringing on the rights of consumers and tort victims, creative lawyers would not be so tempted to stretch bankruptcy to the breaking point.

Courts endeavor to find a statutory basis for reaching a result before turning to constitutional issues. The Fourth Circuit might consider revising its definition of bad faith to permit disposition of cases like *Bestwall* without creating a revolution in constitutional thinking about bankruptcy.

The foregoing are the opinions of this writer, not ABI.

The opinion is *Official Committee of Asbestos Claimants of Bestwall LLC v. Bestwall LLC (In re Bestwall LLC)*, 24-1493 (4th Cir. Oct. 30, 2025).

Lack of financial distress was one of several contributing factors for the Tenth Circuit BAP's affirmance of dismissal for bad faith filing in chapter 11.

Lack of Financial Distress Results in Chapter 11 Dismissal for Bad Faith

In the Third Circuit, lack of financial distress means dismissal of a corporate chapter 11 petition. *See In re LTL Management LLC*, 58 F.4th 738, 64 F.4th 84 (3d Cir. Jan. 30, 2023). To read ABI's report, click here.

For an individual debtor in the Tenth Circuit, lack of financial distress meant conversion of his chapter 11 case to chapter 7, not dismissal.

Investing in real estate, the debtor and the creditor had been business partners. For breach of the partnership agreement, the creditor obtained a judgment in state court amounting almost to $2.5 million with interest and attorneys' fees.

The debtor appealed the state court judgment but was unable to obtain a bond because he had not filed income tax returns for 10 years. However, the debtor had made substantial quarterly payments to the Internal Revenue Service.

Five months after the judgment, the creditor attached the debtor's seven bank accounts. The debtor did not challenge the attachments in state court.

Claiming a liquidity crisis, the debtor filed a chapter 11 petition and asserted that he would file a plan paying all creditors in full, including the IRS and the judgment creditor. The schedules indicated that the debtor had about $7.7 million in assets with a net equity exceeding $3.5 million. Annual income was in the neighborhood of $1 million.

The debtor was current on all debts, other than the judgment and the claim filed by the IRS for about $1 million.

Claiming that the filing was a two-party dispute designed to frustrate enforcement of the judgment, the creditor filed a motion to dismiss or convert the case to chapter 7 under Section 1112(b).

Bankruptcy Judge Thomas B. McNamara of Denver converted the case to chapter 7. He found that the debtor was not in financial distress, that the debtor had filed the petition to gain a litigation advantage and that the case was primarily a two-party dispute.

The debtor appealed, but the Tenth Circuit Bankruptcy Appellate Panel affirmed in a nonprecedential opinion on September 30 by Bankruptcy Judge Sarah A. Hall.

The Clear Error Standard

The outcome of the appeal turned on Section 1112(b)(1), which provides that the court "shall" convert a chapter 11 case to chapter 7 or dismiss the case, "whichever is in the best interests of creditors and the estate, for cause . . . ." Section 1112(b)(4) contains a nonexclusive list of 11 examples of "cause," but none were applicable to the case on appeal.

"[W]e also recognize that bad faith constitutes cause for conversion," Judge Hall said. She cited the Tenth Circuit for telling bankruptcy courts to consider any factors indicating that the filing was an abuse of the Bankruptcy Code or was employed to delay or frustrate legitimate efforts by creditors to enforce their rights.

In reviewing the bankruptcy court's fact-finding for clear error, Judge Hall stated the standard as follows:

> Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous, and an appellate court may not reverse it even though convinced that had it been sitting as the trier of fact, it would have weighed the evidence differently.

Financial Distress

First, Judge Hall reviewed the bankruptcy court's finding that the debtor had no financial distress.

The bankruptcy court found that the debtor had leased an $88,000 car for his girlfriend two weeks before filing, even though he owned 11 unencumbered vehicles. The lower court also found that the debtor had continued "lavish spending" after entry of the judgment.

The debtor did not contend that the fact-findings were wrong but that the bankruptcy court had placed too much emphasis on a balance-sheet solvency test. He argued there was financial distress resulting from the garnishment of bank accounts.

"The Bankruptcy Code does not contain any insolvency requirement (except as to chapter 9)," Judge Hall said, "nor does it direct any application of a specific test to determine financial distress." In addition, she said that "the Tenth Circuit has not addressed what it means to be in financial distress in this context."

On the other hand, Judge Hall said that "several courts have treated financial distress as an additive factor in the totality of the circumstances analysis with a lack of financial distress highlighting an improper purpose for filing." In addition, she cited *LTL* to mean that "a debtor must be in 'immediate' and 'apparent' financial distress that justifies the need for bankruptcy relief."

Judge Hall found no error in finding there was no financial distress, because "the Bankruptcy Court reasonably concluded [that the debtor's] claimed liquidity crisis was of his own making given available state-law remedies and substantial unencumbered assets." Similarly, she decided that "the Bankruptcy Court reasonably found [that the debtor's] failure to use available assets to address the Judgment or the account freeze . . . undermined the credibility of" a liquidity crisis.

Litigation Advantage

The bankruptcy court found that the "entire reason" for filing "was to obtain a tactical litigation advantage" by making bankruptcy "a substitute for posting an appeal bond." A litigation tactic occurs, Judge Hall said, when "the debtor invokes bankruptcy chiefly to gain procedural leverage in non-bankruptcy litigation, stalling enforcement, or using the automatic stay as a substitute for a supersedeas bond, *rather than to reorganize or maximize value*, especially where a debtor with means files after an adverse judgment to forestall a single creditor." [Emphasis in original.]

Even so, Judge Hall said that filing bankruptcy as a substitute for an appeal bond "is not bad faith *per se*." In the case on appeal, she said that the bankruptcy court had not applied a *per se* rule. Instead, she said that the bankruptcy court "treated [the debtor's] choice not to seek a stay or assert exemptions in the state court as indicative of evidence of both a lack of financial distress and a tactical bid for a 'free' appellate stay."

Judge Hall said that the bankruptcy filing shifted the risk of loss from the bonding company to the creditor. She held that "the Bankruptcy Court appropriately considered the totality of the circumstances and did not err in determining [that the debtor's] case was filed to obtain a tactical litigation advantage, which supported conversion based on bad faith."

Two-Party Dispute

Given the claim of the IRS, the debtor contended that the bankruptcy was not a two-party dispute. Judge Hall disagreed, saying that "at least one court has found a two-party dispute even when other creditors exist."

Judge Hall noted that no other creditors were pursuing collections, that the debtor was current on his other obligations and that the debtor had only five nonpriority creditors. She therefore found that "the Bankruptcy Court did not err in finding the bankruptcy case was primarily a two-party dispute despite the existence of the IRS debt."

Moreover, Judge Hall said that "the Bankruptcy Court did not convert the case solely because it was a two-party dispute but rather this fact was but one of the circumstances, in addition to others, indicating bad faith."

Even if "another court might have weighed the evidence differently," Judge Hall said that the appellate court "must defer to the Bankruptcy Court's factual findings unless they are 'completely devoid of minimum evidentiary support displaying some hue of credibility,' or 'bear[] no rational relationship to the supportive evidentiary data.'" She affirmed, because "the Bankruptcy Court's findings are anchored in the record, and thus, they are not clearly erroneous."

The opinion is *McHugh v. Lofstedt (In re McHugh)*, 24-20 (B.A.P. 10th Cir. Sept. 30, 2025).

Reaching the same results and affirming the bankruptcy court, the Third Circuit again holds that a foreign state receivership does not oust a corporation's board of authority to file bankruptcy.

Third Circuit Has a New *Whittaker* Opinion on Jurisdiction and Successor Liability Claims

Forget everything you knew from the Third Circuit's *Whittaker Clark & Daniels* opinion in September about successor liability and a company's ability to file bankruptcy after appointment of a receiver.

Creditors moved for panel rehearing and rehearing *en banc*, and we have an amended opinion.

After extensive briefing, the Third Circuit granted panel rehearing, denied rehearing *en banc* and issued an amended opinion on April 26 reaching the same results as the opinion in September 2025. In concurrences, Circuit Judges Thomas L. Ambro and Cheryl Ann Krause once again launched into a vigorous debate on whether there's any such thing as federal choice of law rules in bankruptcy cases.

To say that the new opinion is consequential is an understatement. In September, the three opinions totaled 88 pages. The three new opinions now consume 107 pages. Most of the new language is in the unanimous opinion on jurisdiction, the effect of a receivership and successor liability.

A comparison of the new opinions with the September opinions shows that the new, unanimous opinions were heavily rewritten. Indeed, the Third Circuit's order granting panel rehearing said, "The amended majority opinion was revised throughout in response to the arguments set out in Committee's [rehearing] petition."

Given the gravity of the topics covered in the new opinions, we today examine the authority of corporate officers to file bankruptcy petitions after a receiver has been appointed. Tomorrow, we will report the circuit's similarly unanimous analysis about the estate's ownership of successor liability claims.

The circuit's original opinion in September is reported at *In re Whittaker Clark & Daniels Inc.*, 152 F.4th 432 (3d Cir. Sept. 10, 2025). To read ABI's reports, click here, here and here.

As before, the debate between Judges Ambro and Krause about choice of law is all *dicta,* because the parties agreed that New Jersey law governed. Judges Ambro and Krause made few changes in their debate about choice of law. Because the concurrences are little changed, we will not trouble our readers with new reports. To read ABI's reports on the choice of law concurrences, here and here.

The Receiver and Successor Liability Claims

The debtor, Whittaker Clark & Daniels Inc., processed asbestos-laden talc and was beset with personal injury suits. In 2004, the debtor sold the business for $200 million cash, leaving it a shell company. As part of the deal, the debtor indemnified the buyer for claims arising from environmental and asbestos tort claims.

When more than 1,000 lawsuits were still pending, a jury in South Carolina awarded a $29 million judgment to a tort claimant. Immediately, the judgment creditor sought and won the appointment of a receiver in state court. The debtor promptly filed a chapter 11 petition in New Jersey without obtaining permission from the South Carolina receiver.

In bankruptcy court, the receiver filed a motion to dismiss, contending that the bankruptcy court had no jurisdiction and that the filing was unauthorized. The bankruptcy court denied the motion and was affirmed in district court.

While the appeal was percolating, the debtor wrangled a settlement where the buyer would pay $535 million in return for a release of successor liability claims. However, some tort claimants were already asserting successor liability claims and wouldn't give them up to the debtor.

The debtor therefore filed an adversary proceeding seeking a declaration that the estate owned the successor liability claims. Eventually, the bankruptcy court granted summary judgment in favor of the debtor. The bankruptcy court authorized a direct appeal, which the Third Circuit accepted.

Jurisdiction

On appeal, the receiver contended that the bankruptcy case should have been dismissed because the bankruptcy court had no jurisdiction and the debtor had no authority to file the petition following appointment of the receiver.

Writing once again for the unanimous circuit court, Judge Ambro mentioned how the Supreme Court previously had said that the propriety of a filing affected the bankruptcy court's jurisdiction. In more recent decisions, he said that the Supreme Court has been "more precise about hanging the 'jurisdictional label' on a statutory provision." These days, the Supreme Court has said that "the 'traditional tools of statutory construction must plainly show that Congress imbued a procedural bar with jurisdictional consequences.'"

Today, Judge Ambro said, "Anything short of a clear indication [of jurisdictional significance] will not do." He continued, "The statutes granting federal courts jurisdiction over bankruptcy cases do not attach jurisdictional significance to the propriety of a debtor's petition." He added that the governing jurisdictional statutes, 28 U.S.C. § 1334(a) and 28 U.S.C. § 157, "establish the jurisdictional grant for district and bankruptcy courts over bankruptcy cases, and neither they, nor any other provision, condition that grant on a properly filed petition."

Although "an improperly filed bankruptcy petition constitutes 'cause' to dismiss a bankruptcy case, 11 U.S.C. § 1112(b)(1)," Judge Ambro held that "it does not strip bankruptcy courts of subject matter jurisdiction."

Choice of Law Agreed in the Case on Appeal

Even if the bankruptcy court had subject matter jurisdiction, the question remained as to whether the case should have been dismissed for lack of permission from the state court receiver. But whose law should apply, South Carolina or New Jersey?

In the case at hand, the appeals court had no occasion to rule on choice of law because the parties agreed that New Jersey law governed the debtor's internal affairs. Judges Krause and Ambro nonetheless debated choice of law in their concurrences.

Receivership Didn't Oust the Board

Judge Ambro turned to New Jersey law to decide whether consent from the South Carolina receiver was required to file bankruptcy.

When a foreign court has appointed a receiver, Judge Ambro said, "New Jersey courts generally 'will appoint an ancillary receiver, [and] the assets will be so administered that creditors in [New Jersey] and in the foreign jurisdiction shall fare alike.'" He cited the Restatement (Second) of Conflict of Laws as being consistent with his holding regarding appointment of an ancillary receiver.

Therefore, Judge Ambro held that "the South Carolina Receiver needed to move for — and be granted — recognition in New Jersey and the appointment of an ancillary receiver to displace [the debtor's] board's control."

The tort claimants countered by arguing the bankruptcy court was required by the Full Faith and Credit statute, 28 U.S.C. § 1738, to enforce the state court's order appointing a receiver. Judge Ambro refuted the theory for three reasons.

Even if the South Carolina court had granted control over filing bankruptcy, Judge Ambro said that the tort claimants "did not attempt to enforce it."

"[M]ore fundamentally," Judge Ambro said, "we doubt [the South Carolina court's] ability" to "place control of [the debtor's] corporate affairs in the hands of the South Carolina Receiver," because "states' power to exercise control over actors within their respective borders is not without limits."

"[W]hen it comes to control over corporate decision-making," Judge Ambro quoted the Supreme Court in saying that "a state 'has no interest in regulating the internal affairs of foreign corporations.'"

As Judge Ambro read the South Carolina receivership order, the state court had not granted power to decide about bankruptcy. "And if it did," he said, "it would be an unprecedented exertion of power over a foreign corporation whose internal affairs are governed by the laws of a sister state, as well as a radical intrusion into the province of a co-equal sovereign."

Judge Ambro held that "New Jersey law governs and sanctions the authority of [the debtor's] board to petition for bankruptcy" because the "state of incorporation . . . enjoys exclusive authority to govern the internal affairs of its corporations."

The opinion is *In re Whittaker Clark & Daniels Inc.*, 24-2210 (3d Cir. April 27, 2026).

Third Circuit judges write dueling treatises on a choice-of-law issue that seldom arises in bankruptcy cases.

Third Circuit Judge Krause Believes State Choice of Law Always Applies in Bankruptcy

Yesterday, we reported on a Third Circuit opinion of practical significance in bankruptcy cases where Circuit Judge Thomas L. Ambro appears to have held that courts in the state of incorporation alone have authority to divest a corporate board of authority to file a bankruptcy petition, if New Jersey corporate law is representative of corporate law in other states.

From the same case, we next report two extraordinary concurring opinions by Circuit Judges Ambro and Cheryl Ann Krause that are *dicta* from top to bottom. On a question of almost purely academic interest, the two Third Circuit judges take divergent positions on whether state choice-of-law rules always apply in bankruptcy cases, or whether federal courts in some circumstances may devise their own standards to govern choice of law.

Both opinions read like treatises or casebooks on federal courts.

The Two Theories

Today, we report on the concurrence by Judge Krause, who believes that bankruptcy courts in all cases must follow the "forum state" rule about choice of law from a diversity case, *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487 (1941).

However, Judge Krause began her concurrence by saying, "I join the majority opinion in full," because "New Jersey law governs the authority of [the debtor's] board to exercise corporate authority, and the South Carolina Court did not — and likely could not — unilaterally divest the board of that authority."

Judge Krause then said she wrote separately "to address which choice-of-law rules govern in bankruptcy — an issue that both looms in the background of this case and … has divided courts for decades." She explained the two theories: the "forum state" rule in *Klaxon*, and the federal common law choice of law. In the case on appeal, there was no dispute because the two theories "converge," since the forum state was New Jersey and the debtor was a New Jersey corporation.

The Split

Federal courts most often face choice-of-law questions when sitting in diversity jurisdiction. In bankruptcy cases, Judge Krause said that the Third Circuit has not taken sides, although other circuits have arrived at “differing conclusions” in a split that has existed “for decades.”

Judge Krause said that the Eighth Circuit follows *Klaxon* in bankruptcy cases and applies the choice-of-law rules of the forum state, except when a federal interest requires a different result. In those cases, though, the Eighth Circuit believes it’s not a choice-of-law question; rather, it’s a rule of decision where federal law ousts state law.

The Ninth Circuit, and “possibly” the Fifth Circuit, Judge Krause said, reject *Klaxon* and require federal choice-of-law rules. The Second and Fourth Circuits employ a “hybrid approach” by applying *Klaxon* in the absence of a compelling federal interest.

Judge Krause devoted her 38-page opinion to explaining why “there is no basis to depart from the established rule from *Klaxon*, and, consistent with the Eighth Circuit’s approach, any conflict-of-laws issue is properly resolved as a matter of rule of decision, not choice of law.”

Reasons to Follow *Klaxon*

Judge Krause gave reasons for following *Klaxon*. First, she said that “parties find[ing] themselves wound up in a bankruptcy case should not work to alter the law that would otherwise govern their rights . . . . But adopting a choice-of-law rule unique to bankruptcy risks just that and would subject identically situated parties to different governing laws simply by virtue of one dispute occurring in bankruptcy court while the other unfolds in run-of-the-mill civil litigation.”

Second, Judge Krause cited the work of “renown[ed] scholars.” Third, extending *Klaxon* is consistent with *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938), and the Rules of Decision Act, 28 U.S.C. § 1652. When a provision in the Bankruptcy Code governs, “the Supremacy Clause obviates any choice-of-law analysis, for federal law always trumps conflicting state law.”

Critiquing the Other Circuits

Aside from the Eighth Circuit, which follows *Klaxon*, Judge Krause explained why, in her view, the Second, Fourth and Ninth Circuits demonstrated “an unwarranted suspicion of *Klaxon*’s relevance beyond diversity cases.” To begin with, federal jurisdiction “is not in itself a mandate” to follow federal law in all cases. By “reflexively employing a federal common law choice-of-law rule, the Ninth Circuit’s approach risks altering parties’ rights by selecting different law than would govern outside of bankruptcy.”

In the Second and Fourth Circuits, Judge Krause said, there can be “exceptional cases” where a “compelling federal interest” requires a federal common law choice-of-law rule. Neither circuit, she said, "has actually identified — much less confronted — such a situation." She said that *Butner v. United States*, 440 U.S. 48 (1979), "is not to the contrary."

Butner taught that property interests are defined by state law, unless a federal interest requires a different result. *Id*. at 55. Although *Butner* might seem to support the Second and Fourth Circuits, Judge Krause said, "*Butner* cannot reasonably be read to suggest that federal law provides the choice-of-law rule to decide among conflicting non-federal laws when it is those laws that provide the rule of decision."

Judge Krause summarized her critique of the other circuits as follows:

> [T]he Ninth Circuit's departure from *Klaxon* is misguided. As for the Second, Fourth, and Eighth Circuits, their approaches in practice always have, and always will, lead to the same result — *Klaxon* applies in bankruptcy, but federal law necessarily provides the rule of decision "when some federal interest requires a different result." [Citation omitted.] But by framing the question as choice-of-law instead of rule-of-decision and leaving the door open for a different choice-of-law rule in theory, the Second and Fourth Circuits invite needless litigation over *Klaxon*'s applicability and leave lingering uncertainty about which law will govern parties' disputes.

Judge Krause therefore believes that the "rule from *Klaxon* extends to bankruptcy cases." However, the "question of *Klaxon*'s applicability to bankruptcy has persisted for nearly 80 years."

Rather than "elide the question of which choice-of-law methodology to employ," Judge Krause saw a "responsibility not to perpetuate this uncertainty" but, "in the appropriate case, [to] resolve this question and give guidance to bankruptcy and district courts in our Circuit in a way that is consistent with the Bankruptcy Code, *Erie* and the Rules of Decision Act, and the policies underlying the grant[ing] of bankruptcy jurisdiction to federal courts."

Tomorrow

Tomorrow, we will report on Judge Ambro's concurrence with his own opinion where he differs from his colleague's belief that *Klaxon* should apply across the board in bankruptcy cases.

The opinion is *In re Whittaker Clark & Daniels Inc.*, 24-2210 (3d Cir. Sept. 10, 2025).

Judge Ambro reads Erie and Butner to mean there could be unusual cases where a bankruptcy court should apply federal choice-of-law rules and not state choice of law.

Circuit Judge Ambro Believes Bankruptcy Cases Could Use Federal Choice-of-Law Rules

Day before yesterday, we reported on the Third Circuit opinion where Circuit Judge Thomas L. Ambro held, among other things, that a "foreign" court's appointment of a receiver cannot deprive the corporate board of authority to file a bankruptcy petition. Yesterday, we recounted the concurrence by Circuit Judge Cheryl Ann Krause, who gave reasons in 38 pages of *dicta* for believing that *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487 (1941), should require bankruptcy courts to implement the forum state's choice-of-law rules across the board.

Today, we report on Judge Ambro's concurrence with his own opinion. He was "uncomfortable" with Judge Krause's views and believes there could be cases in which *Klaxon* should not govern in bankruptcy cases.

Judge Ambro began his concurrence by describing how the Supreme Court decided in *Klaxon* that *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938), requires employing state choice-of-law rules in diversity cases. He then posed the question, "What force, if any, does *Klaxon* have in bankruptcy, where the parties' primary rights and interests are often governed by state law?"

In the case on appeal, Judge Ambro said that the circuit was not required to answer the question because the parties agreed that New Jersey law applied with regard to a receiver's capacity for depriving a corporate board of authority to file a bankruptcy petition. His concurring opinion was an analysis of what the circuit's answer would have been were there no agreement on choice of law.

Erie and *Klaxon*

Judge Ambro described *Erie* as standing for "three basic propositions." First, there is no federal general common law. Second, "without a federal statute or constitutionally authorized federal common-law rule, the Rules of Decision Act, 28 U.S.C. § 1652, commands federal courts to apply the rules of decision of their forum states 'in cases where they apply.'"

Third, when a federal rule like the Federal Rules of Civil Procedure conflicts with state law, Judge Ambro said that "the Rules Enabling Act, 28 U.S.C. § 2072, not the Rules of Decision Act as construed by *Erie* and other cases, determines which law applies . . . . The Rules Enabling Act is also irrelevant for our purposes."

While *Erie* ended the idea of general federal common law, Judge Ambro said that "the Supreme Court has been unequivocal in recognizing that the *Erie* doctrine does not entirely displace federal common law." Citing Justice Brandeis in a decision handed down the same day as *Erie*, he said that "federal courts may still formulate special federal common law on issues of uniquely federal interest." *Hinderlider v. La Plata River & Cherry Creek Ditch Co.*, 304 U.S. 92, 110 (1938).

"Even after *Erie*," Judge Ambro said, "federal courts retain the power to promulgate special federal common-law rules when a strong federal interest requires such rules. Those cases, however, are rare."

The Circuit Split

Like Judge Krause, Judge Ambro laid out the circuit split. He described the Ninth Circuit as limiting *Klaxon* to diversity cases, thus requiring federal courts to apply federal choice-of-law rules in bankruptcy cases. He said that the Eighth Circuit "arguably held" that *Klaxon* applies in bankruptcy cases "without exception." The Second and Fourth Circuits "have held that *Klaxon* applies in federal bankruptcy proceedings unless a strong federal interest justifies creating federal choice-of-law rules as a matter of federal common law."

Explaining where he stood, Judge Ambro said,

> I believe that the Second and Fourth Circuits have it right. The Ninth Circuit is wrong because *Erie*, and thus *Klaxon*, is not limited to federal diversity jurisdiction. Whenever federal courts encounter an issue whose resolution is not a matter of federal law, the Rules of Decision Act compels them to use state substantive law, which includes choice-of-law rules. If the Eighth Circuit held that *Klaxon* applies without exception in federal bankruptcy cases, it is wrong as well.

"I believe it is wrong to conclude that *Erie* applies only in federal diversity cases," Judge Ambro said, because it applies to questions in federal court where the rule of decision is not federal law. He noted that questions arise in bankruptcy cases that are not based on federal law.

Agreeing with Judge Krause that "*Klaxon* applies in bankruptcy proceedings when addressing state-law questions," Judge Ambro said that the remaining question "is whether federal courts sitting in bankruptcy must *always* apply the forum state's choice-of-law rules when the underlying issue is governed by state law. That is where I part with our concurring colleague."

Addressing the five reasons underlying Judge Krause's analysis, Judge Ambro said that none of four "supports the claim that federal courts can never create choice-of-law rules in bankruptcy

— they support only the lesser claim that state choice-of-law rules will almost always apply." On that issue, he agreed.

Judge Ambro disagreed with Judge Krause's idea that "any federal interest strong enough to generate a federal choice-of-law rule would be explicit in the Bankruptcy Code itself; the absence of choice-of-law rules in the Code means there is never any such interest." He said that Judge Krause's "premise is faulty because it would apply with equal strength to the power of federal courts to create substantive common-law rules in bankruptcy."

The inability to craft substantive common-law rules in bankruptcy, Judge Ambro said, was rejected by the Supreme Court because *Butner v. United States*, 440 U.S. 48, 55 (1979), said, "'Property interests are created and defined by state law . . . [u]nless some federal interest requires a different result.'"

"At its core," Judge Ambro said, Judge Krause's "argument is merely that she cannot imagine a case in which a federal court would need to create a federal choice-of-law rule in bankruptcy. As she rightly notes, I cannot think of such a case either . . . . But this is not an argument that federal courts lack the authority to make choice-of-law rules in bankruptcy."

"If *Klaxon*'s application in bankruptcy becomes an issue," Judge Ambro said, he "would endorse the sensible, never-say-never approach of the Second and Fourth Circuits: Absent an 'overwhelming federal policy [that] requires us to formulate a choice-of-law rule as a matter of independent federal judgment, we adopt the choice-of-law rule of the forum state.'"

The opinion is *In re Whittaker Clark & Daniels Inc.*, 24-2210 (3d Cir. Sept. 10, 2025).

Reversing its prior decision after rehearing, the Third Circuit allowed a bankruptcy judge to interpret a confirmation decision made 12 years before by a district judge.

On Panel Rehearing, Third Circuit Permits Reopening a 22-Year-Old Case

Here's something you won't see again for years: The Third Circuit granted rehearing to reconsider a nonprecedential opinion handed down one year ago. In a split decision on August 22, the majority vacated last year's opinion and handed down a new decision with the polar opposite result. The majority reversed the prior opinion right down the line.

In his 32-page opinion for the majority, Chief Circuit Judge Michael A. Chagares broadened the ability of a bankruptcy court to reopen a chapter 11 case filed 22 years before. He also fortified the understanding of what a core proceeding is and the ability of a bankruptcy judge to interpret a confirmation order made by a different judge 15 years earlier. He even said that a bankruptcy judge has the right to interpret a decision by a district judge.

We will run three stories on the Third Circuit opinion. Today, we cover the circuit's opinion about the bankruptcy court's jurisdiction and discretion in reopening a chapter 11 case filed in 2003. Tomorrow, we will discuss the majority's conclusion that a finding in a 2010 confirmation order was *res judicata* and binding on a creditor.

On Monday, we will present the dissent by Circuit Judge Paul B. Matey, an interesting read. He describes the bankruptcy court as a "forum to assist federal judges . . . ."

Bankruptcy Court Finds *Res Judicata*

The debtor was a flooring manufacturer that had been operating since the 1880s. The products had contained asbestos. Facing almost 100,000 personal injury claims, the debtor filed a chapter 11 petition for the first time in 2003. The debtor had a former corporate sibling in the shipbuilding business.

As part of the plan for emerging from the first chapter 11 case, the debtor's insurer bought back its policies in a settlement that included an injunction barring anyone from bringing suit under the policies. As part of the settlement approved by the bankruptcy court, the debtor submitted a declaration saying that the shipbuilder had no responsibility for the asbestos claims.

After the settlement in bankruptcy court, the district court withdrew the reference and eventually confirmed a chapter 11 plan in 2010. The plan provided that confirmation would not release any liabilities under environmental law. The confirmation order nevertheless contained a finding that the shipbuilder had no liability for asbestos claims.

A neighboring landowner, whom we shall refer to as the creditor, had notice of the plan, the disclosure statement, the confirmation hearing and the confirmation order. The creditor did not appear at the confirmation hearing and did not object to the finding in the confirmation order that the shipbuilder had no asbestos liability. The plan went effective, and the district court referred the case once again to the bankruptcy court.

Seven years later in environmental remediation litigation, the creditor asserted claims against the shipbuilder.

The debtor filed a second chapter 11 petition in 2020 before a different bankruptcy judge. In the second bankruptcy, the shipbuilder filed an adversary proceeding against the creditor asserting that it had no environmental liability as a consequence of the finding in the 2010 confirmation order. Bankruptcy Judge Michael B. Kaplan of Trenton, N.J., granted summary judgment in favor of the shipbuilder, deciding that the shipbuilder's liability had been actually litigated in the first bankruptcy.

However, the creditor refused to dismiss the separate remediation suit against the shipbuilder. So, on motion by the shipbuilder, the bankruptcy court reopened the 2003 bankruptcy case, and the "old" case was transferred to Bankruptcy Judge Kaplan, who was presiding over the "new" case.

According to the majority opinion by Chief Circuit Judge Chagares, the bankruptcy judge decided that the shipbuilder's lack of liability was *res judicata* and bound the creditor as a consequence of the finding in the 2010 confirmation order. [Note: Throughout, Judge Chagares and the dissenter use the term *res judicata* rather than claim preclusion, so we shall also.]

The district court reversed on appeal, believing that the district court in the remediation litigation was in a better position to decide about the preclusive effect of the confirmation order. The first time around, the same Third Circuit panel affirmed in a nonprecedential opinion on August 1, 2024, by Circuit Judge Matey. To read the circuit's original opinion, click here. Judge Matey would become the dissenter after rehearing.

The shipbuilder moved for rehearing, which the panel granted and took under submission on June 12, 2025. With a dissent, the majority vacated the prior opinion on August 22 and reversed course. One of the judges on the original panel had taken inactive status. On the panel that heard reargument, he was replaced by Circuit Judge Cindy K. Chung.

Jurisdiction to Reopen

The majority first dealt with the bankruptcy court's jurisdiction and discretion to reopen the 2003 chapter 11 case.

On jurisdiction, Judge Chagares stated how the Third Circuit had "repeatedly held" that a bankruptcy court has jurisdiction to interpret its own orders. After confirmation, he said that bankruptcy courts retain "related to" jurisdiction over core matters like confirmation.

The creditor contended the bankruptcy court had no jurisdiction because the district court had entered the confirmation order. Judge Chagares rejected the argument, saying,

> [T]his distinction is of no significance because the District Court in this case entered the Confirmation Order while sitting in bankruptcy. Additionally, after the case was referred again to the Bankruptcy Court, it was the Bankruptcy Court, not the District Court, that was tasked with adjudicating the case.

Judge Chagares held that the "motion to reopen was plainly a core bankruptcy proceeding, which included disputes concerning the meaning of the Confirmation Order," because the shipbuilder had asked the Bankruptcy Court to "interpret and enforce" the confirmation order.

Notably, Judge Chagares rejected the creditor's contention that a later bankruptcy judge cannot reopen a case to interpret a different bankruptcy judge's order. He said, "The identity of the judge cannot be a jurisdictional prerequisite because the administrative needs of courts frequently require reassignment of cases."

Discretion to Reopen

Having found jurisdiction, Judge Chagares turned to the question of whether the bankruptcy court had abused discretion by reopening the 2003 case.

Judge Chagares observed that the bankruptcy judge had presided over a similar dispute in the newer case and that the district court had "no particular familiarity with the issues." He dismissed the idea that there was no reason to reopen the case when the outcome would not affect the debtor's estate. He said there was cause to reopen for the interpretation and enforcement of a previously approved settlement and confirmation order.

Judge Chagares found no abuse of discretion in the bankruptcy court's "well-reasoned decision to reopen bankruptcy proceedings."

Tomorrow

Tomorrow, we shall report on the majority's decision that the confirmation finding in 2010 was "*res judicata*" and bound the creditor.

The opinion is *In re Congoleum Corp.*, 23-1295 (3d Cir. Aug. 22, 2025).

The First Circuit sympathized with debtors whose discharges left them without a forum to pursue a lawsuit.

Dismissal or Discharge Doesn't Automatically End 'Related To' Jurisdiction, Circuit Says

A decision from the First Circuit demonstrates the principle that a bankruptcy court does not automatically lose "related to" jurisdiction when a bankruptcy case is dismissed or discharge is granted.

The March 4 opinion by Circuit Judge O. Rogeriee Thompson stands for the rule that the bankruptcy court's post-discharge or post-dismissal "related to" jurisdiction is a case- and fact-specific inquiry.

20 Years of Disputes and Litigation

A couple took down a mortgage in 2005 to purchase a home. After they defaulted in 2015, the bank agreed to consider accepting a short sale in lieu of foreclosure. The bank turned down the first three short sale offers but agreed to the fourth proposal. However, the debtors were unable to close before the bank's deadline.

The bank foreclosed and sold the home to the buyer who had made the fourth short sale offer. The bank obtained a deficiency judgment from the debtors amounting to some $115,000, prompting the couple to file a chapter 13 petition in 2017.

The litigation history after bankruptcy was lengthy and complex. Assume that the debtors sued the bank in bankruptcy court under Puerto Rico and federal law. While the adversary proceeding was pending, a relative died, giving the couple an inheritance sufficient to pay creditors in full.

The debtors filed a separate lawsuit against the bank in federal district court and a motion to withdraw the reference from the bankruptcy court, asserting a right to a jury trial. Now, it gets complicated, but we simplify.

The district court denied the motion to withdraw the reference and granted the bank's motion to dismiss the lawsuit in district court. The district court reasoned that comity and efficiency required having the same claims resolved in one court, the bankruptcy court. While the motion to dismiss was pending in district court, the bankruptcy court granted the debtors' discharges.

Following denial of the motion to withdraw the reference, the bankruptcy court, *sua sponte*, dismissed the adversary proceeding without prejudice, reasoning that the grant of discharges left the bankruptcy court bereft of "related to" jurisdiction. The debtors appealed, but the bank won in district court.

For reasons we don't need to explain, the debtors were able to appeal to the First Circuit, raising the question of whether the district and bankruptcy courts erred in failing to withdraw the reference and in dismissing for lack of jurisdiction.

Jurisdiction

We will skip over Judge Thompson's explanation for how there was appellate jurisdiction and how the debtors preserved issues for appeal. Addressing the merits, we begin with "related to" jurisdiction under 28 U.S.C. § 1334(b).

"In general," Judge Thompson said, "'related to' adversary proceedings will be dismissed following the termination of the underlying bankruptcy proceedings . . . . But this rule is not a command set in stone, and nothing in the Bankruptcy Code requires the automatic dismissal of a related adversary proceeding following the termination of an underlying bankruptcy case."

Citing the Second Circuit, Judge Thompson held that the bankruptcy court erred in "finding that the court's previously vested jurisdiction had automatically dissipated following the [debtors'] discharge." She went on to say that "we (like other courts) specifically declined to adopt a blanket rule that jurisdiction automatically terminates following the dismissal of an underlying bankruptcy petition."

"Instead," Judge Thompson cited the First Circuit in saying that "we concluded that the question of a bankruptcy court's post-dismissal (or discharge) jurisdiction is 'a case- and fact-specific inquiry.'" Elaborating, she said "that the case-specific inquiry should be gauged by several familiar factors: judicial economy, convenience to the parties, fairness, and comity." However, she "decline[d] to decide how those factors should be applied."

Nonetheless, Judge Thompson added commentary indicating that the bankruptcy court should seriously consider finding post-discharge jurisdiction. She said, "[T]he bankruptcy court was primed to exercise its jurisdiction and accompany its 65 findings of fact with conclusions of law for the district court's review."

Withdrawal of the Reference

The debtors had made two motions to withdraw the reference. The district court had denied the first as being untimely and denied the second because the first was untimely.

Judge Thompson said that the district court's "opinion [was] ambiguous as to whether it considered the changes in that status following the rejection of the [debtors'] first motion for withdrawal." She found "no authority . . . for the proposition that once a party's motion for withdrawal is deemed untimely, that party is forever barred from filing a timely motion in the future."

Instead, Judge Thompson said that "the district court should have considered the present status of proceedings in the bankruptcy court." Remanding, she said, "[W]e expect the district court to address the [debtors'] request for a jury trial." Although not specifying how the district court should rule on withdrawal following remand, she said, "[T]he fact remains that the [debtors] sought a withdrawal of reference on this basis, and the district court did not engage their request."

Judge Thompson vacated and remanded for the bankruptcy court to reconsider the question of subject matter jurisdiction and for the district court to reconsider withdrawal of the reference.

The opinion is *Guallini-Indij v. Banco Popular de Puerto Rico (In re Guallini-Indij)*, 23-1705 (1st Cir. March 4, 2026).

ROCHELLE'S DAILY WIRE

Fifth Circuit opinion could be understood to mean there is no subject matter jurisdiction in bankruptcy court after confirmation on an executory contract that was assumed but revised.

Fifth Circuit Comes Down Hard on Tenuous Post-Confirmation Jurisdiction

Ruling that the bankruptcy court had no subject matter jurisdiction for a dispute that arose after confirmation, the Fifth Circuit based its new holding on *Craig's Stores of Tex., Inc. v. Bank of La. (In re Craig's Stores of Tex., Inc.)*, 266 F.3d 388 (5th Cir. 2001). There, the appeals court said that "bankruptcy court jurisdiction does not last forever" and is reserved for "matters pertaining to the implementation or execution of the plan." *Id*. at 389, 390.

As Circuit Judge Edith H. Jones said in the new decision, *Craig's Stores* "held that a former debtor's state law dispute that arose a year after confirmation was not within the bankruptcy court's 'related-to' jurisdiction." *Id*. at 391.

In her opinion on November 13, Judge Jones cited *Natixis Funding Corp. v. GenOn Mid-Atl. L.L.C. (In re Mid-Atl. Dev., L.L.C.)*, 42 F.4th 523, 534 (5th Cir. 2022), to mean that the "scope of a bankruptcy court's related-to jurisdiction narrows, however, after a reorganization plan is confirmed, and the reorganized debtor is re-vested with its property and operates outside of bankruptcy court superintendence."

Cautioning courts not to rely on *GenOn* to expand post-confirmation jurisdiction, Judge Jones quoted *GenOn* itself for saying that it "'lives at the limit of related-to jurisdiction'" and that "'[f]ew disputes between non-debtors qualify.'" *Id*. at 535, 538. She explained how *GenOn* found "related to" jurisdiction because the dispute "revolved around a settlement agreement that was expressly contemplated by the debtor's reorganization plan; the settlement had been 'enshrined' in the plan by the bankruptcy court; and the settlement had not yet become final when the litigation ensued." *Id*. at 356. To read ABI's report on *GenOn*, click here.

This writer interprets Judge Jones's opinion to mean that a bankruptcy court lacks subject matter jurisdiction to adjudicate disputes regarding executory contracts that were modified in the process of assumption, because they represent contracts that did not exist before filing. It is less clear, but the opinion also might mean there is no subject matter jurisdiction in the Fifth Circuit to resolve disputes arising after confirmation with regard to assumed executory contracts.

Because everything that occurred becomes a nullity when there was no subject matter jurisdiction, parties should proceed with caution in courts in the Fifth Circuit when bringing post-confirmation disputes into bankruptcy court unless there is a clear jurisdictional nexus.

Circuit Judge Carolyn Dineen King was on the panel. She and Judge Jones are among the most prolific authors of important bankruptcy opinions in the Fifth Circuit. Their opinions ought be given special deference, in this writer's opinion.

Now for a discussion of the new case itself.

Post-Confirmation Assumption and Modification

The chapter 11 debtor was an oil and gas producer. The facts and procedural posture of the case almost defy comprehension. Suffice it to say that the plan allowed the debtor, after confirmation, to assume or reject executory contracts without court authorization. During the case, however, the debtor assumed the executory contract with a so-called midstream services provider, which we shall refer to as the appellant.

At confirmation, executory contracts with other service providers had not been assumed or rejected. We shall refer to those service providers as the appellees. There was an adversary proceeding between the debtors and the appellees involving the appellees' objections to the rejection of executory contracts. The appellant was not a party in the adversary proceeding.

More than a year after confirmation, the debtor settled the adversary proceeding with the appellees. They filed a motion to dismiss the adversary proceeding, but did not call on the bankruptcy court to approve the underlying settlement because the plan allowed the debtor to assume contracts without court approval.

The appellant had filed a lawsuit in state court against the debtor and appellees asserting state law claims that the settlement interfered with its rights under its assumed executory contract. The suit was removed to bankruptcy court, where the bankruptcy judge found post-confirmation "related to" jurisdiction.

Ultimately, the bankruptcy court dismissed the appellant's suit on the merits on several grounds related to the plan. The district court affirmed, bringing the dispute to the Fifth Circuit along with the appellant's contention that the bankruptcy court never had subject matter jurisdiction.

No Jurisdiction for Modified Executory Contracts

Citing *Craig's Stores* as the circuit's "seminal opinion on post-confirmation jurisdiction," Judge Jones paraphrased *GenOn* to mean that the "scope of a bankruptcy court's related-to jurisdiction narrows, however, after a reorganization plan is confirmed, and the reorganized debtor is re-vested with its property and operates outside of bankruptcy court superintendence."

Judge Jones distinguished *GenOn* because the debtor in the appeal before her had authority without court approval to assume or reject executory contracts without court approval. In *GenOn*, by way of contrast, the settlement had been "enshrined" in the plan. Because the bankruptcy court had not approved the settlements between the debtor and the appellees, she said that the bankruptcy court performed nothing "other than a ministerial function in entering" the dismissal order.

The post-confirmation settlements between the debtor and the appellees, Judge Jones said, "are the product of integrated, multiparty, post-confirmation negotiations. Together, they significantly modified the relationships that existed pre-bankruptcy, and they are *in toto* a post-bankruptcy confection." They were not, she said, executory contracts under the plan's definition "because they did not exist before the Plan was confirmed."

Judge Jones said that the settlement "represented a new, fully integrated set of midstream agreements" and that referring to them as assumed executory contracts "would obliterate the distinction between pre- and post-confirmation related-to jurisdiction."

Reversing the bankruptcy court for lack of subject matter jurisdiction, Judges Jones said that the debtor's plan "did not explicitly incorporate changes to or seek to manage the debtors' midstream agreements" with the appellees. "Instead," she said, the reorganized debtor "exploited its post-confirmation free rein to litigate, compromise, settle, and alter the midstream contracts without bankruptcy court involvement." She remanded with instruction to remand to the state court.

Observations

One might be tempted to read Judge Jones's opinion narrowly based on the peculiar facts of the case. This writer recommends resisting the urge, though, because Judge Jones emphasized how *GenOn* represents the outer limits of jurisdiction. Recall that there was jurisdiction in *GenOn* because the settlement had been "enshrined" in the plan.

Reading *GenOn* together with Judge Jones's new opinion, the Fifth Circuit may be saying that obligations must have been created entirely before confirmation to confer post-confirmation jurisdiction. It is possible that contracts assumed after confirmation, but not modified, might not confer post-confirmation jurisdiction on the bankruptcy court.

A finding on appeal of a lack of subject matter jurisdiction means that everything that previously occurred was a nullity. Therefore, it may be prudent in the Fifth Circuit not to stretch the rubber band when it comes to post-confirmation jurisdiction.

The opinions are those of the writer, not ABI.

The opinion is *Carnero G&P LLC v. SN EF Maverick LLC (In re Sanchez Energy Corp.)*, 24-20207 (5th Cir. Nov. 13, 2025).

The majority on a Third Circuit panel decided that a confirmation order many years earlier prevented one nondebtor from suing another nondebtor on an issue that wouldn't affect the debtor's estate but did entail interpreting the confirmation order.

Third Circuit: Confirmation Order Was *Res Judicata* Between Third Parties

Yesterday, we reported the Third Circuit's 2/1 decision on August 22 upholding the bankruptcy court's jurisdiction and exercise of discretion in reopening a 2003 case to interpret and enforce a chapter 11 confirmation order entered by a *district court* in 2010.

The debtor's chapter 11 plan and confirmation order in 2010 dealt with asbestos liability. The confirmation order included a finding that the debtor's affiliate, a shipbuilder, had no liability for asbestos. Years later, a creditor sued the shipbuilder to share the cost of asbestos remediation.

The bankruptcy court in the debtor's second bankruptcy reopened the 2003 case and decided that the 2010 confirmation order was *res judicata* and barred the creditor's assertion of remediation costs against the shipbuilder.

Today, we deal with the portion of the majority opinion by Chief Circuit Judge Michael A. Chagares concerning *res judicata*. [Note: Both Judge Chagares and the dissenter use the term *res judicata*, not claim preclusion, and so shall we.]

Sufficient Notice

The creditor contended it had not received adequate notice and that *res judicata* therefore could not apply. The creditor asserted that its nine boxes of records from the 2003 bankruptcy did not contain the motion to approve the settlement in which the shipbuilder was held to have no asbestos liability. However, the debtor's application for the settlement showed the creditor on two different service lists.

Judge Chagares found that "the record establishes by a preponderance of the evidence that [the creditor] was served with the motion for approval" of the settlement and the settlement order.

The creditor conceded that it had notice of the plan, the disclosure statement, the confirmation hearing and the confirmation order but argued that notice of the finding was not "conspicuous." To the contrary, Judge Chagares said that a "review of the draft Confirmation Order, which included the [finding of no liability], would have alerted [the creditor] to the fact that the . . . Settlement included a determination of [the shipbuilder's] liability."

Judge Chagares said that the creditor's due process rights were "more than satisfied."

The Finding Covered Environmental Liabilities

Next, Judge Chagares addressed the question of whether the confirmation finding bound the creditor in the later remediation litigation because the finding said nothing about environmental liabilities. He quoted the finding, which said that the shipbuilder had "no responsibility for any of the liabilities of" the debtor. He went on to say that the finding was "not a third-party release but rather a determination that [the shipbuilder] was never responsible for the [debtor's] liabilities." He noted how the finding never used the word "release," and that the plan explicitly said there were no third-party releases.

Judge Chagares decided that the circuit "must enforce the Confirmation Order's plain, unambiguous meaning: [the shipbuilder] inherited none of the [debtor's] liabilities."

Res Judicata Applied

Having held that the confirmation finding was binding on the creditor, Judge Chagares analyzed whether it was *res judicata*. Quoting the Third Circuit, he said that *res judicata* applies to "'(1) a final judgment on the merits in a prior suit involving (2) the same parties or their privies and (3) a subsequent suit based on the same cause of action.'" Quoting the Supreme Court, he said that "no party may 'relitigat[e] issues that were or could have been raised in' an action resulting in 'a final judgment on the merits of the action.'"

Judge Chagares said that the creditor was a party in the bankruptcy proceedings and "had an opportunity" to litigate the finding, which became a final judgment binding on all creditors. He added that "the application of *res judicata* to confirmation orders occupies a position of 'high importance in the bankruptcy context' because all parties must be able to rely on a confirmation order without worry[ing] that the order is subject to change following post-confirmation challenges by dissatisfied creditors."

Because it was a creditor with notice, Judge Chagares said that the creditor's "lack of participation is irrelevant; 'a confirmation order is *res judicata* as to all issues decided or which could have been decided at the hearing on confirmation.'" He added that the finding in the confirmation order "resolved the same issue" as the one raised in the creditor's remediation lawsuit.

Judge Chagares held that the finding in the confirmation order "thus binds [the creditor] and has *res judicata* effect." He summarized the majority's holdings as follows:

> The Bankruptcy Court did not err in exercising its jurisdiction to reopen the bankruptcy case because it was asked to interpret and enforce the Confirmation Order, which was entered by a court sitting in bankruptcy. Because the . . . Finding conclusively determined that [the shipbuilder] did not inherit the liabilities of the [debtor] and was a final order binding [the creditor], which had notice of the confirmation and . . . Settlement proceedings, the Bankruptcy Court also did not err in holding that the . . . Finding barred [the creditor's] claims against [the shipbuilder].

On Tuesday, we cover the dissent.

The opinion is *In re Congoleum Corp.*, 23-1295 (3d Cir. Aug. 22, 2025).

The dissenter on rehearing believes there are narrow grounds for reopening a closed bankruptcy case.

Third Circuit Dissenter Says that Bankruptcy Judges 'Assist' Article III Judges

Third Circuit Judge Paul B. Matey dissented from his colleagues who held that a *bankruptcy judge* more than a decade later had the jurisdiction and authority to interpret and enforce a confirmation order signed by a *district judge* after withdrawal of the reference. Remember, the majority had granted panel rehearing and basically reversed a nonprecedential opinion from the year before.

Judge Matey said the panel "reconsidered when a few academics warned the sky was poised to fall." The sky had not fallen, "but still the panel changes course and empowers a congressionally created adjudicative body to wrest jurisdiction from an Article III court."

Judge Matey "respectfully" dissented because "Congress created the bankruptcy forum to assist federal judges, not usurp the Article III prerogative.

The Historical Power to Reopen

Judge Matey traced the history of the bankruptcy court's power to reopen closed cases and said that Congress did not write "on a clean slate" in 1978 with the adoption of the Bankruptcy Code. He began with the Bankruptcy Act of 1898 and said it allowed reopening a case that had not been "fully administered."

In 1938, the reopening power was expanded to allow reopening for "cause shown." "But broader did not mean boundless," Judge Matey said, "and interpretations soon agreed that cause existed when the bankruptcy estate had not been fully administered — much the same circumstances under which reopening was authorized under the 1898 Act."

Consequently, Judge Matey said, "courts allowed reopening when a debtor concealed assets in the bankruptcy or the assets were previously unreachable." In 1973, he explained, the Bankruptcy Rules added "other good cause," a concept carried over in the 1978 Bankruptcy Code. However, he interpreted the advisory committee's note to mean that "the drafters saw no need to expand the reopening power or remove its connection to administration of the bankruptcy estate, acting narrowly to clarify that reopening was proper to provide relief to the debtor."

"In sum," Judge Matey said, "section 350(b) incorporates the unbroken understanding of a restricted reopening power recognized for nearly ninety years." Section 350(b) provides, "A case may be reopened in the court in which such case was closed to administer assets, to accord relief to the debtor, or for other cause.

More Recent Precedent

"Our precedent does not disturb this conclusion," Judge Matey said. For instance, he said, "we have affirmed bankruptcy reopening for other cause under section 350(b) . . . to ensure [that] active state court actions did not intrude on federal bankruptcy cases."

However, Judge Matey said, "those cases cannot be read to countenance a bankruptcy judge wresting jurisdiction from an Article III court competent and capable of interpreting an order collateral to the bankruptcy."

Judge Matey also disagreed with the majority's belief "that the Bankruptcy Court was 'best suited' to consider the motion to reopen." The 2010 confirmation order, he said, "was entered by the District Court exercising its supervisory authority over the bankruptcy judge following a series of errors, leaving the trial judge well-suited to confirm its meaning."

In conclusion, Judge Matey said,

> Today's result stymies the District Court's constitutional and statutory authority while commanding future judges to make way for the "experts." Congress did not promote such protectionism from Article III officials and "the word 'cause' is too weak a reed upon which to rest so weighty a power." *Czyewski v. Jevic Holding Corp.*, 580 U.S. 451, 466 (2017).

Observations

In a footnote citing the withdrawal power of the district court under 28 U.S.C. § 157(d), the majority said, "we respectfully disagree with our dissenting colleague that our holding permits bankruptcy courts to usurp the Article III authority of district courts."

Prof. Ralph Brubaker provided ABI with the following commentary:

> Neither a bankruptcy court nor a district court sitting in bankruptcy can make a factual finding on a third-party claim between two nondebtors, much less enter a binding judgment on that claim, if that claim was never asserted in a way that would actually invoke the court's subject-matter jurisdiction over that claim, *i.e.*, by filing an adversary proceeding that names and serves the party against whom that third-party claim is being made. Bankruptcy discharge is an exception to that principle,

but the panel majority in the *Congoleum* case explicitly held that the confirmed plan did not purport to "release" or discharge the claim at issue.

Prof. Brubaker is the James H.M. Sprayregen Professor of Law at the University of Illinois College of Law.

The opinion is *In re Congoleum Corp.*, 23-1295 (3d Cir. Aug. 22, 2025).

ROCHELLE'S DAILY WIRE

Failure to attach the judgment to the notice of appeal is not 'so egregious' as to warrant dismissal of the appeal.

Nothing Besides Filing the Notice of Appeal Is Jurisdictional, Fifth Circuit Says

Failing to attach a copy of the judgment to the notice of appeal isn't jurisdictional and isn't grounds in itself for dismissing an appeal, the Fifth Circuit said in a November 17 opinion.

In a lawsuit in bankruptcy court by one creditor against another creditor, the appellants filed a notice of appeal on time. However, the appellants did not attach a copy of the judgment to the notice of appeal, as required by Bankruptcy Rule 8003(a)(3)(B).

The clerk gave the appellants a deadline for filing a corrected notice of appeal. Ten days after the deadline and 21 days after entry of the judgment, the appellants filed a corrected notice of appeal, this time including the judgment.

The appellee filed a motion to dismiss the appeal. The district court dismissed the appeal for lack of jurisdiction, citing the appellants' failure to attach the judgment before the deadline. Alternatively, the district court dismissed the appeal as an exercise of discretion, based on the appellants' failure to comply with the Bankruptcy Rules and the deadline for amending the notice of appeal.

The appellants appealed and won reinstatement of the appeal in an opinion by Circuit Judge Irma Carrillo Ramirez.

What's Jurisdictional and What's Not

Appellate jurisdiction is conferred by 28 U.S.C. § 158(c)(2), which provides,

> An appeal . . . shall be taken in the same manner as appeals in civil proceedings generally are taken to the courts of appeals from the district courts and in the time provided by Rule 8002 of the Bankruptcy Rules.

In turn, Bankruptcy Rule 8002(a)(1) requires the filing of a notice of appeal within 14 days from the entry of judgment. The Fifth Circuit held that "the time limit [in Rule 8002] is jurisdictional" because 28 U.S.C. § 158 "expressly requires that the notice of appeal be filed under the time limit provided in Rule 8002." *In re Berman-Smith*, 737 F.3d 997, 1003 (5th Cir. 2013).

Parsing the rules further, Judge Ramirez cited Bankruptcy Rule 8003(a)(3)(B) for requiring that the notice of appeal "be accompanied by the judgment — or the appealable order or decree — from which the appeal is taken."

"This is not a jurisdictional prerequisite because," Judge Ramirez said, "unlike Rule 8002, 'Rule 8003(a)(3)(B) does not follow from a clear federal statute.' *In re Serta Simmons Bedding, L.L.C.*, 125 F.4th 555, 575 (5th Cir. 2024), *as revised* (Jan. 21, 2025), *as revised* (Feb. 14, 2025) (citation modified)." To read ABI's report on *Serta Simmons*, click here and here.

Judge Ramirez continued:

> "Since a failure to attach the appealed-from judgment is not a failure to timely file the notice of appeal, such a failure does not mandate dismissal." *Id.; see*, *e.g.*, *In re Mahadevan*, 2024 WL 3292744, at *1 (5th Cir. 2024).

Because the appellant had filed the notice of appeal before the deadline, Judge Ramirez held that "the district court had jurisdiction over the appeal."

No Abuse of Discretion

In addition to basing dismissal on the appellants' failure to file the judgment on time, the district court dismissed the appeal as a matter of discretion. The appellants contended that the district court abused its discretion.

Addressing discretion, Judge Ramirez turned to Bankruptcy Rule 8003(a)(2), entitled "Failure to Take Any Other Step." It provides that an "appellant's failure to take any step other than timely filing a notice of appeal does not affect the appeal's validity, but is ground only for the district court . . . to act as it considers appropriate, including dismissing the appeal."

"The rule makes clear that, other than an untimely notice of appeal which mandates dismissal, the district court has the authority to dismiss an appeal for infractions of the bankruptcy rules," Judge Ramirez said, citing the Fifth Circuit. She went on to say that "dismissal is typically unwarranted for harmless bankruptcy rule violations, and parties should not invariably suffer for the errors of counsel."

In exercising discretion, Judge Ramirez quoted the Fifth Circuit and said:

> [D]istrict courts should consider, among other things, "what sanctions are appropriate, the prejudicial effect of delay on the appellees, and whether the appellant has exhibited 'obstinately dilatory conduct.'"

In the case on appeal Judge Ramirez observed that "the district court did not consider any sanction short of dismissal," again citing *Serta Simmons*. She noted how the district court "found that dismissal was warranted because [the appellants] were sophisticated parties who had appealed other orders in the bankruptcy case, and . . . provided no reason for not timely correcting the deficient notice of appeal despite receiving notice and an opportunity to do so."

In addition, Judge Ramirez noted how the deficiency notice from the clerk did not warn about dismissal. Furthermore, the appellee "does not assert that it suffered any injury from the delayed filing other than the enforcement of the bankruptcy court's judgment."

Because dismissal is an "extremely severe sanction," Judge Ramirez quoted the Fifth Circuit for saying that dismissal "should 'be reserved for the most egregious of situations.'" In the case on appeal, she could not say that the failure to attach a copy of the judgment to the notice of appeal "was so egregious as to merit the district court's dismissal of the appeal."

Finding abuse of discretion, Judge Ramirez reversed and remanded for further proceedings consistent with the opinion. She declined to address the merits of the appeal.

The opinion is *Royal Street Bistro LLC v. Arrowhead Capital Finance Ltd. (In re Royal Street Bistro LLC)*, 24-30732 (5th Cir. Nov. 17, 2025).

An otherwise enforceable arbitration agreement won't be enforced in bankruptcy if there would be a 'severe conflict' with the purposes of the Bankruptcy Code.

Arbitration Order Given Preclusive Effect Didn't Compel Arbitration in Bankruptcy

Although a prior order in state court compelling arbitration had preclusive effect under New York law on collateral estoppel, the bankruptcy court properly denied a motion to compel arbitration of dischargeability, according to District Judge Ramón E. Reyes, Jr., of Brooklyn, N.Y.

The debtor was an owner of a business along with another individual whom we shall refer to as the creditor. When disputes arose, a rabbinical arbitrator directed the debtor to grant access to corporate books and records. The debtor also filed lawsuits against the creditor in state court. The state court judge ordered arbitration. The arbitration continued for 11 sessions but did not conclude before the debtor filed a chapter 11 petition, automatically halting the arbitration.

In bankruptcy court, the creditor began an adversary proceeding for a declaration that the debt was nondischargeable under Sections 523(a)(2), (4) and (6). The creditor also filed a motion to compel arbitration and modify the automatic stay. Bankruptcy Judge Nancy Hershey Lord of Brooklyn decided that the state court's order compelling arbitration was entitled to preclusive effect under the doctrine of collateral estoppel, a/k/a issue preclusion.

Nevertheless, Judge Lord denied the motions to compel arbitration and modify the stay. The creditor appealed, but District Judge Reyes affirmed in an opinion on September 17.

Preclusive Effect

Employing *de novo* review, Judge Reyes analyzed the preclusive effect of the order from state court compelling arbitration.

Under the New York doctrine of collateral estoppel, the order compelling arbitration would have preclusive effect if (1) the issues on both proceedings were identical; (2) the issue in the prior proceeding was actually litigated; (3) there was a full and fair opportunity to litigate in the prior proceeding; and (4) the issue previously litigated was necessary to support a valid and final judgment.

Like the bankruptcy court, Judge Reyes decided that the arbitration order from state court "meets New York's finality requirement for collateral estoppel purposes."

Standard of Review

Although the arbitration order was entitled to preclusive effect, Judge Reyes turned to the question of "whether arbitration should nonetheless be compelled in the context of this bankruptcy proceeding" under the Federal Arbitration Act, 9 U.S.C. § 1, *et seq*.

Judge Reyes began by quoting the Supreme Court for having said "that 'like any statutory directive, the Arbitration Act's mandate may be overridden by a contrary congressional command.' *Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 227 (1987)." In turn, the Second Circuit requires the court to decide whether the matter is core or noncore. *In re Anderson*, 884 F.3d 382, 387–88 (2d Cir. 2018). If it's core, the court then must decide whether arbitration would create a "severe conflict" with the purposes of the Bankruptcy Code. *Id*.

The Second Circuit also decided that the analysis of core or noncore is reviewed *do novo*, while a decision to enforce an arbitration agreement is reviewed for abuse of discretion.

Core and Severe Conflict

Given that dischargeability is on the nonexclusive list of core proceedings in 28 U.S.C. § 157(b)(2)(I), Judge Reyes quickly concluded that the adversary proceeding on dischargeability was core. He then analyzed whether "compelling arbitration would create the kind of 'severe conflict' with the Bankruptcy Code that permits overriding the strong federal policy in favor of arbitration."

Judge Reyes noted how the Second Circuit has declined to compel arbitration "where the claim at issue was 'integral to the Bankruptcy Code's central purposes.'" For instance, an insurance coverage dispute was core when insurance was the most important asset of the estate. Similarly, "the Second Circuit found that arbitration of a discharge injunction claim would 'seriously jeopardize a particular core bankruptcy proceeding.'" *Anderson*, *supra,* 884 F.3d at 390.

Judge Reyes identified the "same concern" regarding dischargeability. He cited decisions from the Fourth and Ninth Circuits affirming denial of motions to compel arbitration of dischargeability complaints and held "that compelling arbitration here would create a severe conflict with the Bankruptcy Code."

On abuse of discretion, Judge Reyes said that the existence of a valid arbitration agreement "does not render the Bankruptcy Court's decision an abuse of discretion." He affirmed denial of the creditors' motions to compel arbitration and modify the automatic stay.

The opinion is *Reiner v. Paneth*, 24-1402 (E.D.N.Y. Sept. 17, 2025).

When a plan's meaning is clear, there's no post-confirmation subject matter jurisdiction to decide disputed facts that would determine whether the plan applies to a dispute between third parties.

Under *Travelers*, a Dispute on a Plan's Coverage Doesn't Necessarily Convey Jurisdiction

Just because you can doesn't mean you should. And, just because you should doesn't mean you can.

That's the teaching from an opinion by Bankruptcy Judge Craig T. Goldblatt of Delaware. His June 4 decision shows that a dispute can be so tangential to a confirmed chapter 11 plan that the bankruptcy court lacks subject matter jurisdiction.

Judge Goldblatt could have abstained under U.S.C. § 1334(c). Properly, though, he found no subject matter jurisdiction under 28 U.S.C. § 1334(a) and (b).

The chapter 11 debtor installed solar panels on homes, purportedly leasing the solar panels to the homeowners. In chapter 11, the debtor sold all assets. The confirmed chapter 11 plan said that executory contracts and leases that had not been assumed would be rejected on confirmation.

After confirmation, a homeowner surfaced to claim that the lease on her home had not been assumed and therefore had been rejected. Indisputably, the lease had not been assumed.

Assuming it were a rejected true lease and the debtor's successor didn't elect to remove the panels, a homeowner whose lease was automatically rejected would own the panels with no obligation to make lease payments to the debtor or anyone else.

By motion, a homeowner with a lease not assumed wanted Judge Goldblatt to declare that the lease had been rejected.

The plan administrator objected, contending that the lease had been assigned by the debtor six years before bankruptcy to a nondebtor subsidiary used to obtain financing. The plan administrator took the position that the buyer became the lessor indirectly by having purchased the nondebtor subsidiary and other assets.

As he was obliged to do, Judge Goldblatt identified subject matter jurisdiction as a question, reviewed the parties' supplemental briefs and devoted his 18-page decision to explaining why there was no jurisdiction.

The Factual Question Underlying Jurisdiction

"[T]he only serious candidate for jurisdiction," Judge Goldblatt said, was the debtor's contention "that the determination that the lease was rejected seeks an interpretation or enforcement of the plan." But it was "not a case in which the parties are bringing the Court conflicting interpretations of the plan or confirmation," Judge Goldblatt said. Rather, everyone agreed that the plan rejected all leases that had not been assumed, and everyone agreed that the homeowner's lease had not been assumed.

Still, both sides wanted Judge Goldblatt to determine whether the lease had been assigned before bankruptcy to decide whether the court had subject matter jurisdiction. "But in order to decide that factual question, there needs to be a basis for subject-matter jurisdiction over the question," the judge said.

If the debtor's motion was "in fact one to enforce the confirmation order," Judge Goldblatt said, he would have "little trouble with the proposition that it falls within the Court's subject-matter jurisdiction."

No Dispute About the Plan's Meaning

To resolve the question of subject matter jurisdiction, Judge Goldblatt took counsel from two decisions, one from the Supreme Court and another from the Third Circuit.

The *Travelers* decision from the Supreme Court in 2009 involved the *Johns Manville* reorganization confirmed in 1986. *See Travelers Indem. Co. v. Bailey*, 557 U.S. 137 (2009). A dispute arose years later in bankruptcy court involving the interpretation of the breadth of an injunction in the plan protecting insurance companies from further liability after their contributions to fund the plan.

Reversing the Second Circuit, Judge Goldblatt explained how the Supreme Court found subject matter jurisdiction in the bankruptcy court because "there was an ambiguity in the 1986 injunction that needed to be addressed."

The relevant Third Circuit decision was *In re Lazy Days' RV Center Inc.*, 724 F.3d 418 (3d Cir. 2013), where the circuit upheld a finding of jurisdiction. "The point" of the decision, Judge Goldblatt said, "was that the question the parties brought to the bankruptcy court was 'a dispute regarding the Settlement Agreement it had previously confirmed.'"

In both cases, Judge Goldblatt said, “there was language in the bankruptcy court’s order that was either ambiguous or needed to be enforced.” Here, he said, “everyone agrees what this Court’s confirmation order does. It rejects every executory contract held by the debtors as of the effective date.”

In the case before him, Judge Goldblatt said that “the question [is] whether the debtors had actually assigned the lease [before bankruptcy] such that it never came into the bankruptcy estate and therefore was never rejected.” The factual issue, he went on to say, “is just too far removed from any question about the meaning of the plan or confirmation order for the dispute actually to be one over the meaning of the plan or confirmation order.”

Judge Goldblatt dismissed the homeowner’s motion for lack of subject matter jurisdiction because “the only parties with an economic stake are non-debtors and . . . no party is asking this Court to clarify or enforce any provision of the plan or confirmation order.”

The opinion is *In re SunPower Corp.*, 24-11649 (Bankr. D. Del. June 4, 2026).

Because the estate disappears on confirmation, there's no effect on the estate and therefore no subject matter jurisdiction for lawsuits based on breach of contract occurring before filing.

No Post-Confirmation Jurisdiction to Sue for Breach of Contract or to Collect Receivables

For a second time in six weeks in the same chapter 11 case, Bankruptcy Judge Craig T. Goldblatt has written an exhaustive opinion designed to give greater clarity to times when the bankruptcy court will or will not have post-confirmation subject matter jurisdiction over a lawsuit.

In his new opinion on July 23, Judge Goldblatt teaches why there is neither "arising in" nor "related to" jurisdiction for a reorganized debtor to prosecute a lawsuit in bankruptcy court to collect an account receivable or assert a claim for breach of contract that arose before the chapter 11 filing.

In his prior opinion on June 4, Judge Goldblatt explained why the bankruptcy court did not have post-confirmation subject matter jurisdiction to preside over a lawsuit between nondebtors that had no effect on the estate after confirmation. *In re SunPower Corp.*, 24-11649, 2026 BL 208252 (Bankr. D. Del. June 4, 2026). To read ABI's report, click here.

Notably, Judge Goldblatt concluded on June 4 that bankruptcy courts may not exercise supplemental jurisdiction under 28 U.S.C. § 1367.

Anyone with a matter involving post-confirmation jurisdiction should begin research by reading Judge Goldblatt's new, 43-page opinion in full text. Fortunately for readers, Judge Goldblatt summarized his holdings in the first six pages.

The Post-Confirmation Lawsuits

The chapter 11 debtor installed solar panels on homes, purportedly leasing the solar panels to the homeowners. In chapter 11, the debtor sold all assets and confirmed a plan. The plan conveyed all remaining assets and claims either to the reorganized debtor or to a liquidating trust.

After confirmation, the plan administrator sued two entities that had been the debtor's authorized dealers. The dealers had filed proofs of claim for $5 million to $10 million.

The plan administrator's lawsuit included claims for the turnover of about $500,000 in accounts receivable. Other claims in the complaint included breach of contract, disallowance of the claims and recovery of preferences.

The defendants filed a motion to dismiss for lack of post-confirmation subject matter jurisdiction. The defendants won the motion to dismiss the claims for breach of contract and a declaration that the receivables were owing.

Not 'Core'

Judge Goldblatt was addressing the question of whether the bankruptcy court after confirmation had "arising in," "arising under" or "related to" jurisdiction under 28 U.S.C. § 1334. He began by examining whether the lawsuit was "core" under 28 U.S.C. § 157(b)(2) as a counterclaim "by the estate against persons filing claims against the estate."

Judge Goldblatt decided that the answer lay in the statute's use of the words "by the estate." He observed that the estate ceased to exist on confirmation when the assets were reconveyed to the reorganized debtor or transferred to the liquidation trust under Section 1141(b). There being no counterclaim by the estate, he concluded that the lawsuits were not core under Section 157(b)(2).

Judge Goldblatt left the door open for a different result in a case where "all of the issues that are raised by the counterclaim will necessarily be decided in resolving the creditor's proof of claim."

For the turnover claim under Section 542, Judge Goldblatt said there was "arising under" jurisdiction, subject to a "glaringly obvious" question on the merits. He went on to say that courts "have typically held that the turnover power cannot be used to liquidate a disputed claim for breach of contract."

Judge Goldblatt denied the motion to dismiss regarding turnover without prejudice, subject to "the defendants' right to seek summary judgment . . . on that basis."

'Related To' Jurisdiction

Judge Goldblatt turned to the question of "related to" jurisdiction, saying that defining the outer limits is "deceptively difficult." In the Third Circuit, the primary authority is *Pacor*, holding there is "related to" jurisdiction if the outcome could have a "conceivable effect" on the estate.

Agreeing with other courts, Judge Goldblatt read *Pacor* to mean "that a showing of a conceivable effect on the bankruptcy estate is not only sufficient but is *necessary* to bring a matter within the related-to jurisdiction." [Emphasis in original.]

The requirement of necessity led Judge Goldblatt to question whether the bankruptcy court could exercise supplemental jurisdiction, which is granted to district courts under 28 U.S.C. § 1367. Although district courts may exercise supplemental jurisdiction, he concluded that supplemental jurisdiction "may not be transferred to bankruptcy judges," because supplemental jurisdiction "is outside the scope of what is or may be delegated to the bankruptcy judges under § 157(a)."

Jurisdiction After Confirmation

Judge Goldblatt said that "claims asserted after the plan has been confirmed are different," in view of *In re Resorts Int'l, Inc.*, 372 F.3d 154 (3d Cir. 2004).

Because "*Pacor* limits the related-to jurisdiction to matters that have a conceivable effect on the estate," Judge Goldblatt said, "there can be no traditional 'related-to' jurisdiction after plan confirmation," because estate property "typically" revests in the debtor under Section 1141(b).

On the other hand, Judge Goldblatt said that there is no need for post-confirmation "related to" jurisdiction "if all one is doing is seeking to construe or enforce the confirmation order, or a plan."

For Judge Goldblatt, the issue came down to the question of "what kind of connection" to the plan is "sufficient to warrant the invocation of the post-confirmation related-to jurisdiction."

Materiality and Retention of Jurisdiction

In *Resorts*, Judge Goldblatt described the Third Circuit as saying "that even though the claim had the potential to increase the corpus of the litigation trust (and therefore its beneficiaries' recoveries), that was not enough to create a 'close nexus.'" Quoting *Resorts*, he went on to say,

> [The Third Circuit] explained that the possibility of expanding the universe of trust assets was not sufficient to grant the bankruptcy court subject-matter jurisdiction because that would allow any lawsuit asserted by a post-confirmation trust to fall within the category of "related-to" jurisdiction. "Such a result would widen the scope of bankruptcy court jurisdiction beyond what Congress intended for non-Article III bankruptcy courts."

Judge Goldblatt then turned to the question of whether retention of jurisdiction under a plan can supply subject matter jurisdiction. Again pointing to *Resorts*, he said,

> A provision announcing that the court will "retain jurisdiction" over post-confirmation disputes is effective only to the extent jurisdiction otherwise exists under 28 U.S.C. § 1334(b); it cannot enlarge it.

Concluding *Dicta*

Judge Goldblatt had six pages of *dicta* at the end of his opinion that's required reading for anyone practicing in Delaware. He said that the "recurring nature of this issue [makes it] appropriate and helpful to add a word of further guidance on the retention of post-confirmation jurisdiction."

Judge Goldblatt said there is "relatively little authority" on when it's proper to keep the estate open after confirmation to retain subject matter jurisdiction. For guidance, he looked to authorities under chapter 13, "because the language of § 1327(b) is materially identical to that of § 1141(b)." He gave an example of when it might be proper to keep the estate open to maintain jurisdiction:

> If the only way the debtor could meet its obligations under the plan would be to keep a particular asset in the estate and have it liquidated after the effective date, one could certainly say that the asset in question has a "close nexus" to the plan and bears on the "implementation, consummation, execution, or administration of the confirmed plan."

However, Judge Goldblatt said there should be limitations. For instance, he said it would be "difficult to imagine that the proponent of a plan could make such a showing without identifying the claim or cause of action that is being retained in the estate with some degree of specificity." He added, "a retention-of-jurisdiction provision that fails to identify a specific cause of action is unlikely to be sufficient to retain post-confirmation related to jurisdiction."

But when an action has been "specifically identified," Judge Goldblatt said "there is at least a question [of] whether the jurisdictional nature of the analysis means that the question of the propriety of those provisions is subject to being revisited or whether the preclusive nature of the confirmation order means that such a provision should be given effect even if it would not meet the standards described above."

"At first blush," Judge Goldblatt said, opinions like *Espinosa* would mean "that ordinary preclusion principles would apply." However, courts on their own are obliged to establish subject matter jurisdiction, even on appeal for the first time. Since the issue was not before the court, he decided it was "neither necessary nor appropriate to resolve it more definitively here."

Judge Goldblatt dismissed the claims for breach of contract and a declaration that receivables were owing. Claims remain for recovery of preferences, disallowance of claims and turnover.

Observations

To recover prepetition accounts receivable, the plan administrator presumably will file suit in a federal or state court of competent jurisdiction. Meanwhile, the adversary proceeding will go forward in bankruptcy court regarding preferences and disallowance of the claims.

Given that proceedings often move more quickly in bankruptcy court than elsewhere, the plan administrator conceivably might obtain rulings from the bankruptcy court that could resolve some issues in the receivables lawsuits under the doctrine of issue preclusion.

No matter; the plan administrator will be prosecuting lawsuits in two courts against the same defendants.

Is that what Congress intended?

These days, congressional intent takes second place to the words in a statute, especially a jurisdictional statute. In that respect, Judge Goldblatt's opinion is spot on.

Arguably, Congress didn't intend to sweep all lawsuits against creditors into bankruptcy court after confirmation. Were the bankruptcy court to remain the default venue, a former debtor would be under the protection of the bankruptcy court for years after confirmation, and creditors would be defending suits in bankruptcy court far from the venues in which the former debtor otherwise could sue the defendants.

The opinion is *Roberts v. Green Convergence (In re SunPower Corp.)*, 25-52473 (Bankr. D. Del. July 23, 2026).

Plans & Confirmation

Will the Second Circuit along with courts in Delaware and Texas decide that creditors must 'opt in' before granting releases in favor of nondebtors?

New York District Court Reverses a Chapter 11 Plan with Opt-Out Releases

Reversing confirmation of a chapter 11 plan, a district judge in New York ruled that the ability to opt out doesn't mean that releases in favor of nondebtors are consensual. The district judge therefore held that the nondebtor releases were impermissible after *Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024).

In her 17-page opinion on December 1, District Judge Denise Cote made short shrift of several theories supporting the idea that an opportunity to opt out amounts to a consensual release. Under both state and federal contract law, she decided that silence doesn't bind a creditor to a contract or a release.

Driving more stakes into the heart of opt-out plans, Judge Cote held that consenting to the bankruptcy court's jurisdiction isn't consent to "any release the court may approve." Likewise, opting out "utilized in the class action context simply does not apply to the third-party releases."

Except in the case on appeal, a decision like Judge Cote's does not bind bankruptcy courts in different cases in New York. Unless the Second Circuit reverses Judge Cote, are opt-out chapter 11 plans a thing of the past in New York? Will Delaware and Texas follow?

Don't hold your breath waiting for the answer. We may not know whether opting out works until the Supreme Court gives us *Purdue II*.

No Stay Pending Appeal

The debtors comprised a large Brazilian airline with about $4 billion in funded debt. The chapter 11 plan included nondebtor releases in favor of the creditors' committee and its members, along with creditors who were engaged in financing and negotiating the plan.

Without checking the opt-out box on the ballot, creditors who voted on the plan would confer broadly worded releases relating in any manner to the bankruptcy case. Creditors who were not impaired and did not vote would confer releases if they did not check the opt-out box on the notice sent to them. The releases would also bind creditors' "Related Parties."

Among the almost 700 ballots, 10% were returned as undeliverable, and about half of those who voted decided to opt out. Among the almost 3,000 notices to unimpaired creditors, about 70 were undeliverable, but only 14 notices were returned. Among them, 11 opted out.

Over objection from the U.S. Trustee, the bankruptcy court confirmed the plan. *In re GOL Linhas Aéreas Inteligentes SA*, 672 B.R. 129 (Bankr. S.D.N.Y. May 22, 2025). To read ABI's report, click here. The U.S. Trustee appealed.

After the bankruptcy court denied a stay pending appeal, Judge Cote also denied a stay but said that the consent question "raises a sufficiently serious legal issue that deserves resolution." *In re GOL Linhas Aéreas Inteligentes SA*, 225-4610, 2025 BL 198326, 2025 WL 15918330 (S.D.N.Y. June 5, 2025). To read ABI's report, click here.

Judge Cote's decision to deny a stay pending appeal was facilitated, she said, because the debtors "agreed that they would not argue to any court reviewing [the U.S. Trustee's] appeal that the challenge to the third-party releases was equitably moot."

The Bankruptcy Court's Opinion

In nixing nonconsensual releases in *Purdue*, Judge Cote cited the Supreme Court for saying the opinion did not call consensual releases into question and did not express a view on what is consensual.

Approving opt-out releases, the bankruptcy court's opinion confirming the plan was the most comprehensive ever written. Judge Cote described the bankruptcy court as deciding that federal law, not state law, would determine what's consensual. The bankruptcy court saw federal waiver doctrines and Section 1123(b)(6) as providing authority for opt-out releases.

Judge Cote characterized the bankruptcy court as believing that creditors impliedly consented to releases by consenting to the bankruptcy court's jurisdiction, because the releases affected the estate and there was adequate service of process.

Nonconsensual Under State Law

On appeal, Judge Cote said that "most" of the briefing was devoted to the question of whether state or federal law controlled the validity of the releases. She saw no conflict, because "the same general principles of contract law apply under both federal and state law."

Judge Cote said that the debtors did "not seriously dispute" that the releases would be nonconsensual under New York law. She quoted New York's highest state court for following the *Restatement (Second) of Contracts* in saying that a binding contract "'requires an objective manifestation of mutual assent, through either words or conduct, to the essential terms comprising the agreement.'" The Second Circuit quoted the *Restatement* where it says that "an offeror does not have power to cause the silence of the offeree to operate as acceptance."

Judge Cote said that the debtors offered "three cursory arguments" to refute the idea that state law controlled. She described them as contending that silence was sufficient because the released parties made substantial contributions to the case, the creditors had an opportunity to respond, and failure to respond carries consequences.

Judge Cote said that the debtors had no authority for their first two arguments, while the third idea only had support from a class action case that had come down before *Purdue*. She therefore held that the releases were not consensual under state law.

Likewise Impermissible Under Federal Law

The debtors were of a mind that federal law controlled and that the releases were permissible under federal law.

Judge Cote cited the Second Circuit for holding that the federal common law of contracts follows the general principles of contract law. She once again said that "the general principles of contract law, as embodied in the *Restatement of Contracts*, establish that, outside of rare exceptions, consent cannot be implied from silence."

Judge Cote therefore held that "the third-party releases here are nonconsensual under federal law as well."

Consenting to Jurisdiction Isn't Consenting to Releases

The debtors offered other arguments for which Judge Cote said they had "little to no supporting authority."

First, the debtors took the position that consenting to jurisdiction of the bankruptcy court amounted to consent to "the imposition of a third-party release." Even assuming there had been a consent to "adjudication," she said that "it does not follow that all parties that consent to a bankruptcy court's jurisdiction necessarily consent to any release the court may approve."

Regarding the idea that consent to jurisdiction confers consent to releases, she said that the debtors did not cite "any case in which a court made that logical leap."

Next, Judge Cote said that the debtors "attempt[ed] to import a rule from the class action context." She described Federal Rule 23 as "provid[ing] the mechanism for establishing a class and the procedures for protecting the rights of members of a certified class."

In a chapter 11 case, Judge Cote said, "[t]here is no suggestion that the releasing parties in this bankruptcy are members of a defined class certified to litigate or settle defined claims or that the Rule 23 procedures and its safeguards have been followed."

"The opt-out mechanism utilized in the class action context simply does not apply to the third-party release here," Judge Cote ruled.

Last, the debtors argued that rules on default judgments make the releases enforceable. Judge Cote rejected the argument as follows:

> [T]he Debtors fail to identify any opinion in which a court adopted this reasoning to find that a failure to opt out was sufficient to imply consent, let alone a case adopting this reasoning in the context of a third-party release.

Judge Cote ended her opinion by saying,

> Further, it is undisputed that the creditors had no duty to respond to the opt-out opportunity, and courts do not enter default judgments when parties have no duty to respond.

Judge Cote reversed the confirmation order and struck third-party releases from the plan, remanding the case "for further proceedings."

Observations

Should there be an appeal, it's by no means a sure thing that the Second Circuit will affirm Judge Cote and require opting in. Recall that the Second Circuit had reversed the district court and reinstated confirmation of Purdue Pharma's chapter 11 plan when it contained nonconsensual releases. Of course, the Supreme Court reversed the Second Circuit in *Purdue*, but the Second Circuit was in favor of nonconsensual releases when left to its own devices.

Further, recall that *Purdue* was a 5/4 decision in the Supreme Court, meaning that four justices believed that nonconsensual releases were permissible in chapter 11 cases. Also recall that the dissent was more than twice as long as the majority opinion and that Justice Brett Kavanaugh dissented "respectfully but emphatically."

Does the close vote mean that the Supreme Court will not impose a rigorous standard in deciding whether a release is consensual?

The difficulty in deciding what's consensual and what's not will be shown graphically in a two-part article by Prof. Bruce A. Markell to premier in the January 2026 issue of the *American Bankruptcy Institute Journal*. In his piece, "Consensus on Consent? Not Yet," Prof. Markell gives a multitude of examples explaining why consent is not “binary.” Rather, he explains why the concept is “a continuum, varying with the issue at hand and the parties involved.” Prof. Markell is the Professor of Bankruptcy Law and Practice at the Northwestern University Pritzker School of Law.

The definition of “consent” is not the only concept that might ultimately control nondebtor releases in chapter 11 cases. What about personal jurisdiction? By mailing a notice, does a bankruptcy court obtain personal jurisdiction over those to be bound by releases? Is something more required, akin to service of a summons and complaint? Does filing a claim against a debtor imply consent to personal jurisdiction regarding claims the creditor holds against nondebtors?

Even if consensual, can a bankruptcy court or even a district court confer consensual releases without comprehensive legislation akin to Section 524(g) and without comprehensive rules like Rule 23?

A chapter 11 plan with nondebtor releases is a reverse class action. In a class action, injured parties decide when and where to seek relief from the party who caused the alleged damage. In bankruptcy, the party causing the damage decides when and where to sue the victims to obtain a release from them. Can Rule 23 be applied in bankruptcy cases even by analogy?

Some requirements for a successful class action may not be possible in bankruptcy cases. In class actions, there must be commonality among members of the class. In sexual abuse bankruptcy cases, is there sufficient commonality among the victims to justify treatment of the victims as a class? Can the commonality requirement be satisfied by claims processing in a bankruptcy case?

Can an elaborate invention of federal common law cover all the bases, allowing bankruptcy courts to solve a problem where the tort system falls short? And, of course, is the tort system falling short, and is there a problem to solve when it comes to releasing nondebtors who elect not to file bankruptcy themselves?

The opinion is *In re GOL Linhas Aéreas Inteligentes SA*, 25-4610 (S.D.N.Y. Dec. 1, 2025).

Creditors who voted against the plan and classes presumed to reject didn't confer releases on nondebtor third parties.

Not Requiring Opt-In, Miami's Judge Isicoff Approved an Opt-Out Chapter 11 Plan

Persuaded by authorities from the Supreme Court holding that the ability to opt out of a class action satisfies due process concerns, Bankruptcy Judge Laurel M. Isicoff of Miami confirmed a chapter 11 plan where creditors were given the ability to opt out of nondebtor releases.

However, Judge Isicoff parted company with the debtor in her April 21 opinion by ruling that creditors who voted against the plan will not bestow third-party releases despite not opting out. Likewise, creditors or interest holders will not issue releases if they are in classes that are deemed to have rejected the plan.

Finding a "genuine division of approach," Judge Isicoff surveyed opinions throughout the country on the question of opt-in versus opt-out.

Purdue Doesn't Define Consent

The chapter 11 plan before Judge Isicoff contained what she called "opt-out third-party releases." Anyone not wishing to release nondebtors must affirmatively "'opt out' of such release" by checking the opt-out box on the ballot, she said.

The U.S. Trustee had objected to confirmation on several grounds, contending that consent must be governed by state law and that the ability to opt out was not consent. The U.S. Trustee said that neither New York nor Florida law would find consent from the ability to opt out.

Judge Isicoff began her analysis of the merits by alluding to *Purdue* and its proscription of nondebtor releases without consent. *Purdue*, she said, "left open [the issue of] what procedures are sufficient to establish the requisite consent." *See Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024). To read ABI's report on *Purdue*, click here.

Courts around the country, Judge Isicoff said, "have divided over whether silence or failure to act after notice can constitute consent to a third-party release, whether a creditor must affirmatively opt in to consent to a third-party release, or whether some intermediate mechanism may suffice."

Three Approaches Around the Country

Judge Isicoff described the rationales supporting the three approaches to nondebtor releases.

Beginning with *Epstein v. Container Store Group Inc. (Container Store Group Inc.)*, 676 B.R. 356 (S.D. Tex. Feb. 12, 2026), Judge Isicoff said that courts approving opt-out plans find "them appropriate where parties-in-interest received detailed notice, deadlines to object, voting deadlines, and all ballots provided claimants opportunity to opt out." To read ABI's report on *Container Store*, click here. She also noted the approval of opt-out releases in *Spirit Airlines*, "where creditors received clear notice and a meaningful opportunity to decline the release." To read ABI's report on *Spirit Airlines*, click here.

For courts finding that "silence alone is insufficient," Judge Isicoff cited, among others, *In re GOL Linhas Aéreas Inteligentes SA*, 675 B.R. 125 (S.D.N.Y. Dec. 1, 2025), where she said that the district court "held that opt-out mechanisms were insufficient under both federal and New York law to establish creditor consent." To read ABI's report on *GOL*, click here.

Judge Isicoff described the third group of decisions as the "hybrid approach." Cases like *In re Smallhold, Inc.*, 665 B.R. 704 (Bankr. D. Del. 2024), she said, "require some affirmative participation before failure to opt out may be deemed consent." To read ABI's report on *Smallhold*, click here.

In the Eleventh Circuit, Judge Isicoff found no binding authority and said that decisions around the country "reveal a genuine division in approach."

The Analogy to Class Actions

Courts requiring affirmative action or opting in, Judge Isicoff said, believe that "the Bankruptcy Code does not itself authorize nonconsensual third-party releases outside §524(g)" and that "applicable state law does not recognize silence or failure to act as consent." Courts approving opt-out plans, she said, "view the question as arising not in ordinary bilateral contract formation, but in the context of a court-supervised chapter 11 process governed by the Bankruptcy Code."

For courts permitting opt-out plans, Judge Isicoff said that "the controlling inquiry is not whether the creditor affirmatively checked an opt-in box, but whether the creditor received clear and conspicuous notice of the release, understood the consequences of inaction, and had a meaningful opportunity to decline the release by opting out."

For herself, Judge Isicoff decided that opt-out procedures are "an acceptable form of consent." She cited how the "Bankruptcy Code and Federal Rules of Bankruptcy Procedure frequently give legal effect to inaction after constitutionally adequate notice." Specifically, she said, "opt-out procedures have long been recognized in other representative contexts, most notably class actions."

Judge Isicoff alluded to class actions given her belief that the "resolution of this issue is governed solely by federal law" because the power to issue releases arises under Section 105(a), the All Writs Act applicable in bankruptcy cases. She described Section 105(a) as allowing "a bankruptcy court to issue orders necessary or appropriate to carry out the provisions of title 11, so long as those orders do not contravene the Bankruptcy Code."

Judge Isicoff found "[n]othing in the Bankruptcy Code [that] prohibits a court from treating failure to opt out, after clear notice and an opportunity to decline, as consent to a consensual release." After all, creditors in the entire class are bound by a plan, whether they vote in favor or not, as long as the class has accepted the plan by the requisite majorities.

In federal practice generally, Judge Isicoff said "[t]here are many instances in law where the failure to act will bind a party so long as that party has received constitutionally satisfactory notice." The "same principle," she said, "underlies the concept of class action."

Citing *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), Judge Isicoff said that the Supreme Court "rejected a due process challenge to the opt-out procedures" and "specifically rejected the argument that due process required an affirmative request for inclusion."

"Although the class-action context is not identical to a chapter 11 confirmation process," Judge Isicoff decided that "those authorities are instructive insofar as they demonstrate that due process does not invariably require affirmative opt-in participation."

Rejecting a Plan Is Opting Out

Judge Isicoff held that opting out is permissible if three tests are satisfied: (1) Nonconsensual releases must be necessary or appropriate; (2) opting out must be appropriate in the case at hand; and (3) due process must be satisfied.

Applying the standard to the case before her, Judge Isicoff decided that a "party in interest who rejects a plan, or has a claim or an interest in a class that is deemed to reject the plan, cannot be bound to a release provision in the absence of expressly opting out." In other words, opting out "only applies" to creditors "who either voted in favor of the plan and did not opt-out of the Holder Release, or creditors . . . who did not vote."

Finding that affected parties were afforded "adequate notice that satisfies due process," Judge Isicoff confirmed the plan with the modification barring releases from creditors who voted against the plan or were in a class presumed to reject the plan.

The opinion is *In re Pat McGrath Cosmetics LLC*, 26-10772 (Bankr. S.D. Fla. April 21, 2026).

The Second Circuit will review the reversal in GOL where a New York district court struck opt-out releases for nondebtors.

A New York Bankruptcy Judge Permits Opt-Out Plans Despite Reversal in *GOL*

On December 1, a district judge in New York struck nondebtor releases from the chapter 11 plan for Brazilian airline GOL Linhas Aéreas. The district judge faulted the plan for conferring releases given by all creditors who did not affirmatively opt out, even those who didn't vote on the plan one way or the other.

After the *GOL* decision came down, another Brazilian airline, Azul S.A., modified its chapter 11 plan in New York to include releases for nondebtors only to the extent that creditors didn't opt out but voted for or against the plan. In other words, the *GOL* decision is evidently having an effect on debtors, even though the *GOL* opinion by the district court is not binding on bankruptcy judges in New York.

We leave it to our readers to decide whether the *Azul* decision fully conforms to the holdings by the district court in the GOL reorganization, *In re GOL Linhas Aéreas Inteligentes SA*, 672 B.R. 129 (S.D.N.Y. Dec. 1, 2025). To read ABI's report on *GOL*, click here. Note: The GOL debtor appealed to the Second Circuit on January 7.

The Modified Azul Plan

In his opinion on January 6, Bankruptcy Judge Sean H. Lane of New York described Azul as "the largest airline serving Brazil." The chapter 11 plan had $4.8 billion for creditors in 12 classes and discharged $2 billion in debt. More than 90% of creditors in every class voted on the plan, with the exception of the so-called convenience class.

Originally, the plan provided that a creditor would confer a release on nondebtors even if the creditor did not vote on the plan. For creditors who did vote, they were given the option of opting out of nondebtor releases.

Several days after the *GOL* decision came down from District Judge Denise Cote in December, Azul amended its plan. As Judge Lane put it, "the Debtors amended the Plan so that the release is only granted if the voter returns a ballot and does not opt out; no releases are granted by voters who do not return a ballot."

Among the 3,000 ballots that were sent out, Judge Lane reported that there were almost 800 opt-outs.

Among others, the nondebtor releases ran in favor of lenders who financed the chapter 11 case, indenture trustees, the distribution agent, the official creditors' committee and its members, a group of secured lenders and certain shareholders.

The U.S. Trustee lodged the only confirmation objection, contending that releases should only be given by creditors who opt in, and then only to fiduciaries.

Release for Nonfiduciaries

Relying on out-of-circuit decisions like *In re Highland Capital Mgmt., L.P.*, 132 F.4th 353 (5th Cir. 2025), Judge Lane said that the U.S. Trustee "'argues that exculpatory language may only apply to 'court-supervised estate fiduciaries who have performed services during a Chapter 11 case prior to plan confirmation.'" To read ABI's report on *Highland Capital*, click here.

Judge Lane devoted the remainder of his decision to explaining why the "case law in this jurisdiction, including from this Court, has already concluded otherwise." In large part, he relied on his own decision in *Genesis Glob. Holdco, LLC,* 660 B.R. 439 (Bankr. S.D.N.Y. 2024). In *Genesis*, he said that he had "observed that '[i]t is well established in this district that, under the proper circumstances, exculpation is not limited to estate fiduciaries.'" *Id*. at 528.

In the case before him, Judge Lane said that the releases were "appropriate" because they were "included to protect the Exculpated Parties that are involved in the Debtors' cases and the restructuring transactions that underpin the Debtors' reorganization" and because they "made material contributions to the Debtors' cases." Furthermore, he said that the releases were "a bargained-for term in exchange of their supporting the Plan."

Opt-Out Plans Are Ok

Having decided that nonfiduciaries are eligible for releases, Judge Lane turned to the question of whether so-called opt-out releases are permissible as consensual releases after *Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024). Judge Lane described the Supreme Court as making "it clear that *consensual* third-party releases were not the subject of its decision." [Emphasis in original.] To read ABI's report on *Purdue*, click here.

Citing his decision in *In re Spirit Airlines, Inc.*, 668 B.R. 689 (Bankr. S.D.N.Y. 2025), Judge Land said "that many courts in this Circuit and elsewhere have found third-party releases through the use of opt-outs to be consensual — and permissible — under bankruptcy law after careful consideration of the circumstances within each case." To read ABI's report on *Spirit*, click here.

However, Judge Lane noted *In re Smallhold, Inc.*, 665 B.R. 704 (Bankr. D. Del. 2024), in observing "that other courts had reached a contrary view." To read ABI's report on *Smallhold*, click here. He also cited the district court's holding in *GOL* "that the opt-out provisions contained in the plan in that bankruptcy case constituted a non-consensual release of claims against third parties in violation of *Purdue*."

In view of "all of this authority," Judge Lane held "that the third-party releases using an opt-out here are permissible" because "the Debtors amended the Plan to provide that the releases are provided only by creditors that both returned a ballot and did not elect to opt out." He cited "[o]ther cases [holding] that voting on a plan, either to accept or reject, constitutes consent to releases."

Assuming state law controls on what's consensual and undertaking a contract analysis like that in the district court's *GOL* reversal, Judge Lane cited the Restatement (Second) of Contracts in holding "that the Plan complies with state law regarding consent." Citing Section 69 of the Restatement and quoting his *Spirit* decision, he said,

> [T]he second exception in the Restatement provides that "silence and inaction will constitute acceptance of an offer when 'the offeror has stated or given the offeree reason to understand that assent may be manifested by silence or inaction, and the offeree in remaining silent and inactive intends to accept the offer.'"

Judge Lane concluded that creditors in the case before him had "clearly manifested their consent" because they were "given reason to understand that assent may be manifested by silence or inaction, and that in remaining silent and inactive they intend to accept the offer."

Finding that the nondebtor releases were consensual and permissible, Judge Lane overruled the U.S. Trustee's objection. He had already confirmed the plan on December 19. His written opinion on January 6 was a cleaned-up version of his bench opinion delivered on December 19.

Observations

The law in the Second Circuit is altogether up in the air until the Second Circuit comes down with a decision either following, rejecting or modifying *GOL*. The U.S. Trustee might also appeal *Azul*, because the U.S. Trustee has 60 days to appeal.

Indeed, it's fair to say that the law on opt-in or opt-out will remain undecided until and unless the Supreme Court reviews a case like *GOL*. How the Supreme Court will rule on opt-out is unclear because *Purdue* was a 5/4 decision, and four justices saw nonconsensual releases as the best thing since sliced bread.

Although we call on readers to decide whether Judge Lane's *Azul* decision lines up with *GOL*, we note that Judge Lane read the Restatement to find consent more readily than did District Judge

Cote. Still, nothing much matters in New York until the Second Circuit opines on *GOL* and says whether nondebtor releases are sometimes, never or always permissible.

The opinion is *In re Azul S.A.*, 25-11176 (Bankr. S.D.N.Y. Jan. 6, 2026).

ROCHELLE'S DAILY WIRE

Releases by creditor classes who received nothing were not consensual and were stricken.

Houston District Court Upholds an 'Opt Out' Plan for Impaired and Unimpaired Classes

With an exception for two classes, District Judge Lee H. Rosenthal upheld confirmation of an "opt out" plan, finding that the opportunity to opt out of releases in favor of nondebtors made the releases consensual and therefore permissible under *Purdue*.

In her February 12 opinion, Houston's Judge Rosenthal nixed releases by shareholders and subordinated creditors who received nothing under the plan and were deemed to have rejected the plan. She also narrowed "gatekeeping" to line up with the Fifth Circuit's decision in *Highland Capital II*.

The Opt-Out Plan

The debtor, Container Store, filed and confirmed a prepackaged chapter 11 plan. Term loan creditors were the only impaired class and the only class entitled to vote.

Nonvoting, unimpaired classes included other secured claims, asset-based lending claims and general unsecured claims. Equity holders and subordinated creditors received nothing under the plan and were deemed to have rejected the plan.

The plan had releases in favor of nondebtors binding anyone who did not return a ballot or a form opting out of the releases. In addition, the plan had an injunction protecting the nondebtor releasees along with a gatekeeping provision requiring the bankruptcy court's approval before suing a nondebtor releasee.

The U.S. Trustee objected to confirmation, contending that the opt-out releases were nonconsensual and impermissible after *Purdue*. The U.S. Trustee also asserted that the injunction and gatekeeping provisions were not authorized. Bankruptcy Judge Alfredo R. Peréz overruled the objections and confirmed the plan. The U.S. Trustee appealed.

The U.S. Trustee Has Standing

On appeal, the debtor contended that the U.S. Trustee had no standing to appeal. Although Section 307 gave the U.S. Trustee standing in bankruptcy court, Judge Rosenthal said that "the Trustee must also have constitutional standing to appear in this court."

Citing *SEC v. U.S. Realty & Improvement Co.*, 310 U.S. 434, 459–60 (1940), Judge Rosenthal said that the "Supreme Court has recognized that, at least in some circumstances, the government has Article III standing based on purely public interests." She proceeded to cite the First, Second, Third, Fourth, Sixth and Ninth Circuits for "holding that the Trustee has standing to appeal a bankruptcy order even without a pecuniary interest." Judge Rosenthal read the Fifth Circuit's decision in *In re Community Home Financial Services, Inc.*, 990 F.3d 422, 426–27 (5th Cir. 2021), as "favorably [relying] on much of this precedent."

Concluding that "the Trustee represents a significant and concrete public interest in this case by advocating for those who have not formally appeared in the proceedings," Judge Rosenthal held that the U.S. Trustee had standing to appeal.

Not Equitably Moot

The debtor contended that the appeal was equitably moot.

Judge Rosenthal began by saying that the Fifth Circuit is "more hesitant" than other circuits to invoke equitable mootness, citing, among other authorities, the case known as *Highland Capital I*, *In re Highland Cap. Mgmt., L.P.*, 48 F.4th 419 (5th Cir. 2022). To read ABI's report, click here.

Judge Rosenthal read Fifth Circuit authorities as placing "heavy emphasis" on the ability of the court to "excise aspects of the plan" without unraveling the plan. Citing *Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (In re Pac. Lumber Co.)*, 584 F.3d 229, 241 (5th Cir. 2009), she said that the "court may 'fashion whatever relief is practicable' instead of declining to review simply because full relief is not available.'"

Judge Rosenthal declined to apply equitable mootness to the issues on appeal. She saw "little justification" for applying the doctrine to provisions of the plan that were "excisable" and raised "important questions of due process and fairness in the bankruptcy context."

At the end of the discussion, Judge Rosenthal said, "That the Plan might not have moved forward without these provisions does not insulate them from review."

Federal Law Decides What's 'Consent'

For the principal issue on appeal, Judge Rosenthal defined the question as "whether the notification and opportunity to opt out of the third-party releases made the releases consensual, and therefore binding."

Long before *Purdue*, Judge Rosenthal said that the Fifth Circuit only permitted consensual releases. Does state or federal law determine whether a release is consensual? She found two independent grounds requiring the use of federal law.

First, Judge Rosenthal explained why Sections 1123(b)(6) and 105(a) require the use of federal law. She said that *Purdue* and Fifth Circuit authority "do not prohibit a bankruptcy court from relying on § 1123(b)(6) to create *consensual* or *full-satisfaction* releases." [Emphasis in original.]

"Because a bankruptcy court's authority to enter consensual releases follows from the Code's text and structure," Judge Rosenthal concluded that "it raises questions of federal law: what is 'appropriate'; what is 'necessary'; and what it means to 'agree.'"

As a second and independent ground for applying federal law, Judge Rosenthal adopted a novel theory "that a bankruptcy court's authority to enter consensual third-party releases derives from federal law: a federal court's inherent power to enter consent decrees resolving claims within their jurisdiction." Quoting the Fifth Circuit, she said that a chapter 11 plan is "'a kind of consent decree'" and "'can sweep more broadly than can other forms of court-ordered relief.'"

Federal Law OKs Opt-Out

Judge Rosenthal next applied federal law in deciding whether opt-out plans are consensual.

"The key precedent," Judge Rosenthal said, was *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), where she read the Supreme Court as rejecting "the idea that a plaintiff needed to affirmatively 'opt in' to be bound by a class-action judgment." In the case on appeal, she found that the procedures used to advertise and confirm the plan were "sufficient to confer consent."

The factors leading to the conclusion included the existence of an official creditors' committee and the U.S. Trustee's presence as "a powerful watchdog," plus a long list of cases approving opt-out plans. Judge Rosenthal elaborated:

> When reorganization plans are achieved through hard-fought negotiation by the interested parties, including those similarly situated to the silent creditor; inure to the creditor's benefit; give creditors proper notice; and require substantial consent to the third-party releases for the plan's success, it is reasonable to infer an intent to accept the plan from a creditor's silence.

Judge Rosenthal held: "[T]he failure to opt out constitutes consent to a third-party release under the appropriate circumstances."

Two Classes Excepted from Releases

Pointing to subordinated creditors and stockholders who received nothing and were deemed to have rejected the plan, Judge Rosenthal found it "clear that [those] two groups of claimants who received notice and an opt-out opportunity did not consent to the third-party releases." She found "no basis" for believing that those who received nothing from the plan also intended to give up even more by releasing claims and had "no incentive to accept the releases to help the reorganization."

Judge Rosenthal held that the bankruptcy court erred by "finding that the [subordinated creditors and shareholders] consented to the third-party releases by failing to opt out."

Permanent Injunction and Gatekeeping

Regarding the plan's permanent injunction to buttress the releases, Judge Rosenthal held that the bankruptcy court had "related to" jurisdiction and statutory power because "the injunction here is coextensive with a *consensual* release authorized by § 1123(b)(6)." [Emphasis in original.]

In view of *Highland Capital II*, the gatekeeping provision was another subject. *See In re Highland Cap. Mgmt., L.P.*, 132 F.4th 353 (5th Cir. 2025). To read ABI's report, click here.

Judge Rosenthal quoted *Highland Capital II* in saying that "the Fifth Circuit has 'never extended the *Barton* doctrine to give bankruptcy courts gatekeeping power over claims against non-debtors.'" *Id*. at 359. She described the Fifth Circuit as having "narrowed the class of exculpated parties down to trustee-like figures who could be nonconsensually released."

Judge Rosenthal held that the "gatekeeping provision here extends the *Barton* doctrine beyond these limits to cover people and entities who are not officers of the Bankruptcy Court and to cover conduct that is not within the scope of their official duties." On remand, she instructed the bankruptcy court to limit gatekeeping "to the scope of" *Highland Capital II*.

Judge Rosenthal affirmed in part, reversed in part and remanded in part.

The opinion is *Epstein v. Container Store Group Inc. (Container Store Group Inc.)*, 25-618 (S.D. Tex. Feb. 12, 2026).

Like a district judge in the Southern District of New York, Bankruptcy Judge Carl Bucki of Buffalo, N.Y., decided that opt-out releases in chapter 11 require affirmative consent.

Bankruptcy Judge in Western New York Nixes Opt-Out Nondebtor Releases in a Plan

In December, a district judge in the Southern District of New York held that the ability to opt out doesn't mean that releases in favor of nondebtors are consensual in a chapter 11 plan. The district judge therefore held that the opt-out, nondebtor releases were impermissible after *Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024). *In re GOL Linhas Aéreas Inteligentes SA*, 225-4610, 2025 BL 198326, 2025 WL 15918330 (S.D.N.Y. June 5, 2025). To read ABI's report, click here.

The *GOL* decision is on appeal to the Second Circuit.

In the Western District of New York, Chief Bankruptcy Judge Carl L. Bucki of Buffalo, N.Y., gave the Second Circuit something more to think about when he sided with the SDNY district judge and decided, like *GOL*, that a so-called opt-out plan is not consensual and is therefore prohibited by *Purdue*.

On the other side of the fence, the Second Circuit will doubtless consider *Epstein v. Container Store Group Inc. (Container Store Group Inc.)*, 25-618, 2026 BL 46404, 2026 US Dist. Lexis 29054 (S.D. Tex. Feb. 12, 2026), where a district judge in Houston disagreed with *GOL* and upheld confirmation of an "opt out" plan, finding that the opportunity to opt out of releases in favor of nondebtors made the releases consensual and therefore permissible under *Purdue*. To read ABI's report on *Container Store*, click here. [Assuming the decision in *Container Store* is an appealable, final order, the time to appeal has not yet run.]

New York Contract Law Controls

The case before Judge Bucki involved a Catholic diocese that had been in chapter 11 for six years. Finally, the debtor, the official unsecured creditors' committee and several insurers reached agreement on a plan that would confer releases on parishes and other nondebtor entities unless the creditor checks a box to opt out of the releases.

Intelligently, the parties decided to ask Judge Bucki whether the opt-out plan would fly, before enduring the process of approving a disclosure statement, soliciting votes and conducting a confirmation hearing where the U.S. Trustee, if not others, would object to the plan.

In his February 27 opinion, Judge Bucki said he was tasked with deciding whether consent to the plan's nondebtor releases "would be assumed" if a creditor doesn't opt out. Although agreeing with *GOL*, he said there was no binding authority in the Second Circuit about "the standard of consent" following *Purdue*, where the Supreme Court had reversed the Second Circuit.

In the diocese case, Judge Bucki said many if not most abuse creditors had claims against both the debtor and nondebtor entities like parishes, which had relied on the diocese to provide insurance coverage.

"Except in cases involving asbestos liability," Judge Bucki said, there is "nothing in the Bankruptcy Code [that] even contemplates a third-party release." Quoting his own decision in *In re Tonawanda Coke Corp.*, 662 B.R. 220, 222 (Bankr. W.D.N.Y. 2024), Judge Bucki said, "[A]ny proposal for a non-debtor release is an ancillary offer that becomes a contract upon acceptance and consent."

Judge Bucki recited how the debtor and the committee urged him to "develop a federal common law that will infer consent from the absence of objection." He declined the offer, again citing his *Tonawanda* decision, where he concluded that any voluntary contract would be governed by state law. He also cited *Purdue* for saying that "bankruptcy law does not give to this Court 'a roving commission to resolve' all problems of collective liability." *Purdue*, *supra*, 603 U.S. at 220.

Focusing on the facts, Judge Bucki noted that the debtor was a New York corporation, that all of the claims arose from actions taken in New York, and that the claimants' ability to sue arose from a New York law that enlarged the statute of limitations.

"By reason of these many relationships," Judge Bucki held, "the law of New York will set the controlling guidelines for consent."

Silence Isn't Consent

Under New York law, Judge Bucki said that "silence does not constitute consent, except in instances where estoppel might apply." The debtor and the committee, he said, "essentially contend that by silence, creditors are estopped from denying their consent to a third-party release."

Judge Bucki characterized estoppel by silence as having three requirements: (1) a duty to speak; (2) failure to speak; and (3) damage to the other party resulting "directly" from silence.

The victims, Judge Bucki said, are "innocent parties who have no obligation to respond to any request for consent . . . . Nor does this Court have any authority to impose such a duty." He therefore found "no basis to imply consent by estoppel."

Regarding damage, Judge Bucki said that an "abuse victim makes no representation at all when he or she fails to consent to third-party releases." There being no false representation, "there can be no fraud," he decided.

As an alternative to estoppel, the debtor and the committee proposed viewing the committee as a "surrogate" to provide consent, subject to the ability of a creditor to opt out. Rejecting the idea, Judge Bucki said that "the enumeration of rights [of a committee] in section 1103(c) does not include anything like the exercise of a power of attorney on behalf of creditors." Furthermore, he said that the right to vote is "expressly" given to the creditor by Section 1126(a).

Judge Bucki "reject[ed] the debtor's call to create a federal common law on the issue of consent," and sided with the district judge in *GOL*, who held that "consent cannot be implied from silence." *GOL*, *supra*, 2025 WL 3456675, at * 5.

Analogy to the Best Interests Test

Judge Bucki offered "two important bankruptcy guidelines" demonstrating that an "'opt-in' procedure maintains the spirit of at least two important bankruptcy guidelines." First, he offered the best interests test for confirming a plan.

Creditors, Judge Bucki said, "may waive this requirement only through acceptance of the plan," and acceptance "requires submission of an affirmative ballot and is not implied from silence. In like fashion, acceptance of a third-party release should require an affirmative consent to this extra-statutory relief."

Second, Judge Bucki alluded to the automatic allowance of a proof of claim absent objection. He said that "creditors have no reason to expect that the plan will address obligations other than those of the debtor itself. Under these circumstances, the imposition of a third-party release would constitute consent by ambush."

Judge Bucki directed the debtor and the committee to "to re-design a ballot that will require creditors expressly to 'opt-in' to a release of third parties."

The opinion is *In re Diocese of Buffalo, N.Y.*, 20-10322 (Bankr. W.D.N.Y. Feb. 27, 2026).

Rochelle's Daily Wire

The opinion by a district judge in New Jersey upholding stays protecting nondebtors should not be confused with plans protecting nondebtors.

District Judge Explores the Outer Limits of Injunctions Protecting Third Parties

For a comprehensive discussion of the bankruptcy court's subject matter jurisdiction to impose injunctions barring creditors from bringing claims against nondebtors in the Third Circuit, read the October 31 decision by District Judge Zahid N. Quraishi of Trenton, N.J., affirming Bankruptcy Judge Michael B. Kaplan.

Although the discussion by Judge Quraishi is complex, it comes down to this: When creditors are suing a nondebtor who has an indemnification claim against the debtor, the bankruptcy court has core jurisdiction to enjoin the suit, utilizing both the automatic stay under Section 362(a) and the All Writs Act in Section 105(a).

The debtor is Whittaker Clark & Daniels, which manufactured industrial minerals, chemicals and talc until selling the businesses in 2004. As part of the sale, the debtor agreed to indemnify the buyer for asbestos-related talc claims based on activities that arose *before* the sale.

Recently, we reported on an important Third Circuit opinion about Whittaker Clark & Daniels. Circuit Judge Thomas L. Ambro described when the appointment of a receiver will or won't deprive the corporate board of the authority to file bankruptcy. Of perhaps greater eventual significance, Judge Ambro and Circuit Judge Cheryl Ann Krause wrote dueling opinions on whether state choice-of-law rules always apply in bankruptcy cases, or whether federal courts in some circumstances may devise their own standards to govern choice of law. *In re Whittaker Clark & Daniels Inc.*, 152 F.4th 432 (3d Cir. Sept. 10, 2025). To read ABI's report, click here, here and here.

The Facts Regarding the Indemnification Claim

We will greatly compress the facts, but here's what's important: The debtors were beset with asbestos claims. There was no question that the automatic stay halted the suits and prevented the filing of new ones against the debtor.

There were also about 650 claims against the buyer based on activities of the debtor before the sale, for which the debtor had indemnified the buyer. There was no dispute that the automatic stay applied to those claims.

The dispute involved 30 other state law claims against the buyer based only on activities by the buyer after the acquisition for which the debtor had given no indemnification. Although there was no dispute that the claims were based only on the buyer's activities, the bankruptcy court entered a preliminary injunction finding that the 30 claims were halted by the automatic stay or that they could be enjoined under Section 105(a). There was no dispute that the debtor's assets included claims against the buyer based on the buyer's post-sale activities.

Subject Matter Jurisdiction

The official committee of talc claimants appealed the injunction applying to the 30 claims, contending that the bankruptcy court lacked subject matter jurisdiction even to address the debtor's motion for a stay.

The bankruptcy court had determined that it had core jurisdiction over the 30 claims because Section 362(a) is a substantive right under the Bankruptcy Code. "Because the Third Circuit has not addressed the precise issue of whether section 362(a) provides bankruptcy courts with 'core' jurisdiction over state law claims against non-debtors," Judge Quraishi said that "the Bankruptcy Court also determined that it had 'related to' jurisdiction."

Regarding core jurisdiction, Judge Quraishi said "there does not appear to be any Third Circuit precedent about the extent of a bankruptcy court's 'arising under' or 'arising in' jurisdiction to extend the automatic stay of section 362(a) to state-law claims over non-debtors."

Judge Quraishi stated the issue on appeal as being "whether the Court should look to the nature of the underlying state-law claims against [the buyer] when evaluating whether a bankruptcy court has core jurisdiction, or whether a party's invocation of section 362(a) *ipso facto* grants a bankruptcy court with core jurisdiction to enjoin such disputes."

Parsing Third Circuit authority, Judge Quraishi decided "that a bankruptcy court would have 'core' jurisdiction over the state law claims against the debtor, even if those state-law claims are insufficient in and of themselves to confer the bankruptcy court with 'core' jurisdiction." He said it "necessarily follows that a bankruptcy court would have 'core' jurisdiction over the state law claims against the non-debtors if the provisions of section 362(a) are applicable."

Judge Quraishi concluded that the enjoined suits were based on state law, did not fall into the list of core matters under Section 157(b)(2) and didn't invoke substantive rights under the Bankruptcy Code. Still, he said that the Third Circuit "made clear" that "the inquiry does not end there." Because the claims "trigger the Debtors' indemnification provisions" in favor of the buyer, "the Bankruptcy Court properly determined that it had 'core' jurisdiction."

Automatic Stay

Judge Quraishi said that courts in the Third Circuit have extended the automatic stay to cover nondebtors in "unusual circumstances" that exist when there is an indemnity between the debtor and a third party and when a judgment against the third party will have the effect of a judgment against the debtor. Unusual circumstances also exist when the stay is essential for the reorganization, he said, quoting the Fourth Circuit.

Similarly, Judge Quraishi cited a district court in Pennsylvania that held "that 'unusual circumstances' were present because the debtors owed potential contractual and common law duties to indemnify the non-debtors, and the state law actions against the non-debtors would impact the debtors' ability to effectively reorganize."

For the 30 claims, Judge Quraishi said that the claims involved exposure to asbestos before the sale, thus triggering the debtor's indemnification obligations. He therefore held that the claims gave rise to "unusual circumstances" warranting imposition of the automatic stay. Because Section 362(a) provided substantive rights to the debtor, he held that "the Bankruptcy Court properly determined that it had subject matter jurisdiction over those claims."

Section 105(a)

If there were any doubt that the automatic stay applied, the bankruptcy court also invoked Section 105(a), which enables the entry of an injunction if four circumstances are found: (1) reasonable likelihood of a successful reorganization; (2) irreparable harm to the debtor without a stay; (3) the balance of the harm; and (4) the public interest.

Judge Quraishi found that all four requirements were met. He therefore upheld the injunction regarding the 30 claims.

The opinion is *Official Committee of Talc Claimants v. Whittaker, Clark & Daniels Inc.*, 24-10914 (D.N.J. Oct. 31, 2025).

Because the circuits didn't provide a statutory basis for exculpations, District Judge Swain in New York disagreed with circuit courts that approved exculpations.

District Judge Strikes Down Exculpations for Not Being Authorized by the Code

Setting aside exculpations in the chapter 11 plan confirmed by Voyager Digital Holdings Inc., District Judge Laura Taylor Swain of New York held that "the Bankruptcy Court lacked the authority to grant the prospective protection against liability and criminal responsibility . . . , nor did the Bankruptcy Court have authority to constrain the future exercises of governmental prosecutorial or regulatory authority in connection with the implementation of the Confirmed Plan."

In her August 4 opinion, Judge Swain also held that "[n]othing in the Bankruptcy Code or the doctrine of quasi-judicial immunity empowered the Bankruptcy Code to approve the Exculpation Provision." However, she did concede that the bankruptcy court's "concerns" giving rise to exculpations were "not baseless," because "cryptocurrency transactions contemplated by the Confirmed Plan were at best unclear."

Judge Swain did not set aside the exculpations by reliance on *Purdue*. Indeed, she decided that *Purdue* was not controlling one way or the other, because *Purdue* was a narrow decision dealing with releases, not exculpations.

The Plan and the Exculpations

The debtor was a cryptocurrency firm that confirmed a chapter 11 plan with a toggle feature. The assets were to be sold, with proceeds distributed to creditors. If the assets could not be sold, the debtor would liquidate the assets and make distributions.

In either event, the plan called for complicated "rebalancing transactions," because the debtor lacked a sufficient amount of some coins, and prices had fluctuated after filing.

As Judge Swain said, the plan contained an exculpation provision "that purports to protect certain 'Exculpated Parties' from liability for effectuating the Confirmed Plan, including engaging in rebalancing transactions and distributing cryptocurrency to customers." Those exculpated included the debtors, the official committee, committee members, released professionals, the debtors' released employees, the plan administrator and the distribution agent.

More particularly, the plan provided that the "Exculpated Parties shall have no liability for, and are exculpated from, any claim for fines, penalties, damages, or other liabilities based on their execution and completion of the rebalancing transactions and the distribution of cryptocurrencies to creditors in the manner provided in the Plan."

However, the plan said that the exculpations would not inhibit the ability of governmental units to stop or prevent actions contemplated by the plan. If there were regulatory actions after confirmation, Judge Swain quoted the bankruptcy judge as saying that those carrying out transactions contemplated by the plan "'will not be held liable on an *ex post facto* basis for having followed my order in the interim.'"

The U.S. Trustee appealed. Rebuffed in bankruptcy court, the U.S. Attorney and the U.S. Trustee were granted a stay pending appeal by the district court. *U.S. v. Voyager Digital Holdings Inc. (In re Voyager Digital Holdings Inc.)*, 23-02171, 2023 BL 110721, 2023 US Dist Lexis 57735 (S.D.N.Y. March 31, 2023). To read ABI's report, click here.

The debtor appealed the stay, but the Second Circuit dismissed the appeal for lack of jurisdiction. *Voyager Digital Holdings Inc. v. U.S. (In re Voyager Digital Holdings Inc.)*, 23-467, 2023 BL 227453, 2023 WL 4310688 (2d Cir. April 11, 2023). To read ABI's report, click here.

By stipulation, the stay pending appeal was modified to stay only the exculpations, not the remainder of the plan.

Purdue Inapplicable

Judge Swain first decided whether *Harrington v. Purdue Pharma LP*, 603 U.S. 204 (2024), controlled. She described *Purdue* as holding that nonconsensual, nondebtor releases were impermissible under Section 1123(b). To read ABI's report on *Purdue*, click here.

Although *Purdue* bore "superficial resemblance," Judge Swain said it is "fundamentally different" because the exculpations were not a "wholesale discharge of all claims." She said that the exculpation "does not give third parties protection from liability for prior conduct unrelated to implementation of the Plan."

"Because of the material differences between the Exculpation Provision and the nonconsensual third-party release invalidated by the Supreme Court, *Purdue Pharma's* condemnation of nonconsensual third-party releases does not compel this Court's rejection of the Exculpation Provision," Judge Swain said.

Explicit Code Authorization Required

Judge Swain turned to the question of whether the exculpation was "lawful" under the Bankruptcy Code, where her reading of *Purdue* meant that "[e]xplicit Code authorization is required." Mentioning the Fifth, Seventh, Ninth and Eleventh Circuits, she cited other circuits' decisions that have approved exculpations but said that "those cases are unpersuasive because they fail to articulate a statutory basis for exculpation that would be viable here."

The debtor claimed that exculpations were permissible under Sections 105(a), 1123(b)(6), 1129(a)(3), 1142(a), and 1142(b). So, Judge Swain examined them one by one.

Sections 105(a) and 1123(b)(6)

Judge Swain said that Section 105(a) was insufficient by itself to justify exculpations, because the debtors "must show that another Code section authorizes the Exculpation Provision."

Judge Swain turned to Section 1123(b)(6), which provides that a plan may "include any other appropriate provision not inconsistent with the applicable provisions of this title." However, she pointed to *Purdue,* where the Supreme Court said that a provision using Section 1123(b)(6) "must 'concern the debtor — its rights and responsibilities, and its relationship with its creditors.' 603 U.S. at 218."

Judge Swain decided that the exculpation "cannot be justified under section 1123(b)(6) by the argument that it merely facilitates the debtor's ability to obtain bankruptcy relief."

Sections 1129(a)(3) and 1142(a)

Section 1129(a)(3) says that a plan must be proposed in good faith, but Judge Swain said it "does not grant the Bankruptcy Court any affirmative powers."

"Notwithstanding any otherwise applicable nonbankruptcy law, rule, or regulation relating to financial condition," Section 1142(a) says that "the debtor and any entity organized or to be organized for the purpose of carrying out the plan shall carry out the plan and shall comply with any orders of the court."

Judge Swain critiqued the debtor for "neglect[ing] to consider the statute's limiting phrase 'relating to financial condition'" and said that the exculpation "goes far beyond the scope of any protection afforded by the plain text of section 1142(a)."

Section 1142(b)

Section 1142(b) permits courts to "direct the debtor and any other necessary party to execute or deliver . . . any instrument required to effect a transfer of property dealt with by a confirmed plan, and to perform any other act . . . that is necessary for the consummation of the plan."

Judge Swain said that the subsection does not "empower a bankruptcy court to proactively insulate parties from exposure to consequences under nonbankruptcy law, even if those consequences were the result of complying with the court's directions." Furthermore, she said, "there is no authority imbuing the Bankruptcy Court with authority to immunize criminal conduct." She went on to say that the Bankruptcy Code "expressly protects the Government's police and regulatory powers during and after a bankruptcy case."

Judge Swain said that a broad interpretation of Section 1142(b) might infringe on constitutional rights, such as sovereign immunity, the separation of powers, Article III jurisdiction and due process.

Judge Swain held that the "Exculpation Provision is unlawful because it is not specifically authorized by any provision of the Bankruptcy Code."

Quasi-Judicial Immunity

Alternatively, the debtor contended that the exculpations were a permissible application of quasi-judicial immunity.

Judge Swain found quasi-judicial immunity inapplicable because exculpation "preemptively purports to immunize conduct that has not yet even occurred. [Exculpation] also purports to apply in the criminal law context, unlike quasi-judicial immunity."

Judge Swain distilled quasi-judicial immunity as being a "general rule" that "a party acting pursuant to, and within the scope of, a valid judicial order is entitled to immunity." Although the doctrine protects bankruptcy trustees and committees, she said it is "applied as an affirmative defense that was raised in a lawsuit filed after the conduct at issue had occurred."

In comparison, Judge Swain said that the exculpation "preemptively purports to immunize conduct before it has even occurred." In other words, "quasi-judicial immunity is determined by the court in which the defense is raised, not in advance by a court wishing to protect parties before it from future liabilities."

Judge Swain ruled that the exculpations "cannot be justified as a form or an application of quasi-judicial immunity because it exceeds the recognized contours of that doctrine."

Judge Swain vacated the confirmation order "to the extent it approved the Exculpation Provision" and remanded the case to the bankruptcy court.

Commentary

Prof. Robert M. Lawless provided ABI with the following commentary:

> The Bankruptcy Code is showing its age. Exculpation provisions make sense generally. The reward for working on a bankruptcy case should not be a lawsuit from an unhappy litigant. In *Voyager*, there is a reasonable distinction between exculpation from a private lawsuit versus from a governmental investigation. The Code is full of all sorts of provisions that give bankruptcy judges discretion to fashion an appropriate order making distinctions such as these. The accumulation of precedent can transform these broad provisions into all-or-nothing legal issues, as happened here. It is beyond time to take a trip through the entire Bankruptcy Code and think about how it needs to be amended to fit modern reorganization practices.

Prof. Lawless is the Max L. Rowe Professor of Law and co-director of the Program on Law, Behavior & Social Science at the University of Illinois College of Law.

Observations

The plan administrator and the official committee filed an appeal to the Second Circuit two days after Judge Swain entered her order. It'll be interesting to see whether the Second Circuit agrees with the other circuits or creates a split, setting up an opportunity for a grant of *certiorari* by the Supreme Court as a follow-up to *Purdue*.

We urge readers to write comments predicting whether circuits will prohibit exculpations altogether or, perhaps, limit the scope of exculpations along the lines where Judge Swain found them too broad.

The opinion is *U.S. v. Official Committee of Unsecured Creditors (In re Voyager Digital Holdings Inc.)*, 23-2171 (S.D.N.Y. Aug. 4, 2026).

Reversing the bankruptcy court, a district judge in Houston calls for rejiggering the new equity after a chapter 11 plan had become effective.

Lender-on-Lender Violence Prompts Reversal of a Consummated Chapter 11 Plan

Having previously held that an appeal from confirmation of a chapter 11 plan was not equitably moot, District Judge Andrew S. Hanen of Houston built on the Fifth Circuit's *Serta Simmons* opinion by overturning confirmation because denial of the opportunity to participate in backstopping an equity offering violated the mandate in Section 1123(a)(4) that a plan must "provide the same treatment for each claim or interest of a particular class."

The right to propose a different plan after filing to compete with the prepackaged plan didn't mean there was equality of treatment. Rather, Judge Hanen held in his September 25 opinion that all creditors in the class should have been given the opportunity to participate in the backstop. In other words, Judge Hanen wouldn't countenance shutting out part of a group of creditors during negotiations on a prepackaged chapter 11 plan, in the process giving better treatment to some class members but not others.

Judge Hanen reversed and remanded, evidently meaning for the bankruptcy court to rejigger the equity of the reorganized debtor while possibly moving cash among members of the affected class of secured creditors.

The Prepack and the Backstop

A software developer, the debtor had negotiated a restructuring support agreement before filing with the holders of 81% of the first- and second-lien notes. The chapter 11 plan eliminated $1.6 billion in secured debt. Unsecured creditors were to be paid in full.

First-lien holders took back debt alongside the right to receive new equity at a 35% discount in a $245 million equity rights offering. Second-lien holders were slated to receive new equity.

To supply the cash required to operate the reorganized business and to confirm and consummate the plan, a self-selected majority of the lenders backstopped the equity rights offering. In return, the majority were to receive a 10% premium on the recovery for their claims through discounted equity purchases.

A minority of the lenders objected to the plan because they sought but were denied the opportunity to participate in the backstop, which would have given them an increased recovery on their claims. They contended that the plan violated Section 1123(a)(4), which requires the same treatment for every claim in a class.

Playing an important role in his decision to reverse confirmation, Judge Hanen said that the debtor did not commission a market test for the value of the consideration given in connection with the backstop.

The bankruptcy court confirmed the plan, finding that the backstop was both necessary and reasonable, according to Judge Hanen. He went on to say that the "Bankruptcy Court did not apply a market-test requirement, holding that neither the United States Supreme Court nor the Fifth Circuit require it for financing opportunities like the backstopping opportunity at issue here."

Not Equitably Moot

The minority appealed. Waiting several days, the minority filed a motion for a stay pending appeal in district court. Judge Hanen denied the stay motion, finding, among other things, that the minority had not shown irreparable injury because monetary damages could rectify problems with the plan.

Following denial of the stay motion, the debtor and the majority lenders filed a motion to dismiss the appeal as equitably moot. Judge Hanen denied the motion in an opinion in October, explaining how he "found that relief *could* be granted without unwinding the Plan or unfairly damaging the rights of third parties . . . ." [Emphasis in original.] *Ad Hoc Group of Excluded Lenders v. Convergeone Holdings Inc.*, 24-02001, 2024 BL 379892 (S.D. Tex. Oct. 23, 2024). Click here to read ABI's report, where we said, "reversal could mean redistribution of the new debtor's equity."

LaSalle and *Serta Simmons*

Having decided in October that confirmation was not immune from reversal, Judge Hanen turned to the merits, noting how the minority argued that the majority were in line for a 30% greater recovery on their claims for having been allowed to participate in the backstop. In defense, the majority claimed that the larger recovery was justified by the new consideration provided by financing the backstop.

The minority contended that different treatment was impermissible unless all members of the class had been permitted to participate in the backstop or there had been a market test.

As principal authority, Judge Hanen identified *Bank of America National Trust & Savings Association v. 203 N LaSalle St. Partnership,* 526 U.S. 434 (1999), and the Fifth Circuit's recent decision in *In re Serta Simmons Bedding, LLC,* 125 F.4th 555 (5th Cir. Dec. 31, 2024).

In *LaSalle*, a senior class had objected to confirmation on the ground that the plan violated the absolute priority rule in Section 1129(b). Judge Hanen read the Supreme Court as having "rejected a reorganization plan that gave a debtor's pre-bankruptcy equity holders the exclusive opportunity to receive ownership interests in the reorganized debtor if they would invest new money in the reorganized debtor. [*LaSalle*, *supra*] at 437."

Judge Hanen said that a "troubling issue" in *LaSalle* was how "the equity holders who were being prioritized paid nothing for the opportunity to invest new money for an ownership interest, and that the debtor neither considered alternative ways of raising capital nor attempted to market test the plan. *Id.* at 458."

Judge Hanen said that *Serta Simmons* was of "utmost importance" in two respects. It prohibited different settlements among class members, and it "held that a plan must provide an equality of opportunity, even if equality of recovery does not necessarily result."

LaSalle and *Serta Simmons* led Judge Hanen to the same conclusion:

> [T]he exclusive backstopping opportunity present in this case constituted treatment for a claim and allowed for some class members to receive higher recoveries than others in the same class. Therefore, the backstopping opportunity that was offered to some free from competition, but not all, class members violated 11 U.S.C. § 1123(a)(4).

A Competing Plan Wasn't an Antidote

Judge Hanen rejected the idea that the minority lenders were not "really excluded" because they were at liberty to file a competing plan once the chapter 11 case began. He said that the minority lenders "were excluded from those negotiations [on the prepack] from beginning to end," meaning that the ability to file a competing plan was "illusory at best." It was therefore "undisputable" that "the backstopping agreement was an exclusive opportunity given to a subset of class members without giving the Minority Lenders the chance for inclusion."

Moreover, Judge Hanen said that the majority were given their "*exclusive* opportunity to backstop the equity-rights offering without providing any up-front value in exchange for the opportunity." [Emphasis in original.] In addition, there was no "accurate market valuation of the backstopping opportunity."

Judge Hanen pointed to the Seventh Circuit for having "rejected the idea that the mere opportunity to propose a competing plan was sufficient to 'market test' the plan and instead required competitive bidding." *In re Castleton Plaza LP,* 707 F.3d 821, 823 (7th Cir. 2013). Regardless of whatever definition there might be for "market test," he said that "there was no such test here."

Judge Hanen concluded "that the exclusive backstopping opportunity provided to the Majority Lenders likely constitutes unequal treatment among creditors for their claim in violation of the Bankruptcy Code."

Serta Controls

Judge Hanen said that his holding "is also independently supported by the Fifth Circuit's opinion in *Serta*," because "the Court must examine the inequality both in opportunity and result."

"In this case," Judge Hanen said, the plan "may be factually distinguishable from the plan in *Serta,* [but] this Court is not persuaded that it is legally distinguishable. In fact, this case is perhaps more straightforward. In *Serta,* indemnity was offered to all creditors." In the case before him, "there was not even any pretense of equal participation."

"Since this pre-planned arrangement constituted unequal treatment, the backstopping and equity-rights aspect of the Plan violated the equal-treatment requirement of § 1123(a)(4)," so Judge Hanen reversed and remanded "for further proceedings consistent with the Court's decision."

Observations

At the conclusion of our report on Judge Hanen's denial of the motion to dismiss based on equitable mootness, we said,

> In the event of reversal, the appellate court could remand for the bankruptcy court to decide whether there is an available remedy, possibly partial. After all, deciding whether there is an available remedy sounds like a factual question that should be addressed in the trial court, which is already vastly more familiar with the case.

That's what Judge Hanen did. He remanded for the bankruptcy court to devise an appellate remedy given the bankruptcy court's greater familiarity with the case. The remand for an appellate remedy also apparently means there can be no appeal unless Judge Hanen certifies the case for an interlocutory appeal to the Fifth Circuit.

The opinion is *Ad Hoc Group of Excluded Lenders v. Convergeone Holdings Inc.*, 24-02001 (S.D. Tex. Sept. 25, 2025).

In chapter 11, the few decisions are split over the debtor's ability to stretch out the cure of home mortgage arrears over the life of the plan.

Like Chapter 13, Chapter 11 Debtors Can Cure Mortgage Arrears over the Plan's Life

On an issue in chapter 11 where the few decisions disagree, Chief Bankruptcy Judge Peter W. Henderson of Peoria, Ill., decided that the rules in chapter 11 regarding curing arrears on a home mortgage are the same as in chapter 13 in the sense that the debtor can cure arrears over the life of the plan and need not cure arrears all at once on confirmation.

The husband-and-wife debtors had so much in student loans that they did not qualify for chapter 13. In chapter 11, the couple owned a home with a $125,000 mortgage in arrears for some $13,000. They proposed a plan to cure the arrears over the five-year life of the plan while continuing to make regular mortgage payments. The mortgage would not mature until 2049.

Relying on the antimodification provision in Section 1123(b)(5), the mortgage lender objected to the plan, contending that a home mortgage must be cured in full by confirmation of a chapter 11 plan, unlike chapter 13.

Mortgage Cures in Chapter 13

Section 1322(b)(2) was part of the Bankruptcy Code at adoption in 1978. It provides that a chapter 13 plan may modify a secured claim, but not "a claim secured only by a security interest in real property that is the debtor's principal residence." An identical provision, Section 1123(b)(5), was added to chapter 11 in 1994.

"Despite the categorical language of the anti-modification provision," Judge Henderson said in his May 29 opinion, "some changes to the parties' original bargain are permitted in bankruptcy," citing *Nobelman v. American Savings Bank*, 508 U.S. 324, 330 (1993).

Of significance, Judge Henderson noted that 1123(b)(5), "unlike most other cure provisions in the Code, does not specify a time by which a debtor must cure the default." He cited three bankruptcy court decisions, one holding that a home mortgage cure in chapter 11 must be completed by confirmation, while two courts held that a chapter 11 debtor may stretch out a cure until completion of plan payments.

In addition to Section 1322(b)(2), Judge Henderson pointed out that a chapter 13 debtor may also cure mortgage defaults under Section 1322(b)(3) or Section 1322(c)(2). Whichever provision applies, he said that the defaults are cured no later than the end of the plan.

No Statutory Time Limitation in Chapter 11

In chapter 11, Judge Henderson said that some provisions are similar and some are different. Although Section 1123(a)(5)(G) permits curing a default "just like Section 1322(b)(3)," he said,

> No analog to §1322(b)(5) exists in Chapter 11, but Chapter 11 does not limit the duration of a plan, so there is no need to provide for the situation in which a long-term debt will need to be paid after the plan is finished.

"Another difference," Judge Henderson said, "is that a short-term home mortgage may not be modified in Chapter 11; section 1322(c)(2) is unique to Chapter 13."

"Because sections 1123(a)(5)(G) and 1322(b)(3) both permit a plan to provide for the curing of any default," Judge Henderson said, "they should be read as permitting the same treatment of home mortgage claims . . . . There is no reason to think that §1123(a)(5)(G) is subject to more restrictions than §1322(b)(3)."

In chapter 11, a debtor could confirm a plan with the home mortgage lender treated as unimpaired by curing arrears at confirmation. Or, Judge Henderson said, the debtor could confirm a cramdown plan over the lender's objection by treating the lender as impaired and "propos[ing] a plan that provides for the curing of the default over time. See §1123(a)(5)(G)."

Summarizing, Judge Henderson said there is "no single path in either Chapter 11 or Chapter 13 to cure a default on a home mortgage." Regardless of which path a debtor follows, he said,

> [A]ll paths lead to the same outcome: at the time the debtor emerges from bankruptcy with their fresh start, their relationship with their home mortgage lender must be restored to the *status quo ante* to avoid offending the antimodification provision. A debtor may not use bankruptcy to rewrite their relationship with their home mortgage lender going forward, but bankruptcy gives them the power to repair the past.

Judge Henderson overruled the lender's objection to confirmation based on the failure to cure the arrears by confirmation.

The opinion is *In re Koetters*, 25-80895 (Bankr. C.D. Ill. May 29, 2026).

Stays & Injunctions

In bankruptcy, the Ninth Circuit holds that delay is presumed to result from arbitration.

Ninth Circuit: No Arbitration of a Core Claim Alleging Usury in an MCA

Writing in absolute terms, the Ninth Circuit held in a *per curiam* opinion that a debtor's adversary proceeding to recover damages for an allegedly usurious loan is not subject to arbitration.

In the May 21, nonprecedential opinion, the circuit cited the Supreme Court in saying that the lender who made the allegedly usurious loan was automatically entitled to a stay pending appeal from denial of a motion to compel arbitration.

The Merchant Cash Advance

The statement of facts in the *per curiam* opinion were sparse. The following are taken from the parties' briefs:

The corporate Subchapter V debtor was a dental practice which had a "Forward Purchase Agreement" with an entity we shall refer to as the lender. The arrangement, commonly known as a merchant cash advance, called for the lender to purchase future accounts receivable.

According to the debtor, the last transaction was the debtor's sale of about $190,000 in future receivables in return for almost $75,000 in cash from the lender and the application of some $48,000 to pay off prior advances.

In Subchapter V schedules, the debtor listed the lender's claim as disputed and disclosed that it had a usury claim against the lender. The lender filed a secured proof of claim for more than $110,000.

The debtor objected to the lender's claim and at the same time initiated an adversary proceeding against the lender, alleging that the transactions were usurious loans under state law. The appeal to the circuit was taken from the adversary proceeding.

The bankruptcy court sustained the claim objection when the lender did not respond. The lender responded to the adversary proceeding by filing a motion to compel arbitration, based on an arbitration clause in the loan agreement.

The bankruptcy court denied the arbitration motion by application of the Ninth Circuit's so-called *Thorpe* factors. *See In re Thorpe Insulation Co.*, 671 F.3d 1011 (9th Cir. 2012). The bankruptcy court determined that the claim objection and the adversary proceeding were "core" and that arbitration would interfere with the bankruptcy case.

The lender filed a notice of appeal and motions for a stay pending appeal. The bankruptcy court and the district court both denied the motions for a stay pending appeal. The district court dismissed the appeal for lack of appellate jurisdiction to review an interlocutory order.

The lender appealed to the circuit.

Meanwhile, the debtor confirmed a chapter 11 plan providing for recoveries from the lender to supplement distributions to unsecured creditors.

Stays and Appellate Jurisdiction

Citing *Coinbase, Inc. v. Bielski*, 599 U.S. 736, 740 (2023), the circuit held that the district court erred in denying a stay pending appeal because "Section 16(a)(1)(B) of the Federal Arbitration Act gave [the lender] a right to interlocutory appeal of the bankruptcy court's order denying its motion to compel arbitration." To read ABI's report on *Coinbase*, click here.

The circuit said that the district court misread *Coinbase* in believing that "an inherent conflict between the [Federal Arbitration Act] and the Bankruptcy Code [was] an obstacle to [the lender's] right to invoke" the FAA. The appellate panel said that the existence of a conflict between the Bankruptcy Code and the FAA was a merits question.

No Remand

When finding error in failing to dismiss for lack of appellate jurisdiction, a circuit court ordinarily remands for the lower court to consider the merits, but the panel said that the circuit "may nevertheless affirm on any basis presented in the record." The circuit panel said it could rule on the merits when "the record is sufficiently developed and we are 'in as good a position as the district court' to resolve the question."

The circuit panel said that the "district court's order denying leave [to appeal] reached what was, in substance, a merits holding under *Thorpe*," because the district court found that the outcome of the adversary proceeding "'seriously could offset [the debtor's] bankruptcy plans.'"

The circuit found "no need for the district court to further develop the legal issues" because the "district court would not undertake any additional factual development if we were to remand" and "would likely reach the same conclusion."

The Merits

On the merits, the circuit proceeded to review the bankruptcy court's denial of arbitration and found no abuse of discretion.

"Under *Thorpe*," the circuit said that "a bankruptcy court has no discretion to deny arbitration of non-core claims, but it has discretion to deny arbitration of core claims if it concludes that arbitration would conflict with the underlying purposes of the Bankruptcy Code." *Thorpe*, *supra*, 671 F.3d at 1020–22.

In the case on appeal, the lender admitted that the debtor's usury claim was core. The only remaining question was whether the bankruptcy court had abused its discretion.

The circuit described the distribution of assets and the debtor's fresh start as the "twin goals" of bankruptcy. The circuit panel recognized that an "arbitration-induced delay would frustrate those goals."

The lender contended that the bankruptcy court could not assume delay from arbitration without a finding of fact to that effect. *Thorpe* foreclosed the argument, the panel said.

Even if arbitration proceeds expeditiously, the panel quoted *Thorpe* for saying that "'[a]rbitration of a creditor's claim against a debtor, even if conducted expeditiously, prevents the coordinated resolution of debtor-creditor rights and can delay the confirmation of a plan of reorganization.'"

The panel also quoted *Thorpe* for saying "that the bankruptcy court 'would lose control over the timing of the reorganization because it would not have control over the timing of the arbitrations." *Id*. at 1023.

The panel affirmed the bankruptcy court's denial of the lender's arbitration motion.

The opinion *is Harada Family Dental Care PC v. Kapitus Servicing Inc. (In re Harada Family Dental Care PC*, 25-6945 (9th Cir. May 21, 2026).

A nationwide class action for a stay violation seems to be an open issue.

Over Dissent, the Fourth Circuit Says No Arbitration for Automatic Stay Violations

In a split decision, the Fourth Circuit upheld Bankruptcy Judge Paul M. Black, who had denied a motion to compel arbitration in a purported class action alleging violations of the automatic stay in consumer chapter 7 and 13 cases.

Two individual debtors, one in chapter 7 and the other in chapter 13, had credit card debt from the same lender. The lender had notice of the filings but allegedly took actions to collect the debt. One debtor had confirmed a chapter 13 plan, and the other had received a chapter 7 discharge.

Together as named plaintiffs in an adversary proceeding framed as a class action, the two debtors sued the lender, alleging willful violations of the automatic stay. They sought an injunction, compensatory damages, punitive damages and attorneys' fees under Sections 362(k) and 105.

Concededly, the credit card agreements had broadly worded clauses calling for arbitration of all disputes. The lender responded to the complaint with a motion to compel arbitration. Bankruptcy Judge Black of Roanoke, Va., denied the motion. He held that arbitration would irreconcilably conflict with the purposes of the Bankruptcy Code. He was affirmed on appeal. *Goldman Sachs Bank USA v. Brown*, 24-00490, 2025 BL 86807 (W.D. Va. March 17, 2024). To read ABI's report on the affirmance, click here. The lender appealed to the circuit.

The Test: 'Inherent Conflict"

For himself and Circuit Judge Pamela Ann Harris, Circuit Judge Paul V. Niemeyer began analysis of the merits by alluding to Section 362(k). With an exception that's not applicable, the subsection provides that "an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages."

The lender asserted that the subsection evinces no congressional intent to preclude arbitration. However, the lender conceded that the claims were constitutionally and statutorily core.

To decide whether the nature of the claims made a whit of difference, Judge Niemeyer alluded to the Federal Arbitration Act and noted how the Supreme Court had held that arbitration agreements must be "vigorously enforced." Although "arbitration is thus favored as a matter of public policy, so too is the process and relief afforded by the Bankruptcy Code," he said. "Indeed," he added, "it is assured by the Constitution."

Closer to home, Judge Niemeyer quoted the Fourth Circuit for saying that "the automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws."

Naturally, Judge Niemeyer devoted a substantial portion of his opinion to discussion of *Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 226 (1987), the leading authority from the Supreme Court on enforcement of arbitration in bankruptcy cases. In *McMahon*, the Court said that the FAA, like "any statutory directive, . . . may be overridden by a contrary congressional command." *Id*. at 226.

McMahon went on to say that the intent of Congress "will be deducible from the statute's text or legislative history, or from an inherent conflict between arbitration and the statute's underlying purposes." *Id*.

Bankruptcy's 'Underlying Purposes' Aren't Arbitrable

Because the Bankruptcy Code has no textual preclusion of arbitration, Judge Niemeyer searched for an "inherent conflict" between arbitration and the Bankruptcy Code's "underlying purposes." Unlike claims based on tort or contract, he said that "a § 362(k) claim arises from a violation of the bankruptcy court's stay, which falls within the authority of the bankruptcy court under the Bankruptcy Code's statutory framework." Moreover, the "bankruptcy stay . . . is foundational to the successful function of the bankruptcy purpose."

Judge Niemeyer went on to say that a "claim for violation of the stay is so critical because" it "supports 'a principal purpose of the Bankruptcy Code . . . to centralize disputes over the debtor's assets and obligations in one forum, thus protecting both debtors and creditors from piecemeal litigation and conflicting judgments.'" *Moses v. CashCall, Inc.*, 781 F.3d 63, 72 (4th Cir. 2015).

Judge Niemeyer held that granting the lender's motion to arbitrate "the plaintiffs' § 362(k) claim — a claim that has no independent grounding outside of the Bankruptcy Code — would thus undermine the needed centralization of claims and effectively allow [the lender], after allegedly violating the stay, to assert the primacy of a private contractual right over the collective interests of all other creditors. This would, we conclude, fundamentally interfere with a core purpose of the Bankruptcy Code."

"Beyond this degradation of a fundamental purpose of bankruptcy," Judge Niemeyer said that "arbitration of the plaintiffs' § 362(k) claim would, we conclude, also undermine the 'shield' created by the automatic stay." Arbitration, he added, "would diminish, if not eliminate, this breathing spell that the Code intended be enforced."

Judge Niemeyer ticked off the "inherent conflicts" between arbitration and the adjudication of a Section 362(k) claim in bankruptcy court:

> [T]he degradation of the bankruptcy court's core purpose of conducting comprehensive bankruptcy proceedings, the lack of centrality for dispositions, the erosion of the bankruptcy shield, the lack of uniformity, the lack of bankruptcy expertise, and the deterrent purposes of punitive damages.

Along with legislative history, Judge Niemeyer said that the foregoing factors "amply demonstrate that arbitration here would conflict with the underlying purposes of the Bankruptcy Code."

Noting that the Supreme Court had denied *certiorari* in 2018 and 2020 regarding arbitration in bankruptcy cases, Judge Niemeyer affirmed the denial of the motion to compel arbitration.

The Dissent

Circuit Judge Robert Bruce King dissented. He is of the opinion that arbitration was "readily compelled" by *McMahon* and *CashCall*. He saw "no conflict at all in arbitrating the plaintiffs' § 362 automatic bankruptcy stay claims because the success (or failure) thereof would neither add nor subtract a new creditor to these bankruptcies, nor would it serve to 'frustrate creditor distribution.' *See CashCall*, 781 F.3d at 93 (Davis, J., concurring)."

Judge King also believes that the majority "needlessly created a circuit split with the Second Circuit" in *MBNA America Bank, N.A. v. Hill*, 436 F.3d 104 (2d Cir. 2006).

Judge King would have reversed and remanded with instructions to compel arbitration.

Observations

The complaint in the case before the Fourth Circuit aimed to be a nationwide class action. Although the majority opinion is clear that the plaintiffs may pursue their own claims in bankruptcy court without arbitration, neither the majority nor the dissent discussed whether the bankruptcy court may entertain a nationwide class action. The issue, evidently, was not before the Fourth Circuit.

In the Second Circuit, class actions for violation of the discharge injunction are limited in scope to the district in which the bankruptcy court sits.

The first time the case came to the Second Circuit, the appeals court held that contempt proceedings for violation of the discharge injunction are not arbitrable and are in the exclusive jurisdiction of the bankruptcy court. *GE Capital Retail Bank v. Belton (In re Belton)*, 691 F.3d 612 (2d Cir. June 16, 2020), *cert. denied*, 141 S. Ct. 1513. To read ABI's report, click here.

This writer noted how *Belton* contained strongly worded *dicta* that the bankruptcy court may not maintain a nationwide class action to rectify violations of the discharge injunction.

On remand to the bankruptcy court, the bank filed a motion to strike the class action allegations. The bankruptcy court rejected the bank's plea to strike the class. The district court certified a direct appeal, which the circuit accepted.

In the Second Circuit for the second time, the appeals court held that a bankruptcy court may not enforce discharge orders entered in other districts, thus nixing the idea of a nationwide class action alleging contempt of the discharge injunction. *Citigroup Inc. v. Bruce*, 75 F.4th 297 (2d Cir. Aug. 2, 2023). To read ABI's report, click here.

In this writer's view, access to nationwide class actions in bankruptcy court for a stay or discharge violation is an open question.

Acknowledgments

Retired bankruptcy Judge Allan L. Gropper and Edward C. Boltz submitted an *amicus* brief in support of the debtor on behalf of the National Association of Consumer Bankruptcy Attorneys and the National Consumer Bankruptcy Rights Center.

The opinion is *Goldman Sachs Bank U.S.A. v. Brown*, 25-1439 (4th Cir. March 18, 2026).

ROCHELLE'S DAILY WIRE

Disagreeing with the district court's conclusion that an order was final, the Fifth Circuit held that the appeal did not divest the bankruptcy court of jurisdiction to impose sanctions.

Fifth Circuit Upholds $400,000 in Civil Sanctions for Violating a Confidentiality Order

Ruling on an appeal that had been pending for 21 months, the Fifth Circuit upheld Bankruptcy Judge Meredith S. Grabill, who had imposed $400,000 in sanctions on a lawyer for violating a confidentiality order by disclosing the identity of a priest accused of sexually molesting a minor.

Judge Grabill did not have authority to impose criminal sanctions. By upholding $400,000 in civil sanctions, the Fifth Circuit implies that the amount of a sanction is not pivotal in differentiating between civil and criminal sanctions.

Circuit Judge Priscilla Richman wrote the circuit's January 2 nonprecedential opinion. A footnote says that Circuit Judge Andrew S. Oldham concurred "in the judgment only." Judge Oldham wrote no concurrence explaining how he may have disagreed with Judge Richman.

The Archdiocese Bankruptcy

With the Archdiocese of New Orleans in chapter 11 to deal with sexual abuse claims, Judge Grabill entered an elaborate confidentiality order covering information and documents concerning sexual abuse claims. Defining "protected material," the order prohibited disclosure except to authorized persons and only for authorized purposes. If someone wished to make a disclosure that was not permitted, the order prescribed procedures for obtaining permission to disclose.

A lawyer represented four abuse victims who sat on the official creditors' committee. The lawyer was not counsel for the committee.

Representing the four committee members, the lawyer was privy to protected information about a particular priest, the allegations made against him and the resolution after an investigation by the archdiocese. The information also identified the high school where the priest worked.

Without obtaining an exception from the confidentiality order, the lawyer disclosed the information to a news reporter and to a relative who was the principal at the school where the priest worked. After the allegations appeared in the press, Judge Grabill directed the U.S. Trustee, the debtor and the committee to conduct an investigation that identified the lawyer as the source of the leak.

Although he did not do so immediately, the lawyer eventually admitted that he had given confidential information to the school and the press.

Judge Grabill removed the four committee members and replaced them. In her first order, she also said that the lawyer had disclosed confidential information "in direct violation" of the confidentiality order. The first order directed the lawyer to show cause why he should not be sanctioned. The lawyer appealed.

Despite the appeal, Judge Grabill went ahead with a hearing on the show cause order. The lawyer admitted that he had made the disclosures but maintained that he had not violated the confidentiality order because he did so for "legitimate compelling reasons — to protect minors."

Judge Grabill found a willful violation of the confidentiality order and imposed a $400,000 sanction, representing about half of the attorneys' fees incurred by the debtor and the committee in investigating the leak. *In re Roman Catholic Church of the Archdiocese of New Orleans*, 20-10846, 2022 BL 363965 (Bankr. E.D. La. Oct. 11, 2022). To read ABI's report, click here.

The district court affirmed the lawyer's appeal of the $400,000 in sanctions. *In re Roman Catholic Church of the Archdiocese of New Orleans*, 22-1740, 2026 BL 363, 2026 US App Lexis 32 (E.D. La. March 27, 2023). To read ABI's report, click here. The lawyer took a second appeal to the Fifth Circuit. Oral argument was held on April 3, 2024.

The First Order Wasn't a Sanction on the Lawyer

The lawyer raised several issues on appeal in the circuit. He led with an alleged denial of due process, based on the idea that the bankruptcy court had found him in contempt in the first order before he was afforded an opportunity to defend himself.

Judge Richman said that the lawyer failed "to appreciate" the limited scope of Judge Grabill's first order, where, she said, "the bankruptcy court made a preliminary finding that [the lawyer] violated the protective order" but "did not sanction [the lawyer] for his conduct at that time." Removal of his clients from the official committee was not a sanction but was a "prudential prophylactic step."

Furthermore, a prior Fifth Circuit panel had upheld Judge Grabill's removal of the four clients from the committee because there is no right to serve on a committee. *In re Roman Cath. Church of Archdiocese of New Orleans*, 101 F.4th 400 (5th Cir. 2024). To read ABI's report, click here.

Judge Richman rejected the idea that Judge Grabill's first order was "a non-monetary sanction due to his perceived reputational harms." Of particular significance, she said that Judge Grabill "did not consider [her first] decision regarding [the lawyer's] conduct to be final," because she was scheduling a hearing on an order to show cause where the lawyer had "adequate notice and an opportunity to rebut the charges against him."

The First Appeal Didn't Divest the Bankruptcy Court of Jurisdiction

As a second facet of his due process argument, the lawyer contended that his appeal from Judge Grabill's first order deprived the bankruptcy court of jurisdiction to impose the $400,000 in sanctions. The lawyer buttressed his argument by alluding to decisions by the district judge on the first appeal.

The district judge had denied the church's motion to dismiss the first appeal on the grounds that it was not a final order, but Judge Richman disagreed with the district court's conclusion that the appeal from the first order was final and appealable. Citing Fifth Circuit authority, she said that a "district court cannot impliedly grant leave to appeal by merely ruling on an appeal before it from the bankruptcy court."

Because the district court had not granted leave to appeal an interlocutory order, Judge Richman held that the lawyer's appeal from the first order was "premature and of no effect." Because the appeal from the first order had no effect on the lawyer, the appeal did not divest the bankruptcy court of jurisdiction to conduct a later hearing and hold the lawyer in contempt.

No Abuse of Discretion

Judge Richman rejected the lawyer's arguments to the effect that Judge Grabill abused her discretion by finding contempt and imposing $400,000 in sanctions. Even if the confidentiality order was overbroad, she held that the lawyer violated the order by "failing to follow" the terms of the order. Furthermore, the findings by Judge Grabill were "supported by competent evidence."

Similarly, Judge Richman dismissed the argument that there was no contempt and that the sanction was disproportionate because the lawyer was protecting children. Under Federal Rule 37(b)(2), she said that "a bankruptcy court may impose sanctions for the failure to obey discovery orders, including protective orders," and that courts have "broad discretion" to impose remedies "suited to the misconduct."

Since Judge Grabill's $400,000 sanction was about half of the fees incurred by the debtor and the committee as a consequence of the lawyer's violation of the confidentiality order, Judge Richman held "that the bankruptcy court did not abuse its discretion." She affirmed the district court's judgment affirming the bankruptcy court's finding of contempt and imposing sanctions.

The opinion is *Trahant v. Official Committee of Unsecured Creditors (In re Roman Catholic Church of the Archdiocese of New Orleans)*, 23-30466 (5th Cir. Jan. 2, 2026).

ROCHELLE'S DAILY WIRE

A bankruptcy court isn't bereft of jurisdiction over a personal injury tort action if it doesn't involve distributions of the estate.

Contempt Proceedings Are Core and Consent Not Required for Referral, Fifth Circuit Says

In early January, the Fifth Circuit upheld Bankruptcy Judge Meredith S. Grabill of New Orleans, who had imposed $400,000 in sanctions on a lawyer for violating a confidentiality order by disclosing the identity of a priest accused of sexually molesting a minor.

Arising from the same contempt proceedings, the Fifth Circuit has now handed down a decision that could be understood to mean in *dicta* that a bankruptcy court can enter a final order in a proceeding regarding a personal injury tort if the proceeding does not entail the allowance of a claim.

Note, however, that the February 11 *per curiam* opinion is nonprecedential.

Contempt of a Confidentiality Order

In an archdiocese chapter 11 case, a lawyer represented four sexual abuse tort claimants but was not counsel for the official committee. Bankruptcy Judge Grabill had entered a confidentiality order that prohibited revealing the identity of alleged abusers, among other things. As the circuit panel said in the new decision, the lawyer disclosed the identity of an alleged abuser "to a third party and the media on multiple occasions and in violation of the protective order."

Contempt proceedings ensued. Initially, Bankruptcy Judge Grabill removed the lawyer's four clients from the committee. The issue then arose as to who should receive notice of the removal order containing the name of the lawyer. Judge Grabill directed the debtor's counsel to serve the order on the entire mailing matrix, not just the limited special notice list.

Later, the contempt proceedings culminated in $400,000 in sanctions that Bankruptcy Judge Grabill imposed on the lawyer. The lawyer appealed, but the district court and the circuit both affirmed. *Trahant v. Off. Comm. of Unsecured Creditors (In re Roman Catholic Church of Archdiocese of New Orleans)*, No. 23-30466, 2026 WL 18901 (5th Cir. Jan. 2, 2026) (unpublished). To read ABI's report, click here.

While the sanctions appeal was pending, the lawyer filed a lawsuit in state court against the debtor's counsel and the debtor's service agent for having served the removal order on the entire service list. The suit sought damages for abuse of process and intentional infliction of emotional distress.

The debtor removed the suit to district court, where the district judge referred the suit to the bankruptcy court. Bankruptcy Judge Grabill denied a motion to remand and a motion for her recusal. Ultimately, Judge Grabill granted summary judgment in favor of the debtor's counsel and the service agent, reasoning that they were protected by derivative judicial immunity. The district court affirmed Judge Grabill's order, prompting the lawyer's appeal to the Fifth Circuit.

The Proceedings Were 'Core'

On appeal in the circuit, the lawyer argued that denial of remand was error because the bankruptcy court lacked jurisdiction and because the action was not "core."

The panel cited Fifth Circuit authority holding that "arising under" and "arising in" proceedings under 28 U.S.C. § 157(a) equate to core proceedings, and that a proceeding is core if it could only arise in a bankruptcy case.

Noting that the dispute arose from actions taken as the debtor's counsel and noticing agent, the panel held that the lawyer's suit was "undoubtedly a core proceeding." Because the claim was core, the panel said there was no error in refusing to remand or abstain.

Consent Not Required for Referral

The lawyer made a novel argument by contending that referral to the bankruptcy court was error absent the lawyer's consent.

"Stated plainly," the panel said, "consent is not required for core proceedings. Because [the lawyer's] claims are 'core,' the district court was permitted to refer this action to the bankruptcy court for all purposes without [the lawyer's] consent."

Next, the lawyer took the position that the bankruptcy court was bereft of authority to preside over his personal injury tort action by 28 U.S.C. § 157(b)(2)(B), which provides that core matters do not include "the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11."

The panel dispensed with the argument, saying that the lawyer "fail[ed] to explain how this action constitutes a liquidation or estimation of claims against the estate for purposes of distribution."

The lawyer took the position that he was entitled to a trial in district court, because Section 157(b)(5) provides that the "district court shall order that personal injury tort and wrongful death claims shall be tried in the district court . . . ."

The panel saw no need to reach the issue, because the bankruptcy court had core jurisdiction and "the district court [had] conducted a *de novo* review of the bankruptcy court's summary judgment order."

Recusal

The lawyer contended it was error for the bankruptcy judge not to have recused herself. To support his cause, the lawyer trotted out what the panel called a "mere collection of declarations from other people asserting that the declarants believe recusal [was] required."

The panel said that "the quantity of declarations a litigant compiles is not determinative on a question of recusal, especially where declarations appear to be form declarations." The panel saw no error in the denial of the motion to recuse, because the declarations "cannot support recusal where it is not otherwise required based on a judge's conduct."

Finding no error in granting summary judgment dismissing the lawyer's complaint, the panel affirmed.

The opinion is *Trahant v. Mintz (In re Roman Catholic Church of the Archdiocese of New Orleans)*, 25-30193 (5th Cir. Feb. 11, 2026).

Following Zale, a Dallas district judge required an adversary proceeding and punctilious compliance with Rule 65 to obtain a typical injunction protecting nondebtors at the outset of a chapter 11 case.

Nondebtor Preliminary Injunctions Require Adversary Proceedings, District Judge Says

A district judge in Dallas set aside an injunction barring suits against nondebtors entered in the early days of the reorganization of Genesis Healthcare Inc.

In her May 1 opinion, District Judge Jane J. Boyle required punctilious compliance with the rules for an adversary proceeding and meticulous findings of fact to justify a preliminary injunction protecting nondebtors.

Because Judge Boyle's reversal will not become effective until 14 days after entry, one assumes that the bankruptcy court will have time on remand to enter a temporary restraining order in an adversary proceeding reinstating nondebtor injunctions that Judge Boyle set aside.

Judge Boyle's opinion is mostly about procedure, not substance.

The Usual Nondebtor Preliminary Injunction

The debtor operates healthcare facilities throughout the country. Naturally, customers, patients and families had personal injury, negligence and wrongful death claims and lawsuits.

Typical for reorganizations of the sort, the bankruptcy court entered an injunction early in the case barring suits against nondebtors such as affiliates, professionals, employees who committed allegedly wrongful acts and staffing service providers who placed personnel at the facilities. The injunction also covered officers and directors.

Three groups of tort claimants opposed the injunction, appealed and sought a direct appeal to the Fifth Circuit. The appeals were consolidated.

No Direct Appeal

Judge Boyle began by disposing of the appellant's motion for a direct appeal to the circuit. Under 28 U.S.C. § 158(d)(2)(A), she said that the claimants would be entitled to a direct appeal if it were a "matter of public importance" and if an appeal would "materially advance the progress of the case."

Judge Boyle denied the motion for a direct appeal in four pages of analysis. Among other things, she said there was "no open question of law affecting this appeal" because the "outcome of these appeals is squarely controlled by *Feld v. Zale Corp. (In re Zale Corp.)*, 62 F.3d 746 (5th Cir. 1995)."

Similarly, Judge Boyle said that the importance of the issue to the parties "will not meet the standard if the issue can be resolved by the district court without resort to complex constitutional analysis or the like."

The tort claimants contended that a direct appeal was appropriate because the outcome would affect tort claimants and tortfeasors in the future. If she were to accept the argument, Judge Boyle said that "every appeal would meet the standard for direct appeal because of the possibility that a future court might cite the district court's opinion."

"The matters involved in this appeal, though important, do not directly impact the public in a way that justifies the exceptional recourse of direct appeal," Judge Boyle said, in denying the motion for a direct appeal to the circuit.

The Requirements of *Zale*

Addressing the merits of the injunction, Judge Boyle began with a discussion of *Zale*, which "squarely controlled." *Zale* involved the bankruptcy court's approval of a settlement that barred claims against an insurer.

Judge Boyle said that *Zale* "recognized that any § 105 injunction against a non-debtor could not, consistent with the bankruptcy code, be permanent" and that its "holding has been the law in the Fifth Circuit for decades." *Zale*, she said, held that a "temporary injunction might be proper under 'unusual circumstances.'"

Most applicable to the case on appeal, Judge Boyle said that *Zale* "addressed the procedural requirements for temporarily enjoining claims against non-debtors" and "held that this sort of injunction required an adversary proceeding."

The lack of an adversary proceeding was not the only shortcoming in the case on appeal. Quoting *Zale*, Judge Boyle said that "the bankruptcy court needed to have 'conducted the proper analysis and made the requisite [four] findings for entry of a preliminary injunction' before temporarily enjoining claims against non-debtors."

In *Zale*, Judge Boyle described the Fifth Circuit as having "held that the bankruptcy court's failure to follow proper procedure was an independently sufficient reason (alternative to lack of jurisdiction and lack of power) to reverse the decision."

An Adversary Proceeding Is Required

Judge Boyle noted how the tort claimants had not waived the right to an adversary proceeding. "Regardless of how robust the process was," she held that "the failure to provide an actual adversary proceeding after [tort claimants] invoked their rights is, on its own, reversible error," because "a preliminary injunction must adhere to the requirements laid out in FRCP 65(d)."

Among the procedural shortcomings in the bankruptcy court's injunction, Judge Boyle said that the injunction "referred to another document in its core description of the acts restrained, directly contravening FRCP 65(d)(1)(C)."

Judge Boyle analyzed whether the bankruptcy court's injunction included the required findings.

Regarding the likelihood of success on the merits, Judge Boyle said that "'success on the merits' cannot mean a permanent injunction restraining lawsuits against non-debtors because that relief is prohibited under Supreme Court and Fifth Circuit precedent, which the Bankruptcy Court appropriately recognized." In a bankruptcy case, she said that success could be "the successful sale of assets, confirming a plan, or something else."

Whatever it is, Judge Boyle said it "needs to be defined, and the Bankruptcy Court must determine that it is substantially likely to be reached to issue a temporary injunction."

Regarding the balance of harm from an injunction, Judge Boyle said that "the Bankruptcy Court appears not to have properly considered the weight of threatened harm to those opposing the injunction." Specifically, she said that the court "must consider the ongoing harm the claimants face while prevented from seeking relief to which they are entitled."

In the case on appeal, Judge Boyle said that the bankruptcy court "only considered" the debtor's "ability to continue to care for patients and pay employees."

The debtor's "lead argument," Judge Boyle said, was that the debtor and its "affiliated non-debtors had an 'identity of interests.'" That requirement, she said, was "necessary to establish that the Bankruptcy Court had power to act, but it does not fulfill the procedural requirements laid out in *Zale*."

Judge Boyle rejected the idea that the procedures used below were harmless error. She could not "assess the substantive propriety of the Extend Stay Order when procedural safeguards, including adherence to the preliminary injunction factors, were not followed."

Judge Boyle ended her opinion by rejecting the tort claimants' contention that nondebtor injunctions were precluded by *Purdue*. She conceded how "it seems odd that a bankruptcy court could do something temporarily that it does not have the power to do permanently. But that dichotomy has been the law in the Fifth Circuit since at least *Zale* . . . explicitly said that temporary injunctions were allowed in certain circumstances."

Judge Boyle held that *Zale* "controls" and that "the Bankruptcy Court's order does not conflict with *Purdue Pharma*." She vacated the bankruptcy court's injunction and remanded for further proceedings, noting that a "final judgment will follow but will not become effective until after fourteen days from entry as prescribed by FRBP 8025(a)."

Observations

Requiring an adversary proceeding to obtain a temporary and preliminary injunction protecting nondebtors makes the process more complex and possibly lengthier but should not alter the outcome.

The four requirements for a preliminary injunction are standard, and their explicit invocation challenges the bankruptcy judge to write an opinion finding facts to justify an injunction.

Procedurally, the requirement of an adversary proceeding seems to mean that the targets of an injunction presumably should be named in the complaint and receive service of a summons and complaint.

But what about unknown targets of the injunction or third parties who may in the future aim to sue nondebtors? Should the complaint include defendants John and Jane Does 1 to 1,000? Must there be notice by publication in every location where the debtor had operations?

The requirement of an adversary proceeding will raise questions in the future. Will appellate courts everywhere require an adversary proceeding or permit a contested matter if the requirements for an injunction have been satisfied?

Disclosure

This writer's brother's law firm was among those representing tort claimants on the appeal.

The opinion is *In re Genesis Healthcare Inc.*, 25-2963 (N.D. Tex. April 1, 2026).

The ipso facto clause prohibits the loss of management rights in a limited partnership just like it does for a limited liability corporation.

State Law Can't Terminate a General Partner's Management Right by Filing Bankruptcy

State law automatically terminating a general partner's management rights in a limited partnership upon the general partner's bankruptcy violates the so-called *ipso facto* clause in Section 541(c)(1)(B).

The Ninth Circuit Bankruptcy Appellate Panel therefore held that limited partners violated the automatic stay when they replaced the general partner following the general partner's bankruptcy.

In short, the law on limited partnership is the same in that regard as it is for limited liability corporations.

Removal of the General Partner

A corporation was the general partner in a limited partnership that had several limited partners. The limited partnership had owned real property. The partnership agreement gave the general partner "all decision-making authority," including the right to refinance the property.

When disputes arose between the limited partners and the general partner, the general partner put itself and the limited partnership into chapter 11. A year later, the limited partners exercised powers under California law to remove the general partner and install a new general partner.

The creditors' committee in the jointly administered cases moved in bankruptcy court for a declaration that removal of the general partner violated the automatic stay and was void. Bankruptcy Judge Charles D. Novak of Oakland, Calif., agreed with the committee and decided that state law was inconsistent with the prohibition of *ipso facto* clauses. The new general partner appealed to the BAP.

Management Rights Are Estate Property

For the BAP in her June 29 opinion, Bankruptcy Judge Julia W. Brand first dealt with the new general partner's contention that there was no stay violation because management rights were not estate property.

Judge Brand defined the question as "whether certain California limited partnership statutes are preempted by the Bankruptcy Code." The issue, she said, was a matter of first impression in the Ninth Circuit and one not decided by the California Supreme Court.

Although the scope of estate property in Section 541(a)(1) "is intended to be broad," Judge Brand cited *Butner* for the principle that the nature and extent of an interest in property is determined by state law.

Judge Brand described California law governing limited partnerships as creating "a statutory management interest for a general partner in a limited partnership" but "provid[ing] for the termination of this management right upon a general partner's bankruptcy filing."

Citing a 2018 BAP decision, Judge Brand said that the former general partner's "pre-bankruptcy rights included, among other things, its statutory and contractual right to manage" the limited partnership and that the "[p]repetition contract rights are property of the estate." Even though management rights are not transferrable, she said it "does not mean that such rights do not exist or are not a property interest of that partner."

Judge Brand therefore held that management rights "became property of the estate."

Preemption

State law provides that a general partner is "disassociated" from the partnership on the general partner's bankruptcy. Therefore, the new general partner took the position that management rights did not become estate property.

Judge Brand countered with the *ipso facto* clause in Section 541(c)(1)(B), which provides that "an interest of the debtor in property becomes property of the estate . . . notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law . . . (B) that is conditioned on the insolvency or financial condition of the debtor [or] on the commencement of a case under this title. . . ."

Quoting a decision by Bankruptcy Judge Christopher Lopez of Houston, Judge Brand said that "'parties cannot contract around what becomes estate property, and states cannot legislate estate property away.'" Holding that "that these *ipso facto* clauses are preempted by the Bankruptcy Code," she said, "Many courts have reached the same conclusion with respect to similar nonbankruptcy law provisions."

The new general partner argued that the authorities dealt with limited liability corporations and were not applicable to limited partnerships. Judge Brand regretted the "dearth" of authority regarding limited partnerships, but said, "this is a distinction without a difference." She saw "no logical reason why the result should be any different in a partnership case."

Non-Assignability

The new general partner took the position there was no estate property because the general partnership interest was not assignable. Even were it true, Judge Brand responded by citing the Ninth Circuit for having "held that an executory contract, regardless of whether it is assumable or assignable, is property of the estate protected by the automatic stay."

Judge Brand ruled that the limited partners' removal of the general partner was void and violated the automatic stay in Section 362(a)(3) by having taken an action "to exercise control over property of the estate." She affirmed the bankruptcy court.

The opinion is *Andrew v. Official Committee of Unsecured Creditors (In re Lefever Mattson Corp.)*, 25-1238 (B.A.P. 9th Cir. June 29, 2026).

Retention & Compensation

The pricey litigation funding agreement had not been disclosed to creditors before confirmation.

Removal of Liquidating Trustee for Undisclosed Funding Agreement Affirmed

A district judge affirmed Bankruptcy Judge Stacey G.C. Jernigan of Dallas for having removed a liquidating trustee who made a litigation funding agreement without court approval and without notifying creditors. The funding agreement was remarkable in that the funder could have received several times its investment and the lion's share of recoveries.

The Post-Confirmation Financing

The corporate debtor sold the assets and confirmed a chapter 11 plan creating a litigation trust to pursue lawsuits that would be unsecured creditors' only recoveries.

The individual who had been the financial advisor for the unsecured creditors' committee was made the liquidating trustee by the plan, and the liquidating trustee engaged the law firm that had represented the committee.

Nine months after confirmation, the liquidating trustee filed a $100 million lawsuit in bankruptcy court, naming 22 defendants who were insiders or affiliates. The claims included fraudulent transfers and breaches of fiduciary duty.

Before the lawsuit was filed, the liquidating trustee entered into a litigation funding agreement obligating the funder to advance $2.325 million toward counsel fees.

As District Judge Brantley Starr described in his July 20 opinion, the funder had the right to review a proposed settlement two business days before "it could be finalized." He described the funder's compensation by saying that the funder "would receive three times whatever the litigation funder funds ($6,975,000) plus 12% of any litigation proceeds exceeding $6,975,000."

At a status conference three years later, Judge Jernigan learned about the funding agreement "somewhat inadvertently" and entered an order to show cause directing the liquidating trustee to produce the funding agreement and explain his authority to enter into it. She denied the liquidating trustee's request to have the agreement filed under seal.

Judge Starr described Judge Jernigan as finding that the funding agreement was not a "reasonable business judgment." Judge Starr cited one of Judge Jernigan's hypotheticals where the trustee settled for $10 million. The funder would receive more than $7.3 million, leaving some $500,000 for creditors, because the trustee's attorneys were owed more than $2.1 million.

Judge Jernigan removed the liquidating trustee, who appealed.

Jurisdiction

The removed trustee challenged the bankruptcy court's post-confirmation jurisdiction. Judge Starr framed the issue as whether the trustee had authority to enter into the funding agreement.

Judge Starr found jurisdiction because "this issue is a matter pertaining to the implementation and execution of the Plan."

The plan also reserved jurisdiction to remedy inconsistencies with the plan. Judge Starr said there would be jurisdiction "if the Agreement was found to be inconsistent with the Plan."

Authority for the Agreement

Judge Starr next addressed the question of whether the liquidating trustee had authority to enter into the funding agreement.

No one espoused the idea that the plan expressly authorized the liquidating trustee to make the agreement, but the trustee contended that he had authority to make agreements "necessary" in administration of the trust without court approval.

Judge Jernigan had held that the agreement was inconsistent with the plan's anticipated funding for the trust. Judge Starr agreed with Judge Jernigan that the plan did not give the trustee authority "to enter into an agreement that would place a funder's interests above creditors, without first disclosing the agreement to the creditors."

Judge Starr said that Judge Jernigan was interpreting the plan that she had confirmed. He therefore deferred to Judge Jernigan's "reasonable interpretation."

Even without deferring to the bankruptcy court's interpretation of the plan, Judge Starr held that the "Agreement was an unnecessary contract [in] the administration [of] the Trust." He said that the word "necessary" was not defined but means "absolutely necessary."

Given that the benefits from the agreement "primarily run to [the funder] and not the creditors," Judge Starr said that he "cannot conclude that the Agreement was absolutely needed to administer the Trust to the benefit of the creditors."

Authority to Remove the Trustee

The litigation funder took the position that the bankruptcy judge had no jurisdiction to remove the trustee after confirmation. In response, Judge Starr quoted Section 105(a), which provides:

> No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, *sua sponte*, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

Because "the bankruptcy court could *sua sponte* issue an order necessary to enforce the Plan," and because the liquidating trustee "entered into without authority under the Plan," Judge Starr held that the liquidating trustee "abused his discretion as trustee." He ruled that "the bankruptcy court's order removing [the liquidating] trustee was proper under section 105(a) to enforce a court order and prevent an abuse of process."

Finding jurisdiction and no abuse of discretion, Judge Starr affirmed.

The opinion is *Litchfield Ventures LLC v. Jones (In re Fresh Acquisitions LLC)*, 25-2282 (N.D. Tex. July 20, 2026).

Reversing the bankruptcy court, a district judge in Arizona held that counsel for a deposed Sub V debtor was entitled to compensation from the estate for confirming a chapter 11 plan after the debtor was removed as debtor in possession.

Counsel for a Deposed Sub V DIP Is Entitled to Compensation from the Estate

Reversing the bankruptcy court, a district judge in Arizona held that counsel for a Subchapter V debtor that had been removed as debtor in possession is eligible for compensation under Section 503(b)(1)(A) for having prosecuted confirmation of a chapter 11 plan.

As described in greater detail by the bankruptcy judge, the corporate debtor was a medical practice with revenue of $25 million and no secured debt. The primary unsecured creditor had a claim for $12 million. On motion by the creditor, the bankruptcy court removed the debtor as debtor in possession three months after filing.

Debtor's counsel filed a Subchapter V plan three weeks after the debtor in possession was deposed. Following six months of litigation with the creditor, the bankruptcy court confirmed the debtor's chapter 11 plan.

The debtor's counsel filed a fee application for about $1.3 million covering work performed from the time the debtor was deposed through plan confirmation. The lender objected, contending that counsel for a dispossessed debtor is not entitled to compensation from the estate as a matter of law.

The bankruptcy court agreed with the objecting creditor and held that the debtor's counsel was not entitled to compensation from the estate, even though the debtor had confirmed a chapter 11 plan. *In re Athena Medical Group LLC*, 672 B.R. 788 (Bankr. D. Ariz. July 29, 2025). To read ABI's report, click here.

The debtor's counsel appealed and won in an opinion on July 13 by District Judge Susan M. Brnovich of Phoenix.

Lamie Once Again

Judge Brnovich surveyed the statutory landscape in Subchapter V, beginning with Section 1184, which gives the debtor in possession all of the powers of a trustee except for compensation and for "the duties specified in paragraphs (2), (3), and (4) of section 1106(a)." Thus, she said, the debtor in possession had the right to retain counsel. Indeed, the bankruptcy court had authorized the retention of counsel for the debtor in possession, or DIP.

Retained professionals, of course are entitled to compensation under Section 330(a)(1).

However, Judge Brnovich quoted *Lamie*, where the Supreme Court held "'that § 330(a)(1) does not authorize compensation awards to debtors' attorneys from estate funds, unless they are employed as authorized by § 327.' *See Lamie v. U.S. Tr.*, 540 U.S. 526, 534 (2004)."

In the case on appeal, the DIP had been removed, or "dispossessed," under Section 1185(a), as Judge Brnovich said. Despite removal, she said that the debtor retained the exclusive right to file a plan, because Section 1189(a) provides that "[o]nly the debtor may file a plan under this subchapter."

The right to file a plan, Judge Brnovich said, continues to apply "regardless of whether the debtor is dispossessed."

The debtor's counsel had three theories underpinning the right to compensation even though the firm was no longer serving the DIP. Judge Brnovich rejected two of counsel's three theories, but one was enough for reversal.

Rejected Theories

The debtor's counsel took the position that it had a right to compensation under Section 330(a) because the debtor retained the exclusive right to propose a plan.

Judge Brnovich rejected the theory, because a deposed Subchapter V debtor does not retain the right to retain counsel under Section 327(a). Consequently, she reasoned, Section 330(a) is inapplicable because Section 330(a) pertains only to professionals "employed" under Section 327.

Next, the debtor's counsel argued that Section 330(a) allowed compensation because the firm had been retained under Section 327.

Judge Brnovich disagreed, because "the Supreme Court found that only attorneys employed under § 327 are entitled to § 330 compensation. *Lamie*, 540 U.S. at 538–539." She said that the debtor's firm "ceased to be a § 327 attorney upon the debtor's dispossession. *Id.* at 542." She saw "no indication that § 1189 [the debtor's exclusive right to file a plan] somehow overcomes *Lamie*'s conclusion . . . ."

The Winning Theory

Judge Brnovich agreed with counsel that the firm was entitled to compensation as an administrative expense under Section 503(b)(1)(A). The subsection allows administrative claims for "the actual, necessary costs and expenses of preserving the estate including . . . wages, salaries, and commissions for services rendered after the commencement of the case . . . ."

By seeking allowance of an administrative expense, Judge Brnovich said that counsel was "not . . . circumventing §§ 327, 330 and 503(b)(2) because those statutes are inapplicable in the first instance."

While Section 330(a) allows compensation for "actual" and "necessary" expenses, Judge Brnovich said that "Section 503(b)(1)(A) employs a materially similar standard." In other words, "§ 503(b)(1)(A)(i) envisions that providers may be paid for services that do not fall under §§ 327, 330, and 503(b)."

Judge Brnovich reversed and remanded for further proceedings "consistent with this order." Suggesting that reversal doesn't mean that counsel are entitled to everything they sought, she said, "not every service rendered by such professionals will be … 'actual, necessary costs and expenses of preserving the estate.'"

Given that counsel prosecuted a confirmed plan, Judge Brnovich had words that counsel likely will cite on remand in bankruptcy court: "[T]o the extent equities are of any tangential concern," she said, "the Court separately notes that the equities favor [the law firm]."

The opinion is *Athena Medical Group LLC v. Wound Care Specialists LLC*, 25-02926 (D. Ariz. July 13, 2026).

When their recoveries were limited to a fixed amount in a pot, unsecured creditors had no financial interest in fee allowances and were no longer parties in interest under Section 1109(b).

After Confirming a Fixed-Pot Plan, Unsecured Creditors Lack Standing for Fee Objections

When unsecured creditors of a chapter 11 plan are only entitled to payment of their claims from a fixed sum of money held in a trust, they don't have standing to object to remaining applications for allowances of compensation, for reasons explained by Bankruptcy Judge Meredith S. Grabill of New Orleans.

In her March 10 opinion, Judge Grabill described the tortured history of the six-year reorganization of the Roman Catholic Church of the Archdiocese of New Orleans. In the last year or two of the case, a group of holders of sexual abuse claims began objecting to interim allowances of compensation sought by counsel for the debtor and the official committee.

While the objections were pending, the debtor reached a compromise leading to confirmation of a chapter 11 plan that created a $230 million trust for creditors with abuse claims. Regardless of the ultimate amount of allowed abuse claims, Judge Grabill said that the abuse claimants' "monetary recovery is limited exclusively to the" trust.

Constitutional Standing

With a hearing approaching on interim and final allowances of compensation after confirmation, counsel for the debtor and the committee objected to the abuse claimants' standing to object to allowances.

With regard to constitutional standing, Judge Grabill said that the claimants were not invoking federal jurisdiction in objecting to allowances of compensation, nor were they required to. Judge Grabill cited a decision by Bankruptcy Judge Craig T. Goldblatt of Delaware, who said last year that "only the party invoking the jurisdiction of a federal court — the one that is seeking relief — needs to have Article III standing." *In re AIO US Inc.*, 672 B.R. 261, 265 (Bankr. D. Del. June 6, 2025). To read ABI's report, click here.

In the archdiocese case, no one was questioning the constitutional standing of the law firms to assert their fee applications.

Nevertheless, Judge Grabill said that the objecting claimants "must qualify as 'parties in interest' under § 1109(b) of the Bankruptcy Code to appear and be heard regarding the Pending Interim Fee Apps."

Standing as 'Parties in Interest'

Section 1109(b) provides that a "party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a *creditor*, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter." [Emphasis added.]

Judge Grabill said that the definition of "party in interest" is "broad" but "not limitless." Again quoting *AIO*, she said that "'party-in-interest standing under § 1109(b) limits an objector to asserting its own rights — it may not assert the rights of others.'" *Id*. at 274.

More particularly, Judge Grabill quoted Bankruptcy Judge Martin Glenn of New York, who said that "an entity that does not hold a financial stake in the case is generally excluded from the definition of 'party in interest.'" *In re MF Global Holdings, Ltd.*, 469 B.R. 177, 188 (Bankr. S.D.N.Y. 2012).

In the case before her, Judge Grabill said that the question was "whether the standing conferred by § 1109(b) to [abuse claimants] during the pendency of the case extends post-confirmation or whether they forfeited their standing by entering into a settlement with the Archdiocese" providing that their recoveries would only come from the $230 million trust.

Judge Grabill distinguished a pair of cases involving confirmed plans where the recovery by objecting creditors would be affected by successful objections to professionals' compensation applications. In the case before her, she said that the abuse claimants "do not currently hold a pecuniary interest in the payment of attorneys' fees to counsel for the Reorganized Debtor and the former Committee" because their recoveries were "absolutely limited to the Settlement Trust."

Judge Grabill overruled the fee objections, holding that the objecting claimants lacked "standing under § 1109(b) to maintain their objections to the Pending Interim Fee Apps as well as to object to any final fee application filed in this case."

The opinion is *In re Roman Catholic Church of the Archdiocese of New Orleans*, 20-10846 (March 10, 2026).

The prohibition in Section 326(a) to calculating a chapter 11 trustee's commission on distributions to the debtor does not apply when creditors are paid in full and a distribution goes to equity security holders.

In a Surplus Chapter 11 Estate, Trustee Commissions Are Based on Distributions to Equity

When Bankruptcy Judge Alan S. Trust of Central Islip, N.Y., wrote his opinion on March 18, no circuit had spoken to whether the calculation of a chapter 11 trustee's commissions may include distributions to equity security holders when creditors are paid in full under a plan.

Parting company with two bankruptcy courts on a question that had not by that time been decided by any circuit court, Judge Trust concluded that the calculation of a chapter 11 trustee's commissions may include distributions to equity security holders when creditors are paid in full under a plan.

Then, on March 27, the Fifth Circuit ruled to the contrary and issued a nonprecedential opinion holding that a trustee's compensation may not be based on a surplus distribution to equity holders. *Henderson v. U.S. Trustee (In re VCR I LLC)*, 25-60204 (5th Cir. March 27, 2026).

Today, we report Judge Trust's decision. Tomorrow, we report the Fifth Circuit's *Henderson* opinion. After reading both reports, readers may form their own opinions about the better answer to a question not addressed directly by the statute.

The Surplus for Equity

After the corporate debtor was supplanted by a chapter 11 trustee, Judge Trust approved the sale of the debtor's real property for about $4 million. Under the confirmed chapter 11 plan, the sale price permitted the payment of creditors' claims in full with interest, leaving a surplus of more than $800,000 for distribution to the debtor's sole equity security holder, who happened to be the debtor's former principal.

The trustee filed an application for compensation requesting commissions based on the trustee's disbursements, including the distribution of surplus to the equity security holder. The U.S. Trustee objected on the grounds that Section 326(a) doesn't permit commissions based on distributions to former equity owners.

In his March 18 opinion, Judge Trust said that the "Second Circuit has not previously addressed the issue," and the "caselaw on this issue is sparse." Indeed, he said, "no Circuit has addressed this issue with respect to a chapter 11 surplus estate."

Section 326(a)

Eventually coming down on the side of the trustee, Judge Trust began with Section 326(a), which provides in pertinent part:

> In a case under chapter 7 or 11, other than a case under subchapter V of chapter 11, the court may allow reasonable compensation [on a sliding scale] under section 330 . . . for the trustee's services . . . upon all moneys disbursed or turned over in the case by the trustee to parties in interest, *excluding the debtor*, but including holders of secured claims. [Emphasis added.]

Citing the Supreme Court's *Jevic* decision, Judge Trust said, "The distribution scheme in chapter 11 is different than for cases commenced under chapter 7, as distributions in such cases are controlled by § 726(a)" and are "somewhat more flexible" in chapter 11.

'Debtor' and 'Equity Security Holder' Aren't the Same

The plan extinguished the principal's equity security interest but provided for a surplus distribution to the principal on account of his equity holding.

The U.S. Trustee contended that the equity security holder, who was the debtor's former principal, was essentially standing in the shoes of the debtor. Although the argument was "plausible," Judge Trust said that an equity holder is "clearly" not the debtor under the definitions of equity security holder and debtor in Section 101.

"Had Congress intended to include equity security holders as defined in § 101(17) or 'functional equivalents' of a debtor in the prohibition of § 326(a), it would have explicitly done so," Judge Trust said. Because "Congress did not include these terms within § 326(a) as the statute only excludes a commission on monies disbursed to a 'debtor,'" he concluded that "the term 'debtor' cannot be said to also include equity security holders or functional equivalents of a debtor."

Interpreting the confirmed plan and the Bankruptcy Code together, Judge Trust concluded that the surplus distribution was being made to the equity security holder, not the debtor. However, he discussed decisions from 2020 and 2024 where two courts concluded that a chapter 11 trustee could not be paid based upon distributions to equity holders.

One of the decisions was the district court opinion in *Henderson*, affirming the bankruptcy court and concluding that distributions to equity don't enhance a trustee's commission. *In re VCR I, LLC*, 23-CV-37, 2024 WL 1394507, at *1 (S.D. Miss. Mar. 30, 2024). The Fifth Circuit reached the same conclusion and affirmed, as we shall report tomorrow.

Judge Trust did not find either decision in the lower courts "to be persuasive."

Policy and Objectives

Beyond the statute, Judge Trust explained why his conclusion was "further supported by the objective and policy underlying § 326." Together, Sections 326 and 330 were designed "to maximize the distribution of assets to creditors." When creditors have been paid in full with interest, "allowing the trustee to receive a commission on distributions to equity security holders cannot be said to injure or even impact creditors," he said.

Of significance, Judge Trust added, "Equity security holders are not creditors."

"Congress excluded compensation of a chapter 11 trustee for distributions made to individual debtors under chapter 7 and chapter 11 but simply did not do so with respect to equity security holders of non-individual debtors," Judge Trust said.

"Applying the objective and policy behind § 326 to the facts here," Judge Trustee permitted the trustee to base the calculation of commissions on the distribution of surplus to the equity security holder, because those distributions "cannot be said to go against the overall purpose of § 326(a)."

The opinion is *In re South Broadway Realty Enterprises Inc.*, 23-74237 (Bankr. E.D.N.Y. March 18, 2026).

In a nonprecedential opinion, the Fifth Circuit concludes that a chapter 7 trustee's commissions are not based on distributions to equity holders, even when creditors are paid in full.

In a Surplus Chapter 11 Estate, Trustee Commissions *Aren't* Based on Equity Distributions

Yesterday, we reported how Bankruptcy Judge Alan S. Trust of Central Islip, N.Y., had no authority from a circuit court when he decided that a trustee's commission can be based on distributions to equity holders when creditors are paid in full with interest. *In re South Broadway Realty Enterprises Inc.*, 23-74237 (Bankr. E.D.N.Y. March 18, 2026). To read ABI's report, click here.

Nine days after Judge Trust decided *South Broadway*, the Fifth Circuit majority took the opposite tack in a nonprecedential decision on March 27, holding that a trustee's commission cannot be based on distributions to equity.

The facts before the Fifth Circuit, whose opinion we cover today, were basically the same as those in *South Broadway*.

Owning real property, the corporate debtor filed a chapter 11 petition, but the case converted to chapter 7. The chapter 7 trustee sold the property for almost $7 million.

There was one equity security holder. The corporate debtor was dissolved.

Claims were paid in full, resulting in a distribution of more than $2.6 million to the equity security holder. The trustee filed a final report, calculating the trustee's commissions based on inclusion of the distribution to equity.

The U.S. Trustee objected, taking the position that Section 326 does not allow calculation of commissions to include distributions to equity. The bankruptcy court agreed, and the district court affirmed. On a second appeal, the Fifth Circuit majority affirmed in a *per curiam*, nonprecedential opinion on March 27.

Functionally, Equity Holder Is the Debtor

On the merits, the circuit majority began with the relevant statutes. Regarding the calculation of a trustee's commissions, Section 326(a) provides, in pertinent part:

> In a case under chapter 7 or 11, other than a case under subchapter V of chapter 11, the court may allow reasonable compensation [on a sliding scale] under section 330 . . . for the trustee's services . . . upon all moneys disbursed or turned over in the case by the trustee to parties in interest, *excluding the debtor*, but including holders of secured claims. [Emphasis added.]

Because a trustee's commissions are based on "all moneys disbursed or turned over," the majority cited Section 726(a)(6), saying that "the remaining 'surplus' shall be distributed: 'sixth, to the debtor,'" after distributions to the five higher priorities under subsections (a)(1)–(5) have been completed.

Applying the law to the facts, the panel majority that the sole shareholder was "an equity security holder." However, the panel said, Section 726 "makes no mention of disbursements made to equity security holders."

"Instead," the panel said, "it mandates that estate property shall be distributed first as a payment in satisfaction of, or interest on, a 'claim,' *see* § 726(a)(1)–(5), and second, as a payment 'to the debtor,' *see* § 726(a)(6)." The equity security holder "does not squarely fit within either camp," the panel said.

"Similarly," the majority said that the equity security holder "cannot be a creditor."

Once all payments were made to creditors under subsections (a)(1)–(5), "the remaining surplus was statutorily required to be paid to the Debtor," the majority said. But by that time, the debtor "had been dissolved."

"So, while [the equity holder] is not a 'debtor' *per se* under Section 726," the majority said that the equity holder "functions as one here in the actual debtor's absence," and "it is to receive all disbursements to which [the debtor] would have been entitled." The majority therefore held:

> [The equity security holder] is the functional and practical equivalent of the debtor, only for the limited and agreed purpose of receiving surplus funds otherwise belonging to the debtor, so that the bankruptcy case may be closed. Accordingly, the Chapter 7 trustee is not entitled to compensation for that disbursement.

Contrary Arguments Rejected

The trustee contended that the equity security holder was a "party in interest" under Section 326(a), therefore entitling the trustee to commissions based on distributions to equity. "True," the majority said, "Section 326 allows reasonable compensation 'upon all moneys disbursed . . . by the trustee to the parties in interest.' 11 U.S.C. § 326(a)."

Assuming that "parties in interest" is ambiguous, the majority "resolve[d] such ambiguities in the context of other, similar statutes. *See City of Chicago v. Fulton*, 592 U.S. 154, 159 (2021). Read together with Section 726(a), 'parties in interest' must refer only to 'claimholders' and the 'debtor,' because the trustee is mandated to make disbursements to those parties."

The majority also rejected the idea that a trustee is entitled to larger compensation because a commission under Section 326 "is 'presumptively reasonable' and only to be reduced in extraordinary circumstances." The majority said, "Our holding today explains an existing limitation under the statute. It does not create one."

Affirming, the majority consisted of Circuit Judges Carolyn Dineen King and Leslie H. Southwick.

The Dissent

Circuit Judge Catharina Haynes disagreed, in a half page respectful dissent. She began by agreeing with the majority that the equity holder was not the debtor.

Because "11 U.S.C. § 326(a) very clearly says THE debtor (emphasis added)," Judge Haynes said that "the denial of being able to allow [the trustee] to receive a percentage from what was paid to [the equity holder] is wrong."

Judge Haynes elaborated, "The debtor . . . is very different from [the equity holder] who is not a debtor and has not been having those problems which makes an entity need to be a bankrupt debtor." She would remand for the bankruptcy court to recalculate the commission based on the distribution to the equity holder.

Note

There was no appeal from Judge Trust's order in *South Broadway*. Without an appeal, there will be no opportunity for the issue to reach the Second Circuit and possibly create a circuit split.

Observation

Imagine this: The corporate debtor with a surplus estate has hundreds or thousands of shareholders, perhaps both common and preferred shareholders. Predictably, there will be disputes about who is entitled to distributions and how much.

In a case like that, the trustee will shoulder responsibility, investigate the facts, make important decisions and expend considerable effort in the equity distribution. The trustee's professionals would be paid, but what about the trustee? Why should a trustee exercise fiduciary duties and oversee a process necessary for closing the estate without receiving compensation?

The opinion is *Henderson v. U.S. Trustee (In re VCR I LLC)*, 25-60204 (5th Cir. March 27, 2026).

Preferences, Fraudulent Transfers & Claims

Sixth Circuit holds that BFP from the Supreme Court does not apply to tax foreclosures and that there is no per se rule exempting tax foreclosures from preference attack.

Sixth Circuit Says Tax Foreclosures Can Be Avoided as Preferential Transfers

Circuit Judge John B. Nalbandian wrote a meticulous preference opinion.

In a May 27 opinion for the Sixth Circuit, Judge Nalbandian split with other courts by deciding that a *real estate tax foreclosure* can be a preference, notwithstanding the Supreme Court's decision in *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994), that a regularly conducted *mortgage foreclosure* is not subject to attack as a fraudulent transfer.

Judge Nalbandian held that a tax foreclosure was preferential in a chapter 13 case because foreclosure would have given the municipality a commission of 5% of the eventual sale price under state law, when the 5% commission would not have been an allowed secured claim in bankruptcy. He concluded that the municipality would have received more in foreclosure, therefore satisfying the "more than" requirement for a preference in Section 547(b)(5).

In a sense, finding a preference was twice nothing for the municipality, because the municipality had a valid, secured claim that would be paid in full in the chapter 13 case, including interest due under state law. The municipality would not receive the 5% sales commission, but the municipality in bankruptcy would not incur the trouble and expense of selling the foreclosed property.

The Multistep Tax Foreclosure

The tax foreclosure occurred in Michigan, where state law has a complex, years-long process before the owner loses all interest in the property. However, the owner never loses the right to the surplus, if any, after the property is sold to a third party, assuming the owner has taken the steps required for preserving the surplus.

In the case on appeal, the debtor owned real property with a fair market value of about $75,000. The property turned out to be the debtor's only potential asset with nonexempt value, Judge Nalbandian said.

For nonpayment of about $6,000 in real estate taxes, the municipality initiated foreclosure. The last two steps in foreclosure were pivotal for the preference analysis.

Two years earlier, the foreclosure process had given the municipality a super-priority tax lien. Then, there was a date outside the 90-day preference period when the municipality won a foreclosure judgment. Later still, there was a date by which the owner "forfeits" the property if the taxes were not paid; title vests "absolutely" in the municipality; the municipality has the right to possession, and the owner loses all rights to redemption, except the right to receive a surplus, if there is one, after the sale of the property by the municipality to a third party. We shall refer to that date as the "forfeiture date."

Less than 90 days after the forfeiture date, the debtor filed a chapter 13 petition and brought a preference action. If the preference action were to succeed, Judge Nalbandian said that the municipality would be paid in full, the mortgage lender would be paid in full, and almost $9,000 would remain for unsecured creditors.

The bankruptcy court granted the municipality's cross motion for summary judgment, dismissing the preference suit. The bankruptcy court decided that the transfer took place within the 90-day preference lookback but saw foreclosure as not giving the municipality more than it would have received in a hypothetical chapter 7 liquidation. The district court affirmed, bringing the appeal to the Sixth Circuit.

Transfer Within the Lookback

The appeal raised two questions: (1) the lookback period under Section 547(b)(4); and (2) the "more than" test under Section 547(b)(5).

The municipality took the position that the transfer occurred outside the 90-day preference period when the municipality won the foreclosure judgment.

Judge Nalbandian disagreed, concluding that Section 101(54)(D) put the transfer on the forfeiture date. Among four alternatives, the subsection defines a "transfer" to mean "each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with — (i) property; or (ii) an interest in property."

In deciding that the date of the transfer was the forfeiture date and not the foreclosure date, Judge Nalbandian based his holding on the debtor's right to redeem the property before the forfeiture date.

Buttressing his conclusion, Judge Nalbandian also held that the municipality had not perfected the transfer, as required by Section 547(e)(2), until a few days after the forfeiture date, when the municipality recorded title to the property.

‘More Than’

Judge Nalbandian turned to the question under Section 547(b)(5) of whether foreclosure would have given the municipality “more than such creditor would receive” in a hypothetical chapter 7 liquidation had the transfer not been made.

Immediately, Judge Nalbandian pointed to the 5% sales commission that the municipality would *not* have received in a hypothetical chapter 7 liquidation. Had the transfer *not* occurred before bankruptcy, the municipality would *not* have sold the property to a third party and would *not* have been eligible for the 5% commission under state law.

Judge Nalbandian dealt with uncertainties arising in a preference analysis. In part, he said,

> Because we’re dealing with hypotheticals, some uncertainty inheres in the Chapter 7 analysis. Predicting events and how trustees will administer estates “is not an exact science” and can require “an estimation of the value of all of the bankruptcy estate’s assets, including such hard to determine values as disputed and contingent claims, the potential disallowance of claims (under § 502(d)), [and] the probability of success and value of causes of action held by the estate.”

Among other things, he identified the amount that the municipality would have received through foreclosure as “less certain.” In the case on appeal, Judge Nalbandian said that the municipality had removed enough uncertainty by conceding that a sale at any range of prices would have paid the municipality’s claim in full, with interest.

Judge Nalbandian ruled that the “transfer [on the forfeiture date] enabled the Treasurer to receive more than he would’ve if the transfer hadn’t happened and the case was a Chapter 7 bankruptcy,” because “creditors in bankruptcy don’t receive sales commissions.” He therefore held that the debtor had satisfied her burden under the “more than” test, even drawing inferences in favor of the municipality based on disputed facts.

Distinguishing *BFP*

Ending the opinion with his most significant conclusions, Judge Nalbandian confronted the question of whether his decision was at odds with *BFP*, where the Supreme Court held that a regularly conducted mortgage foreclosure may not be attacked as a fraudulent transfer. Enlarging the anomaly seemingly created by his decision, he said,

> We recognize that a pre-petition transfer to a fully secured creditor isn’t usually a preferential transfer. But we reject a *per se* rule that would immunize property tax

> foreclosures from preferential status even when, as here, the creditor is drastically oversecured. Nothing in the Code prescribes such rigidity. [Citation omitted.]

Judge Nalbandian distinguished *BFP*, first by noting it dealt with fraudulent transfers, not preferences. Next, he noted that fraudulent transfers deal with "reasonably equivalent value," a term not appearing in Section 547.

Identifying the Supreme Court's limitations on its own opinion, Judge Nalbandian said,

> [T]he Court expressly limited its § 548 reasoning to mortgage foreclosures, acknowledging that "considerations bearing upon other foreclosures and forced sales (to satisfy tax liens, for example) may be different."

BFP, *supra*, 511 U.S. at 537, n.3.

"Still," Judge Nalbandian said, "some courts" have applied *BFP* "to find property tax foreclosures *per se* non-preferential." He then cited other courts that "have found property tax foreclosures preferential, rejecting the view that *BFP* foreclosed its conclusion or counseled against it."

Judge Nalbandian saw the "more than" element in Section 546(b)(5) as "clear and unambiguous," thus prohibiting considerations of policy from overcoming a "plain statutory command."

Judge Nalbandian reversed the district court's affirmance of the bankruptcy court's order granting the municipality's summary judgment order and reversed the bankruptcy court's denial of the debtor's motion for summary judgment.

Observations

This report does not do justice to the scholarship in Judge Nalbandian's opinion. In particular, he has written an exquisite analysis of the multiple hypotheticals raised in preferences. Anyone defending or prosecuting a preference action should read the opinion in full text to identify issues that are typically missed in preference litigation.

The opinion is *Reinhardt v. Prince (In re Reinhardt)*, 25-1072 (6th Cir. May 27, 2026).

The aim of recovering specific real property resulting from a fraudulent transfer entitled the plaintiff to a preliminary injunction.

Grupo Mexicano Was No Bar to a Preliminary Injunction in a Fraudulent Transfer Suit

Bankruptcy Judge Peter D. Russin of Fort Lauderdale, Fla., identified a commonly occurring circumstance in which the Supreme Court's decision in *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308 (1999), does not apply.

In *Grupo Mexicano*, the Supreme Court barred *Mareva* injunctions in federal practice by holding "that a federal court may not freeze a defendant's assets when the plaintiff asserts what is only a legal claim against the defendant." *Id.* at 333.

Grupo Mexicano was a departure from practice in the U.K. where English courts since 1975 have issued *Mareva* injunctions prohibiting defendants from transferring assets before judgment. *See Mareva Compania Naviera S. A. v. International Bulkcarriers S. A.*, 2 Lloyd's Rep. 509.

Less than two months ago, we reported on a decision where the Second Circuit found no loophole in *Grupo Mexicano* and held that a plaintiff cannot freeze the assets of a guarantor when the plaintiff only had a claim for money damages against the guarantor. *Advantage Capital Holdings LLC v. Leadenhall Capital Partners LLP*, 171 F.4th 155 (2d Cir. March 23, 2026). To read ABI's report, click here.

In his May 5 opinion, Judge Russin could be understood as having held in substance that a plaintiff may obtain a preliminary injunction in a fraudulent transfer suit to recover specific property, but not when the objective is to obtain a money judgment in lieu of specific property.

The Alleged Fraudulent Transfers

The facts in the case before Judge Russin were distinguishable from both *Grupo Mexicano* and *Advantage Capital*.

An individual was the owner of a corporate debtor in chapter 11. After the owner was removed from management, the debtor confirmed a liquidating chapter 11 plan that created a liquidating trust for making distributions to creditors and recovering assets, including claims against the owner.

The trust sued the owner for receipt of fraudulent transfers under Section 548 and Florida law. The complaint alleged that the owner caused the debtor to transfer about $10 million to purchase real property in Florida held in the name of a corporation that the owner controlled and owned. We shall refer to the real property as the "property."

After filing the adversary proceeding, the trust moved for and obtained a temporary restraining order preventing the owner from encumbering, transferring or disposing of the property. Judge Russin wrote his opinion to explain the reasons for entering a preliminary injunction following a hearing and expiration of the TRO.

Most of Judge Russin's 45-page opinion is devoted to laying out the facts necessary for showing the trust's entitlement to a preliminary injunction. We shall focus on the portions of his opinion explaining why a preliminary injunction was available after *Grupo Mexicano* and similar authorities like *Advantage Capital*.

Grupo Mexicano and Its Progeny

Judge Russin described *Grupo Mexicano* as holding "that a federal court has no authority to issue a preliminary injunction preventing a defendant from disposing of its assets pending adjudication of a contract claim for money damages where the plaintiff claims no lien or equitable interest in the defendant's property." He explained that the "Court's reasoning was grounded in the historical limitations on equity jurisdiction" as they existed at the adoption of the Judiciary Act in 1789.

In *Grupo Mexicano*, the Court distinguished *Deckert v. Independence Shares Corp.*, 311 U.S. 282 (1940), where the Court, decades earlier, had "upheld a preliminary injunction to preserve assets pending an action for rescission and restitution," Judge Rusin said. "[W]hen a plaintiff's underlying claims are equitable in nature," he went on explain how *Deckert* means that "a preliminary injunction to preserve a specific *res* pending final adjudication remains within the court's equitable authority."

The claims in the case before him, Judge Russin held, "fall within the *Deckert* exception."

Next, Judge Russin cited *Pettigrew v. Graham (In re Graham)*, 747 F.2d 1383 (11th Cir. 1984), where, he said, the "Eleventh Circuit addressed the legal or equitable character of fraudulent conveyance actions." In *Graham*, he said that the Eleventh Circuit "court drew a clear line: '. . . an action by a creditor or trustee-in-bankruptcy to set aside a fraudulent conveyance is an equitable action, while an action by a creditor or trustee-in-bankruptcy seeking money damages is an action at law.'" *Id*. at 1387-88.

Judge Russin then said that *Graham* was "consistent" with *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989), where he described the Supreme Court as holding "that a Section 548 action seeking to recover 'a determinate sum of money' is a legal claim." However, "the Court endorsed the principle that the legal or equitable determination turns on the nature of the property transferred."

In the case before him, the trust was aiming to recover "a specific parcel of real property," Judge Russin said. Under the framework "endorsed by *Granfinanciera*, when the subject matter of the fraudulent transfer is land, the trustee may invoke the equitable process," he said.

Given that the trust's claims were equitable in nature, Judge Russin held that "the *Deckert* exception applies, and *Grupo Mexicano* does not bar the relief" in the form of a preliminary injunction.

Judge Russin devoted the remainder of his opinion to findings of fact showing the trust's entitlement to a preliminary injunction. Granting the injunction, he found that the trustee had demonstrated "(1) a substantial likelihood of success on the merits; (2) that irreparable injury will be suffered unless the injunction issues; (3) that the threatened injury to the movant outweighs whatever damage the proposed injunction may cause the opposing party; and (4) that the injunction would not be adverse to the public interest."

Observations

What if the defendant had fraudulently transferred money? Because money is fungible, is a preliminary injunction unavailable? What if tracing could identify the cash that was originally transferred?

The opinion is *VPX Liquidating Trust v. Owoc (In re Vital Pharmaceuticals Inc.)*, 22-17842 (Bankr. S.D. Fla. May 5, 2026).

Second Circuit pointed out that Wagoner was a case where the trustee was not bringing suit under Section 544.

Narrowing *Wagoner*, Second Circuit Says Trustees Have Standing for Alter Ego Claims

The Second Circuit held that a trustee has standing to bring a veil piercing claim alongside standing to assert claims that could be brought by any creditor.

Of perhaps greatest significance, the April 6 opinion by Circuit Judge Richard J. Sullivan cabined the Second Circuit's *Wagoner* decision, which sometimes has been read to mean that a trustee cannot sue on behalf of a company when the company was a participant in fraud. *Shearson Lehman Hutton, Inc. v. Wagoner*, 944 F.2d 114 (2d Cir. 1991).

Judge Sullivan pointed out that *Wagoner* was not based on Section 544, the provision on which the trustee in the case on appeal was asserting an alter ego claim.

The Yacht and Alter Ego Claims

An individual who claimed to be a multi-billionaire contended that he did not own a yacht worth tens of millions of dollars. Rather, he took the position that his daughter owned the corporation that owned the yacht.

Years ago, a creditor won a $116 million judgment against the individual, whom we shall refer to as the debtor. The creditor obtained an attachment of the yacht and a restraining order supposedly barring the yacht from leaving the jurisdiction. Nonetheless, the yacht sailed away, prompting the creditor to bring contempt proceedings. The court held the debtor in contempt, finding that he had stashed his assets in corporations to avoid and deceive creditors.

Soon after the contempt order, the debtor filed a chapter 11 petition. In due course, the bankruptcy court called for a chapter 11 trustee.

In the chapter 11 case, the daughter and her corporation filed an adversary proceeding claiming that her corporation owned the yacht. The trustee filed a counterclaim, asserting that the debtor was the owner and that the daughter's corporation was the debtor's alter ego.

The bankruptcy court granted the trustee's motion for summary judgment, finding for the trustee on the alter ego claim. After the district court affirmed, the daughter and her corporation appealed to the circuit.

Creditors Have Veil Piercing Claims

In the circuit, the daughter and her corporation contended that the trustee lacked standing to assert what amounted to reverse veil piercing.

Quoting Second Circuit authority, Judge Sullivan said that a "'bankruptcy trustee may bring claims founded [both] on the rights of the debtor and on certain rights of the debtor's creditors.'" To assert claims belonging to the debtor, the trustee relies on Section 541, but to assert claims of creditors, the trustee uses the so-called strong-arm clause in Section 544(a) giving the trustee the rights of a hypothetical judicial lien creditor.

"In other words," Judge Sullivan said, "section 544(a) permits the trustee to assert any generalized claims that would belong to a hypothetical high-priority lien creditor." In turn, state law determines whether a lien creditor could bring the claim.

Delaware law governed because the corporate owner of the yacht was a Delaware corporation. Judge Sullivan said that "Delaware law recognizes outsider reverse veil-piercing claims." In other words, he said, the trustee was "invok[ing] those creditors' rights to make [the corporation] pay for [the debtor's] debts."

Wagoner Pigeonholed

Judge Sullivan recounted how the daughter argued that *Wagoner* required the court to read Section 544 more narrowly.

Indeed, Judge Sullivan quoted *Wagoner* as saying that "'a bankruptcy trustee has no standing generally to sue third parties on behalf of the estate's creditors, but may only assert claims held by the bankrupt corporation itself.'" *Wagoner*, *supra*, 944 F.2d at 118. Still, he said,

> [S]ection 544 can coexist with *Wagoner* because that statute does not allow trustees to assert just any creditor claim. Instead, courts must distinguish between "general" and "personal" claims.

In a footnote, Judge Sullivan noted that *Wagoner* "did not involve or attempt to interpret section 544." He recounted how the trustee in *Wagoner* was not asserting claims of creditors. Again quoting *Wagoner*, the appeals court said it was "'unnecessary for us to delve deeply into when, if ever, a trustee may sue a third party on behalf of the bankrupt's creditors.'" *Id*. at 118.

Drilling down to the question of when a trustee may assert a claim belonging to creditors, Judge Sullivan quoted *Paul Fire & Marine Ins. Co. v. PepsiCo, Inc.*, 884 F.2d 688, 701 (2d Cir. 1989):

> "If a claim is a general one, with no particularized injury arising from it, and if that claim could be brought by any creditor of the debtor, the trustee is the proper person to assert the claim."

Synthesizing *Wagoner*, *St. Paul* and Section 544, Judge Sullivan said, "[T]he *Wagoner* rule bars trustees from asserting personal-creditor claims, while section 544 allows them to pursue general causes of action that would benefit any hypothetical creditor."

Even more on point, Judge Sullivan quoted the Seventh Circuit for holding "that the trustee 'has creditor status under section 544 to bring suits for the benefit of the estate and ultimately of the creditors,' and that '[alter ego] allegations that could be asserted by any creditor could be brought by the trustee as a representative of all creditors.'"

Alter Ego Claims Are General, Not Personal

Judge Sullivan found himself left "with one final task: to determine whether the claims at issue here are general or personal." For him, the answer was "clear." Quoting *In re Nordlicht*, 115 F.4th 90, 108-09 (2d Cir. 2024), he said, "'reverse veil-piercing claim[s] [are] . . . general'" because "a hypothetical creditor could bring these generalized claims against [the corporation]."

Having found that the trustee had standing to assert reverse veil piercing, Judge Sullivan ended his opinion by examining whether the bankruptcy court properly invoked summary judgment. Suffice it to say, he found that "the Trustee presented a mountain of evidence suggesting that [the corporation] was [the debtor's] alter ego." He affirmed summary judgment granted in favor of the trustee.

Observations

Arguably, there is a split of circuits on *Wagoner*.

In 2016, the Sixth Circuit held that the *Wagoner* rule does not apply in federal litigation. The Cincinnati-based appeals court cited the Eighth, Eleventh and Third Circuits as also having disagreed with *Wagoner*. *Bash v. Textron Financial Corp. (In re Fair Finance Co.)*, 834 F.3d 651 (6th Cir. Aug. 23, 2016). To read ABI's report, click here.

Wagoner was not jurisdictional. It espoused a rule of prudential standing not embraced by all circuits. Following the decision by Judge Sullivan, *Wagoner* may have no relevance when a trustee invokes Section 544 as grounds for filing suit based on a claim that could be asserted by creditors.

The opinion is *Guo v. Despins (In re Kwok)*, 24-2504 (2d Cir. April 6, 2026).

Fifth Circuit says that agreement on material terms in mediation made the settlement enforceable without a written agreement.

Agreement on Material Terms Makes a Mediated Settlement Enforceable

Mediation plays a major role in bankruptcy. A decision from the Fifth Circuit tells us there can be an enforceable settlement, even if a principal on one side believes there was no agreement at the conclusion of mediation.

The June 15 opinion by Circuit Judge Stephen A. Higginson could be understood to mean there's an enforceable settlement if there was agreement on the material terms and no one walked out of mediation saying there was no settlement.

Mediated Agreement on Material Terms

The defendants, as we shall call them, were a corporate medical practice and a doctor who was its principal. The U.S. government sued the defendants in federal district court under the False Claims Act for the submission of inflated bills. Including civil penalties and treble damages, the government was after more than $20 million.

The parties mediated under the district's local rules. The mediator was a former state court judge.

There was no dispute that mediation resulted in a settlement where the defendants would pay $2.3 million over 42 months, with an initial payment of $100,000. The government's lawyer said he would include the terms in a written agreement along with other "standard terms."

At the conclusion of the mediation, neither the defendants nor their counsel disagreed or said there was no deal without agreement on written terms. The parties shook hands, and the mediator filed a form with the district court saying there was a settlement.

The government later submitted the written agreement, which the defendants never signed. Two months later, the government moved in district court to enforce the written agreement. Based on a concession by the government, the district court decided after an evidentiary hearing that there was an enforceable settlement based on the material terms of payment.

The defendants appealed, contending there was no settlement because there was no signed agreement.

Agreement on Material Terms Is Enough

Because the parties' claims were based on federal law, Judge Higginson said that "federal contract law governs the validity and enforceability of a purported settlement agreement." On appeal, the question was "whether the district court abused its discretion in concluding that the parties reached a binding, final agreement as to all material terms at mediation."

In the Fifth Circuit, Judge Higginson said there is no agreement "when an agreement leaves material matters open for future adjustment and agreement that never occur." The circuit has said that material terms "may be quite sparse." Therefore, the first issue was whether there had been agreement on material terms.

Judge Higginson said that "the district court concluded that the terms addressed at mediation encompassed all the material terms," *i.e.*, $2.3 million paid over 42 months with an initial payment of $100,000. He held that "it was not an abuse of discretion for the district court to conclude that these provided the essential parameters to create a deal."

Next, Judge Higginson examined whether terms in the written agreement were material. Citing the Fifth Circuit, he said that "federal contract law requires no written agreements or signatures to form a valid agreement."

On appeal, the defendants took the position that five terms in the written agreement were material and that the lack of agreement meant there was no settlement.

"Especially where, as here, the defendants' counsel understood that a subsequent written agreement would include additional, standard terms," Judge Higginson held, the "district court did not abuse its discretion in finding the written agreement's provisions immaterial."

Of perhaps greatest significance, Judge Higginson held that "the district court did not abuse its discretion in finding that the parties' oral agreement at mediation was final and binding." Quoting Fifth Circuit precedent, he said that an agreement will be enforceable "unless the parties explicitly provide that a valid contract will not be formed until the parties execute a formal, finalized agreement."

Judge Higginson affirmed the district court's enforcement of the settlement agreement.

The opinion is *U.S. v. Ma*, 25-50067 (5th Cir. June 15, 2026).

Third Circuit Judge Bibas sat by designation in district court to rule on a Delaware bankruptcy appeal.

Even a Void 'Securities Contract' Qualifies for the 'Safe Harbor,' Third Circuit Judge Says

Sitting by designation as a district judge to hear a bankruptcy appeal in the District of Delaware, Third Circuit Judge Stephanos Bibas had harsh words for chapter 11 debtor Mallinckrodt. He called Mallinckrodt the "dominant opioid manufacturer" that "prop[ped] up the company's share price" by "artificially inflat[ing] its value by buying back its stock," in the process making "its shareholders billions before it sought refuge in Chapter 11 bankruptcy."

Although saying that "[c]itizens and communities harmed by opioids deserve payment," Judge Bibas affirmed the bankruptcy court by holding that the safe harbor in Section 546(e) protects shareholders who sold their Mallinckrodt stock, even if the stock repurchase agreements were void *ab initio* under Irish law.

In his November 24 opinion, Judge Bibas declined to follow *Enron Corp. v. Bear, Stearns Int'l Ltd. (In re Enron Corp.)*, 323 B.R. 857 (Bankr. S.D.N.Y. 2005), where a bankruptcy court in New York read the safe harbor as inapplicable to void contracts.

The Stock Buyback

Judge Bibas said that being the largest opioid manufacturer was "lucrative" for Mallinckrodt but came at the "cost" of 600,000 deaths from opioids between 2000 and 2020.

When the "opioid market went bust," Judge Bibas said that Mallinckrodt propped up the value of its stock by spending $1.6 billion in stock buybacks between 2015 and 2018. The purchases, he said, "artificially inflated Mallinckrodt's share price even as its core business was in a death spiral." The buybacks "meant that there was less left over to pay the injured people, companies, and communities who were left holding the bag."

Judge Bibas described how Mallinckrodt's confirmed chapter 11 plan created a trust that sued "to recover money fraudulently transferred out of Mallinckrodt while it was insolvent — including claims that sought to claw back the money Mallinckrodt paid to buy back its shares." The fraudulent transfer claims were under state law and Section 544(b)(1) because the purchases were more than two years before bankruptcy.

The defendants asserted a defense under the safe harbor in Section 546(e), which provides that "the trustee may not avoid a transfer that is a . . . settlement payment . . . or that is a transfer made . . . in connection with a securities contract."

Bankruptcy Judge John T. Dorsey of Delaware granted summary judgment in favor of the defendants, holding that the defendants were banks, hedge funds and money managers that qualified as "financial institutions" and that the transfers were "qualifying transactions" because they were "settlement payments."

The trust appealed, contending that the safe harbor did not apply because the repurchase contracts were void and could not qualify as securities contracts.

Contracts Void Under Irish Law

The debtor was an Irish company. The trust contended that the safe harbor did not apply because Irish law controlled the buybacks and that Irish law considers unlawful buybacks by an undercapitalized company to be void.

"Whether void payments are protected by § 546(e)'s safe harbor," Judge Bibas said, "has come before a court only one other time," citing *Enron*. The bankruptcy court in *Enron*, he said, "held that void payments are not 'settlement payments,' so financial institutions cannot take refuge in the safe harbor."

Judge Bibas did not leave the reader in suspense. Immediately, he said, "that single decision neither binds nor persuades me, so I affirm the bankruptcy court."

The outcome turned on the meaning of "settlement payment" and whether a void transaction gives rise to a settlement payment. The term is defined in Section 741(8) to mean "a preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade."

Citing *Bevill, Bresler & Schulman Asset Mgmt. Corp. v. Spencer Sav. & Loan Ass'n*, 878 F.2d 742, 749 (3d Cir. 1989), Judge Bibas said that the term "settlement payment" has been given an "extremely broad definition," so broad that a "payment alone is enough, even if the transaction does not ultimately settle."

Similar to the meaning ascribed to settlement payment in the Third Circuit, Judge Bibas cited *Picard v. Ida Fishman Revocable Trust (In re Bernard L. Madoff Inv. Sec. LLC)*, 773 F.3d 411, 422–23 (2d Cir. 2014). There, the Second Circuit held that payments by the fraudster were settlement payments even though no stock was ever bought or sold by the Ponzi-schemer.

"*Madoff* looks like this case," Judge Bibas said. He explained:

> The underlying transactions appear to have been void *ab initio* under Irish law. But the payments are very real, and they were made to complete a securities transaction. That satisfies § 546(e) here as it did in *Madoff*.

Enron on 'Shaky Ground'

Judge Bibas said that *Enron* "stands alone and stands on shaky ground." Among other things, he said it "relies on a simplistic distinction between void and voidable transactions," although fraudulent transfers "are typically voidable contracts."

Although it was "true" that Mallinckrodt had no legal obligation to pay under contracts that were void *ab initio*, Judge Bibas said that the debtor "still made payments to fulfill a purported obligation. That is all that the safe harbor requires." In short, "payments made to settle securities transactions of all stripes count as settlement payments."

Judge Bibas took the voidness idea a step further. "If the Trust were right that voidness under Irish law stops the operation of the Bankruptcy Code, it would defeat the Trust's whole claim," he said, because only contracts may be avoided.

"So if the transactions at issue in this case were truly void as the Trust claims, § 544(b)'s avoidance power would be unavailable," Judge Bibas said. He affirmed the judgment of the bankruptcy court.

The opinion is *Opioid Master Disbursement Trust II v. Citadel Securities LLC (In re Mallinckrodt PLC)*, 25-00114 (D. Del. Nov. 24, 2025).

On direct appeal, the Third Circuit said that the PBGC's new rules dealing with the American Rescue Plan Act of 2021 did not violate the major questions doctrine.

Third Circuit Upholds PBGC's Rulemaking Authority in Calculating Withdrawal Claims

Affirming Bankruptcy Judge Craig T. Goldblatt on direct appeal, the Third Circuit decided that bankrupt trucker Yellow Corp. could not reduce its liability for withdrawing from multiemployer pension plans by drawing on some of the billions of dollars that Congress appropriated during the pandemic to save pension funds.

In his September 16 opinion, Circuit Judge Thomas L. Ambro decided that two regulations promulgated by the Pension Benefit Guaranty Corp. were "reasonable conditions" and were neither arbitrary nor capricious.

Of perhaps greater significance in terms of a possible petition for *certiorari*, Judge Ambro held that the PBGC's rulemaking did not violate the major questions doctrine.

The American Rescue Plan Act of 2021

Judge Ambro began his opinion by tracing the history of the Employee Retirement Income Security Act of 1974 and the Multiemployer Pension Plan Amendments Act of 1980. Created under ERISA, the PBGC collects insurance premiums to provide benefits when underfunded pension plans terminate.

Judge Ambro explained that ERISA gave the PBGC "wide regulatory authority" to issue regulations. The appeal dealt with two regulations adopted by the PBGC after Congress passed the American Rescue Plan Act of 2021 during the pandemic "to shore up the nation's struggling pension system" with billions of dollars.

One regulation required pension plans to phase in financial assistance from the ARPA over several years rather than add the funds to plan assets all at once. Judge Ambro said that the regulation would "affect[] withdrawal liability, as an employer that withdrew later would calculate its liability against a bigger base of plan assets, offsetting the amount owed."

The second regulation prohibited pension plans from recognizing funds received from the ARPA before the funds were paid into the plan. Judge Ambro explained how the rule meant that a pension plan's withdrawal liability would not be reduced by funds that were awarded but not received before withdrawal.

Yellow's Withdrawal Date

Yellow filed a chapter 11 petition in August 2023 and liquidated, terminating pension plans in the process. Pension plans filed $6.5 billion in claims for withdrawal liability, which was calculated as of December 31, 2022, but the pension plans did not receive funds from the ARPA until January 2023. For Yellow, its pension plans had smaller assets in view of the date of withdrawal, giving the debtor larger withdrawal liability. For other pension plans, debtors had larger withdrawal liability as a result of the phase-in regulation limiting the size of the plans' assets.

After the debtor lodged objections to the plans' claims, both sides filed motions for summary judgment, with the debtor challenging the validity of the two regulations. Bankruptcy Judge Goldblatt upheld the regulations and certified a direct appeal, which the Third Circuit accepted.

PBGC Had 'Gap-Filling' Regulatory Authority

On the merits, Judge Ambro began by saying that the debtor "lob[bed] a slew of challenges at the regulations" by arguing "that the regulations violate the PBGC's statutory authority and are arbitrary, capricious, or otherwise invalid." However, he said that the debtor's "strongest argument is that ARPA did not grant the PBGC the *regulatory* authority to change the *statutory* formula for withdrawal-liability calculation." [Emphasis in original.]

Judge Ambro was "not convinced" by the argument. He quoted Judge Goldblatt for correctly holding that "'Congress has expressly granted the PBGC the type of gap-filling authority that [*Loper Bright Enters. v. Raimondo*, 603 U.S. 369 (2024)] described, both in ERISA as originally enacted in 1974 and again in the provisions of [ARPA] that are directly at issue here.'" He held that "the more specific provisions of ARPA control over the general provisions of" earlier legislation.

Judge Ambro ruled that "the two regulations are 'reasonable conditions' on the grant of funds to the plans, promulgated according to Congress's grant of authority to the PBGC in ARPA."

Reasonable Regulations

Next, Judge Ambro turned to the question of whether the two regulations were arbitrary or capricious. He did not review the regulations *de novo*. Rather, he asked whether the PBGC gave a "satisfactory explanation" for its actions.

"As [Bankruptcy Judge Goldblatt] aptly explained," Judge Ambro said, "the notice-and-comment process for the regulations was comprehensive.'[I]ndustry stakeholders, including employers, pension plans, actuarial firms, law firms, individuals, and members of Congress,' weighed in."

"We are convinced," he said, "that the administrative record reflects 'reasonable' rulemaking, 'reasonably explained,' given the "'appropriate deference' . . . owed to 'agency decisionmaking.''""

Major Questions Doctrine

The debtor contended that the regulations violated the major questions doctrine pronounced by the Supreme Court in *West Virginia v. EPA*, 597 U.S. 697, 716, 724 (2022). Judge Ambro said that the doctrine means that "[a]n agency cannot take action that results in a 'transformative expansion' of its authority — especially over issues of 'vast economic and political significance' — without express permission from Congress."

It was "not an extraordinary case," Judge Ambro said. "Far from a 'transformative expansion,'" he said, it was "PBGC business as usual, transacted per 'clear congressional authorization.'"

Affirming the bankruptcy court, Judge Ambro held that the two regulations "were valid exercises of its delegated authority under ARPA, and [that the debtor] must pay the higher withdrawal liability contracted for with the" pension plans.

The opinion is *In re Yellow Corp*., 25-1421 (3d Cir. Sept. 16, 2025).

Delaware bankruptcy judge sides with courts allowing suits against subsequent transferees without having sued the initial transferee to avoid the fraudulent transfer.

Courts Split on Suing an Initial Transferee Before Suing a Subsequent Transferee

Bankruptcy Judge Craig T. Goldblatt of Delaware stepped into the middle of a circuit split by holding that a trustee may sue a subsequent transferee of a fraudulent transfer without previously or simultaneously suing the initial recipient of the transfer.

Judge Goldblatt's February 4 opinion is written like a bench memorandum for circuit judges should the issue eventually find its way to the Third Circuit. But don't hold your breath: The case only involves $250,000, so the parties may decide to settle now that Judge Goldblatt has laid down the law.

Suit Against the Subsequent Recipient

An individual formed a corporation that solicited investments from accredited investors who were told that their investment would be used exclusively to purchase real estate projects. Instead, Judge Goldblatt said that the individual "fraudulently diverted those funds into his own account to use for his own personal benefit."

Eventually, the individual pled guilty to wire fraud and admitted that he had misappropriated and converted the investments.

The corporation ended up in chapter 11 and confirmed a plan creating a trust that took over prosecution of claims belonging to the estate. Neither the trustee nor the debtor had sued the individual. Rather, the individual made a global settlement that was engrafted into the plan. Neither the settlement nor the plan avoided fraudulent transfers to the individual.

After confirmation, the trustee identified a transaction where the individual had transferred $250,000 from the debtor to his own account and then transferred the $250,000 to an entity we shall refer to as the defendant. There was no relationship between the debtor and the defendant, and the debtor received no value from the defendant.

The trustee sued the defendant as a subsequent recipient of a fraudulent transfer made with "actual intent" under Sections 548(a)(1)(A) and 550(a)(2). The defendant moved to dismiss for failure to state a claim.

The defendant argued that the trustee could not recover against a subsequent transferee without first avoiding the initial transfer to the individual. The defendant also took the position that the initial transferee must be a party to the lawsuit against the subsequent transferee.

Judge Goldblatt said that "the implication of [the defendant's] argument would be that all subsequent transferees have effectively won get-out-of-jail free cards."

The Governing Statutes

Addressing the merits, Judge Goldblatt said there is "a square circuit split" with no Third Circuit authority. He cited *Slack-Horner Foundries Co.*, 971 F.2d 577 (10th Cir. 1992), from the Tenth Circuit and lower court opinions siding with the defendant. He devoted his opinion to explaining why those decisions were "wrongly decided."

Under Section 548(a)(1)(A) a trustee may avoid a transfer "if the statutory elements are met," Judge Goldblatt said. Once avoided, "the trustee may recover, under § 550(a)(1), 'the property transferred' or 'the value of such property' from 'the initial transferee' or 'the entity for whose benefit such transfer was made.'"

"In addition," Judge Goldblatt said, "§ 550(a)(2) permits the trustee to recover the property transferred or its value from 'any immediate or mediate transferee of such initial transferee,' subject to the defenses set forth in § 550(b)."

Next, Judge Goldblatt said that the complaint sufficiently alleged that the initial transfer from the debtor to the individual's own account was a fraudulent transfer with "actual intent" and that the defendant had received funds that were fraudulently transferred to the individual. The question remained as to whether the trustee could recover from the defendant without having avoided the transfer in a suit against the individual.

Avoidance Is Just an Element of a Claim Against a Subsequent Transferee

Judge Goldblatt identified "confusion in some of the caselaw seem[ing] to stem from the belief that the initial transferee needs to be a party to a lawsuit seeking to avoid the initial transfer." He proceeded to explain why "there is no reason . . . that needs to be the case."

Citing the Ninth Circuit Bankruptcy Appellate Panel and several district courts, Judge Goldblatt said that most courts "have correctly held that a transfer can be avoided, and recovery had from a subsequent transferee, without suing the initial transferee." As the leading case among the authorities for his point of view, he cited *S.I.P.C. v. Bernard L. Madoff Inv. Sec. LLC*, 501 B.R. 26 (S.D.N.Y. 2013), by District Judge Jed S. Rakoff.

In *Madoff*, Judge Rakoff defined the issue as "whether the Trustee's recovery action against a subsequent transferee under 11 U.S.C. § 550(a) must be dismissed unless the Trustee has either obtained a judgment against the relevant subsequent transferee avoiding the initial transfer or the Trustee asserts a claim against the subsequent transferee to avoid the initial transfer within the period prescribed by 11 U.S.C. § 546(a)." *Id*. at 34.

Judge Rakoff saw "no basis in the language of either section 550(a) or the Bankruptcy Code's avoidance provisions to assume that avoidance actions must be brought — or fully adjudicated — against an initial transferee for recovery proceedings to go forward against a subsequent transferee." *Id*. at 31.

Judge Rakoff held "that section 550(a)'s limitation on the Trustee's recovery of transfers 'to the extent that a transfer is avoided' requires the Trustee to show that a given transfer is avoidable and does not require an actual judgment of avoidance." *Id*. at 37.

On his side of the fence, Judge Goldblatt cited the Eleventh Circuit for making the question "harder than it ought to be." The Eleventh Circuit, he said, "implicitly accept[ed] the notion that the initial transferee would need to be a defendant in order to avoid the initial transfer." However, he went on to say that the Atlanta-based appeals court "suggested that it is not necessary actually to 'avoid' the transfer [but] suggested that it would be sufficient to show that the initial transfer is 'avoidable.'"

The Flaw in the Contrary Decisions

In *Slack-Horner*, Judge Goldblatt identified the "central flaw" in the Tenth Circuit's logic as the court's failure "to recognize that the 'avoidance' of a transfer is simply an element of claim that needs to be proven against the defendant against whom recovery is sought . . . . There is no reason, however, why the initial transferee needs to be a party to the lawsuit in which that transfer is avoided." He elaborated:

> The central analytic flaw in these cases is that they do not treat the avoidance of the "transfer" like an element of a lawsuit that must be established for the trustee to establish the liability of a particular defendant. Rather, they treat the "transfer" almost as if it were a physical object existing somewhere in the universe, and a bright orange sticker with the word "avoided" either has or has not been affixed to it.

In other words, Judge Goldblatt said, "There is no reason . . . why the 'avoidance' of a transfer should be conceptually different than a finding" that a fraudulent transfer occurred. However, he agreed with the Tenth Circuit "that the transfer from the debtor to the initial transferee must be *actually avoided*, not merely shown to be 'avoidable,' before a subsequent transferee can be held liable." [Emphasis in original.]

Nonetheless, Judge Goldblatt saw "no reason that the initial transferee needs to be a party to the lawsuit in order to accomplish that." He explained:

> If the initial transferee is not a party to a suit against a subsequent transferee, and a trustee successfully makes out the elements of a fraudulent conveyance from the debtor to the initial transferee, then the transfer has been *actually avoided* as applied to the subsequent transferee. [Emphasis in original.]

Judge Goldblatt held that "the avoidance of a transfer from the debtor to the initial transferee is simply an element that the trustee must establish in order to recover a transfer or its value from a subsequent transferee" and rejected the contention "that the complaint fails to state a claim on account of [the individual's] absence as a defendant."

There was a flaw in the complaint that precluded Judge Goldblatt from simply denying the motion to dismiss. He directed the trustee to file an amended complaint within 30 days.

Observations

Once the trustee files an amended complaint, Judge Goldblatt presumably will deny the defendant's motion to dismiss. The denial of a motion to dismiss won't enable the defendant to appeal unless Judge Goldblatt grants leave to appeal an interlocutory order.

With only $250,000 at stake and a long road to the Third Circuit, the parties may decide to settle rather than incur the expense of appeals.

Note: The decision by District Judge Rakoff in *Madoff* was interlocutory and therefore invited no appeal. Although Bernard Madoff's Ponzi scheme has launched scores of lawsuits against initial and subsequent recipients of fraudulent transfers, the holding in Judge Rakoff's decision has not been challenged in the Second Circuit.

Indeed, it's possible to read the Second Circuit's seminal Madoff decisions — *In re Picard*, 917 F.3d 85 (2d Cir. 2019), and *Picard v. Citibank, N.A. (In re Bernard L. Madoff Investment Securities LLC)*, 12 F.4th 171 (2d Cir. 2021) — as following or comfortably consistent with Judge Rakoff's opinion. To read ABI's reports, click here and here.

The opinion is *Phillips v. SS Associates LLC (In re ONH AFC Investors LLC)*, 25-51090 (Bankr. D. Del. Feb. 4, 2026).

Except for partners, nondischargeability for 'actual fraud' requires fraudulent intent by the debtor, Bartenwerfer notwithstanding.

Bartenwerfer Interpreted Narrowly; Except for Partners, Fraudulent Intent Required

Bankruptcy Judge Mina Nami Khorrami of Columbus, Ohio, refused to expand *Bartenwerfer* when she held that net winners in a Ponzi scheme are not saddled with nondischargeable debts for "actual fraud" under Section 523(a)(2)(A).

Although Judge Nami Khorrami's May 14 opinion does not say so explicitly, the joint chapter 13 debtors evidently were so-called net winners in a Ponzi scheme. A net winner is someone who invested in a Ponzi scheme and took out more cash than it received. The difference between the cash in and cash out is typically viewed as a transfer that can be recovered under state or federal law as a transfer with "actual intent."

In the case before Judge Nami Khorrami, a receiver had been appointed in state court to clean up a Ponzi scheme. In state court before the transferees' bankruptcy, the receiver sued the debtors to recover more than $3 million. The receiver did not allege that the debtors had actual intent to defraud, nor did the receiver even allege that the debtors were aware of the Ponzi scheme.

Before judgment in state court, the debtors filed a chapter 13 petition. The receiver filed a claim and a complaint in bankruptcy court to declare the debt nondischargeable under Section 523(a)(2)(A) as a debt obtained by "actual fraud."

The debtors filed a motion to dismiss, taking the position that the nondischargeability complaint failed to state a claim because the receiver was not alleging that the debtors themselves had "actual intent" to defraud.

"Before *Bartenwerfer*," Judge Nami Khorrami said, "this would be an easy case," because "*Husky*, *Bullock*, *Neal*, and their progeny" would have required dismissal. She described the receiver as "assert[ing] that *Bartenwerfer* 'represents a sea change in how courts are required to interpret section 523(a)(2)(A).'"

Reading *Bartenwerfer* Narrowly

Aside from Supreme Court authority, the outcome turned on Section 523(a)(2), which makes a debt nondischargeable if "obtained by — (A) false pretenses, a false representation, or actual fraud . . . ."

Addressing the merits, Judge Nami Khorrami began with *Bartenwerfer v. Buckley*, 598 U.S. 69 (2023), where the husband-and-wife debtors had formed a partnership. The husband had committed fraud, but the wife had not. When the creditor sued the wife for nondischargeability, the wife contended that the debt should be discharged because she had not herself committed fraud. To read ABI's report on *Bartenwerfer*, click here.

Judge Nami Khorrami condensed *Bartenwerfer's* holding to mean that "the husband's fraud was sufficient to trigger § 523(a)(2)(A)" for the wife because "California's law of partnership and agency imputes the fraud of one partner to the other partners." She conceded that *Bartenwerfer* "used [a] certain broad statement," for example, when the Court "stated that '§ 523(a)(2)(A) turns on how the money was obtained, not [on] who committed fraud to obtain it.' 598 U.S. at 72."

Judge Nami Khorrami chose to read *Bartenwerfer* more narrowly given "the Supreme Court's 'usual practice of deciding no more than is necessary to dispose of the case before us.'" She proceeded to examine whether *Bartenwerfer* limited or overruled cases like *Husky*, *Neal v. Clark*, 95 U.S. 704 (1878), or *Strang v. Bradner*, 114 U.S. 555 (1885), when she said,

> The Supreme Court has held that "actual fraud" includes frauds that can be accomplished without a false representation that induced reliance by the creditor. *Husky Int'l Elecs., Inc. v. Ritz*, 578 U.S. 355, 360, (2016). "The word 'actual' has a simple meaning in the context of common-law fraud: It denotes any fraud 'that involves moral turpitude or intentional wrong.'" *Id*. (quoting *Neal v. Clark*, 95 U.S. 704, 709 (citation modified)). "Thus, anything that counts as 'fraud' and is done with wrongful intent is 'actual fraud.'" *Husky*, 578 U.S. at 360.

Judge Nami Khorrami concluded, "Nothing in *Bartenwerfer* suggests that the Supreme Court was considering anything other than the ongoing validity of *Strang's* imputation of fraud to an innocent partner under partnership and agency principles."

Courts Reading *Bartenwerfer* as Applying Only to Partnerships and Agency

Judge Nami Khorrami cited "other courts" for having "widely ruled that *Bartenwerfer* applies only where the law of partnership or agency would impute the fraud of one actor to the debtor." Moreover, she said, "interpreting *Bartenwerfer* to apply outside the partnership and agency context here would bring it into conflict with *Husky*."

Judge Nami Khorrami noted that "*Bartenwerfer* did not overrule, limit, modify, or even mention *Husky*." She held, "*Husky* is the case which directly controls here" and "requires that the Debtors here had fraudulent intent."

Judge Nami Khorrami elaborated on her holding, saying,

> [T]o assert a § 523(a)(2)(A) claim, the Receiver must plausibly allege either that the Debtors received the Transfers with the intent to defraud, or that they were in a partnership or agency relationship with [the Ponzi-schemer] such that his intent to defraud could be imputed to them.

Judge Nami Khorrami granted the debtors' motion to dismiss, while giving the receiver the option of filing an amended complaint showing why the Ponzi-schemer's fraudulent intent should be imputed to the debtors.

Observation

The holding by Judge Nami Khorrami is in keeping with the concurrence in *Bartenwerfer* by Justice Sotomayor, joined by Justice Ketanji Brown Jackson.

Justice Sotomayor joined the Court's opinion with the "understanding" that it concerns fraud only by "agents" and "partners within the scope of the partnership." *Bartenwerfer*, *supra*, 598 U.S. at 84.

The opinion is *Dottore v. Scheibal (In re Scheibal)*, 25-02012 (Bankr. S.D. Ohio May 14, 2026).

Delaware's Bankruptcy Judge Horan gives examples of preference complaints that adequately plead performance of due diligence.

No Pleading Around the 'Due Diligence' Requirement for a Preference Complaint

Effective in 2020, Congress amended Section 547(b) by requiring a debtor or trustee to perform "due diligence" before filing a preference complaint, covering the defendant's "known or reasonably knowable affirmative defenses."

Delaware's Bankruptcy Judge Thomas M. Horan wrote an opinion effectively barring plaintiffs from "pleading around" the due diligence requirement. In an opinion on December 5, he gave examples of due diligence pleadings that will survive a motion to dismiss.

The chapter 7 trustee filed a complaint under Section 547 alleging a preference of almost $740,000. Although "it is possible that some Transfers might be subject in whole or in part to defenses under 11 U.S.C. § 547(c)," the complaint went on to say that the "Defendant bears the burden of proof pursuant to 11 U.S.C. § 547(g) to establish any defense(s) under 11 U.S.C. § 547(c)."

The defendant filed a motion to dismiss under Rule 12(b)(6), contending that the complaint failed to state a claim.

Deciding that the dismissal motion was well founded, Judge Horan quoted Section 547(b), which allows the filing of a preference complaint "based on reasonable due diligence in the circumstances of the case and taking into account a party's known or reasonably knowable affirmative defenses under subsection (c) . . . ."

Naturally, Judge Horan said that "a complaint must present well-pleaded facts, not mere conclusory statements, that establish the *prima facie* elements of the claim," although detailed facts "are not necessary." Furthermore, the court must accept all factual allegations as true, in the light most favorable to the plaintiff.

Previously, Judge Horan had decided that the due diligence requirement amounts to a condition precedent evaluated under Rule 9(c). The rule says that a complaint "suffices" if it "allege[s] generally that all conditions precedent have occurred or been performed." He quoted a Delaware bankruptcy judge who said, "'To satisfy § 547(b), the plaintiff only needs to allege that it conducted reasonable due diligence into the defendant's known or reasonably knowable affirmative defenses.'"

Regarding the words in the complaint before him, Judge Horan said that "the trustee . . . merely states the obvious — the defendant may have defenses and if it does, it is the defendant's burden to prove them." An allegation like that, he said, "would be true in virtually every instance."

To the contrary, Judge Horan said that the "trustee is required to plead that he performed due diligence and has taken into account known or reasonably knowable affirmative defenses. He has done neither."

Judge Horan gave examples of two complaints that properly alleged performance of due diligence. In one, the plaintiff said it had performed its own due diligence evaluation of the reasonably knowable defenses, had reviewed books and records, and had identified no invoices qualifying for the new value defense. The complaint went on to say that new value is an affirmative defense with the burden on the defendant.

In another case of adequate pleading, the complaint said that the plaintiff had performed its own due diligence of reasonably knowable affirmative defenses and had determined that it may avoid transfers even after taking affirmative defenses into consideration.

"The trustee here has made no such allegations in the complaint," Judge Horan said. "The complaint does not use the term 'due diligence' or any other language with similar meaning. It contains no language that plausibly could be understood as alleging that the trustee made any inquiry at all into whether there were 'known or reasonably knowable affirmative defenses.'"

The trustee had asked for dismissal of the complaint with leave to amend. In the Third Circuit, Judge Horan said that "a plaintiff seeking leave to amend a complaint must submit a draft amended complaint so that the court may determine if amendment would be futile."

In the case at hand, the trustee had not submitted a proposed amended complaint, so Judge Horan dismissed the complaint without prejudice, while giving the trustee 14 days to "file a motion to amend the complaint, along with a draft amended complaint and redline."

The opinion is *Miller v. Prestige Patio Co. Ltd. (In re Christmas Tree Shops LLC)*, 25-50876 (Bankr. D. Del. Dec. 5, 2025).

New York's Judge Philip Bentley split with the Fifth and Eleventh Circuits by holding that 'reasonableness' doesn't apply to a fully secured lender's prepetition fees, costs and charges.

Fully Secured Creditor's Prepetition Fees Aren't Subject to 'Reasonableness' Test

The Fifth and Eleventh Circuits, according to Bankruptcy Judge Philip Bentley of New York, hold that the "reasonableness" standard in Section 506(b) applies not only to postpetition claims but also to the allowance of prepetition claims of fully secured creditors for "fees, costs or charges."

In his July 20 opinion, Judge Bentley reports that "a number of lower courts have disagreed with those two courts of appeal" and hold that state law alone governs the allowance of prepetition fees, costs or charges for oversecured creditors.

Although he said that the "text of section 506(b) does not provide a clear answer to this issue," Judge Bentley devoted part of his July 20 opinion to explaining why he split with the circuits by holding that "reasonableness" in Section 506(b) does not apply to *pre*petition claims of oversecured creditors for fees, costs or charges.

Sections 502(b) and 506(b)

Judge Bentley had confirmed a liquidating chapter 11 plan for the single asset real estate debtor. For his opinion, Judge Bentley assumed that the mortgage lender was fully secured for its claim of around $25 million. Other claims were miniscule, meaning that the disallowance of parts of the mortgage claim would mean a larger recovery by the debtor.

The debtor therefore objected to the lender's prepetition and postpetition claims for late fees, forbearance fees and default interest.

Judge Bentley was confronted with the task of interpreting the interplay between Sections 502(b) and 506(b). Regarding the question at hand, he said that Section 506(b) is "ambiguous."

In pertinent part, Section 502(b) directs the court to "determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition . . . ."

For an oversecured creditor, Section 506(b) provides that the lender "shall be allowed . . . interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State statute under which such claim arose." The subsection does not say whether it applies to prepetition claims or postpetition claims or both.

Section 506(b) Invokes State Law

Citing the Second Circuit, Judge Bentley said that Section 502(b) means that "postpetition interest and other postpetition charges are generally excluded from the claim and not allowed." For an oversecured creditor, though, Section 506(b) kicks in and "allows an oversecured creditor to recover postpetition interest, plus any reasonable postpetition fees or other charges, to the extent the value of the creditor's collateral covers those amounts."

Judge Bentley said that Section 506(b) is "ambiguous" in terms of prescribing whether "reasonableness" applies to prepetition fees and charges, because "section 506(b)'s reasonableness requirement on its face applies to all fees, costs and charges provided for by agreement or statute, without any temporal limitation."

"On the other hand," Judge Bentley said, "a broad reading of this provision, so as to impose a reasonableness limitation on prepetition as well as postpetition charges, conflicts with section 502(b)'s allowance of prepetition charges to the full extent provided by nonbankruptcy law."

For two reasons, Judge Bentley adopted the narrow reading of Section 506(b) to mean that "reasonableness" only applies to postpetition fees and charges. The narrow reading "harmonizes that section [506(b)] with section 502(b) in a manner consistent with the text of both sections."

Judge Bentley went on to say that the broad reading "produces an absurd result." As an example, he said that oversecured creditors would be treated "less favorably than undersecured creditors with respect to their prepetition claims."

Judge Bentley recognized a "legitimate" policy concern that "disfavors the payment of unreasonably large fees to oversecured creditors, particularly when unsecured creditors are being paid only pennies on the dollar." Nonetheless, he said that imposing reasonableness on prepetition fees "on the prepetition fees of oversecured, but not undersecured, creditors is not a coherent or a textually supported solution to this issue."

For Judge Bentley, the "only conclusion that makes sense . . . is that Congress chose not to impose a reasonableness requirement on the prepetition claims of any secured creditors, whether oversecured or undersecured." He held,

> [S]ection 506(b)'s reasonableness requirement applies only to postpetition fees and other charges. Charges that accrue prepetition in favor of an oversecured creditor are allowed to the full extent provided by nonbankruptcy law.

State Law Issues

The remainder of Judge Bentley's opinion was devoted to questions of New York contract law governing late fees, forbearance fees, default interest and compound interest.

For our readers confronting questions of the type involving New York law, we recommend reading Judge Bentley's opinion in full text.

The opinion is *In re 1300 Desert Willow Road LLC*, 25-11375 (Bankr. S.D.N.Y. July 20, 2026).

The allowance of contractual default interest has a rebuttable presumption.

Judge Bentley Synthesizes Law on the Allowance of Contractual Default Rates of Interest

Bankruptcy Judge Philip Bentley of New York wrote an opinion synthesizing the case law on the allowance or disallowance of contractual default rates of interest.

Because unsecured creditors other than insiders wouldn't have a smaller recovery, Judge Bentley allowed a 16% default rate in his April 4 opinion, even though the debtor was *in*solvent.

The single asset real estate debtor owned an unoccupied luxury residence in an area on Long Island, N.Y., known as "the Hamptons." The debtor had confirmed a liquidating chapter 11 plan based on a sale of the property for about $4.3 million.

With a claim of $3.3 million including contractual default interest totaling $516,000, the mortgage lender was oversecured. The loan had a nondefault rate of 6.99% that rose on default by 9.01%, for a total contractual default rate of 16%.

The plan paid administrative and priority creditors in full, as well as noninsider general unsecured creditors, whose claims totaled only $7,000.

Unsecured insider creditors were owed $2.3 million. Their distribution under the plan would be made only after all other creditors were paid in full. If the lender's default rate were allowed, the insider creditors would recover only $600,000, Judge Bentley said.

Including the insider claims, the debtor was insolvent.

Aiming to enhance the recovery by insiders, the debtor objected to the allowance of the lender's default rate and to the allowance of a $29,000 late charge.

Rules on Allowance of the Default Rate

The allowance of the default rate for a secured creditor is governed by Section 506(b). Judge Bentley described the subsection as providing that an oversecured creditor "is entitled to interest on its secured claim, plus 'any reasonable fees, costs, or charges provided under the agreement.'" However, he said that "section 506(b) does not address the rate of interest at which such postpetition interest should be paid."

To fill in the blank, Judge Bentley said "that courts construing section 506(b) have generally applied a rebuttable presumption that an oversecured creditor is entitled to postpetition interest at the contractual default rate." He quoted retired Bankruptcy Judge Robert Drain as having said that "'most cases describe it as a strong presumption," although "'subject to limited equitable considerations.'"

In the Second Circuit, Judge Bentley said that courts "generally" apply a five-factor test to decide whether the debtor has rebutted the presumption of allowance. They are whether: (1) the debtor is solvent; (2) the default rate is a penalty; (3) there was misconduct by the creditor; (4) allowance of the fault rate would harm other creditors, and (5) allowance would adversely affect the debtor's fresh start.

Again citing Judge Drain, Judge Bentley said that none of the factors is dispositive and that they should be applied "sparingly."

When the debtor is solvent, Judge Bentley said that courts treat the first factor as a "very strong, perhaps unrebuttable or close to [an] unrebuttable" presumption. When a debtor is solvent, disallowing the default rate would benefit the debtor alone, Judge Bentley said.

Even when the debtor is insolvent, he said that courts "still have applied a presumption in favor of allowing default rate interest," but they "have done so with a lighter thumb on the scales, disallowing default interest if the debtor can show that at least one of the four equitable considerations — factors 2 through 5 in the five-part test — warrants that result."

In the case before him, the debtor was insolvent, meaning that Judge Bentley would allow the default rate "only if [the debtor] can show that one or more of the four relevant factors warrants disallowance."

No Penalty

First, Judge Bentley asked whether the default rate was a penalty. He noted that the mortgage had been negotiated between "commercially sophisticated parties" represented by counsel.

The default rate did not violate state usury laws, and there was no evidence that the rate was designed as a penalty, Judge Bentley said. Furthermore, the additional 9% on default was "well within the range of rates that courts in this Circuit have allowed under section 506(b)."

Judge Bentley held that the default rate was not a penalty.

Other Factors

Noting there was no allegation that the lender had been guilty of misconduct, Judge Bentley turned to the question of whether the default rate "would materially harm other creditors."

Judge Bentley didn't adopt the idea that creditors are harmed whenever their distributions would decline. Instead, he said that "a better formulation of this factor is that it requires harm to creditors other than the dollar-for-dollar reduction in their distributions caused by the increased payment to the secured creditor on account of default rate interest." In the case before him, allowance of the default rate would not put the reorganization at risk of failure because there was a confirmed liquidating plan.

There being no harm to creditors other than insiders, Judge Bentley found that the fourth factor did not favor disallowance. Because the liquidating plan already had been confirmed, he likewise decided that allowance of the default rate would not impair the debtor's fresh start. He therefore overruled the debtor's objection to the allowance of the default rate.

The Late Charge

The debtor also objected to the allowance of a $29,000 late charge.

Judge Bentley quoted retired Bankruptcy Judge Stuart M. Bernstein of New York, who said, "'The decisional law is uniform that oversecured creditors may receive payment of either default interest or late charges, but not both.'"

Having allowed the default rate, Judge Bentley disallowed the late charge.

The opinion is *In re 33 Mako LLC*, 25-11256 (Bankr. S.D.N.Y. March 4, 2026).

Due diligence required under Section 547(b) before filing a preference suit is a condition precedent that may be alleged generally.

A Preference Complaint Needn't Negate Defenses to Show Required 'Due Diligence'

Before filing a complaint to recover a preference, Section 547(b) now requires a debtor or a trustee to perform "reasonable due diligence."

For a preference complaint to survive a motion to dismiss, may the trustee or debtor generally allege the performance of due diligence, or must the complaint specifically describe the actions taken to investigate defenses?

In his October 22 opinion, Chief Bankruptcy Judge Dale L. Somers of Topeka, Kan., tells us that a complaint is "sufficient" if the trustee alleges that "he did not find any viable defenses."

The Demand Letter and the Complaint

A pig farm was the corporate chapter 7 debtor. For several years, a supplier provided feed for the animals. Within the 90-day preference period, the debtor had paid the supplier about $3.4 million.

The trustee sent the supplier a demand letter for $3.4 million and asked the supplier to explain any defenses it had to a preference. After retaining counsel, the supplier stated that it had a lien under Kansas agricultural law and that the payments were made on account of a valid secured debt and therefore were not preferential.

The trustee subsequently filed a $3.4 million preference complaint. The complaint alleged that the trustee had "request[ed] identification and substantiation of any verifiable defenses" and that the supplier "failed to supply any viable and provable basis for defenses."

The supplier responded to the complaint with a motion to dismiss under Rule 12(b)(6), alleging that the trustee had "failed to allege its compliance with [the due diligence] requirement [in Section 547(b)] and has ignored [the supplier's] defenses, even after [the supplier] provided a detailed explanation of the law and evidence supporting its status as a secured creditor by virtue of its agricultural input lien."

Judge Somers denied the motion to dismiss.

Conditions Precedent

By amendment in 2019, Section 547(b) now provides that a "trustee may, based on reasonable due diligence in the circumstances of the case and taking into account a party's known or reasonably knowable affirmative defenses," file a complaint to recover a preference.

Judge Somers characterized the motion to dismiss as contending "that the Trustee failed to perform reasonable due diligence by simply and generically averring in the Complaint." The motion then went on to detail the supplier's defenses.

Opposing the motion to dismiss, the trustee said that he had considered the proffered defenses but decided that they did not state a provable defense. The trustee also argued that the due diligence pleading requirement is governed by Rule 9(c), which only requires general allegations.

Bankruptcy Rule 7009 incorporates Federal Rule 9 in adversary proceedings. "In pleading conditions precedent," Rule 9(c) provides that "it suffices to allege generally that all conditions precedent have occurred or been performed."

Citing a law dictionary, Judge Somers said that a "condition precedent is '[a]n act or event, other than a lapse of time, that must exist or occur before a duty to perform something promised arises.'" He went on to quote the *Collier* treatise for saying, "'[I]t is clear that the due diligence requirement is a condition precedent. As such, a general allegation that the Trustee has performed due diligence satisfies the due diligence requirement. The Trustee need not plead around potential affirmative defenses.'"

In addition, Judge Somers cited the Third Circuit in saying that the "pleading of conditions precedent falls outside the *Iqbal/Twombly* standard which governs Rule 8(a)."

Still, the Bankruptcy Code does not define "reasonable due diligence," Judge Somers said. "Nor does it set forth how a Trustee takes into account 'a party's known or reasonably knowable affirmative defenses.'"

Rule 9(c)

"Because the due diligence requirement is a condition precedent," Judge Somers said he was obliged to "evaluate, under Rule 9(c), whether the Trustee generally alleged that the due diligence requirement was met."

In the complaint, the trustee alleged that he had reviewed the debtor's books and records and analyzed the supplier's "applicable and provable defenses." The trustee also alleged that the supplier's response to the demand letter did not lay out any viable defenses.

"In short," Judge Somers said, "the Trustee alleges that he investigated the transfers and any defenses to their avoidance." Consequently, he held that the "Trustee's allegations were competent and sufficient to generally allege the condition precedent of due diligence in the circumstances of the case."

Denying the motion to dismiss, Judge Somers held:

> Trustee is not required to "plead around the defenses" by describing which defenses he considered and why he determined that they were not viable or what his reaction to Defendant's explanation of its defenses might have been. It is sufficient that Trustee alleged he did not find any viable defenses. Trustee is further not required to plead his due diligence efforts with any particularity but that they generally occurred as required by Rule 9(c).

Observations

The sufficiency of a complaint to survive a motion to dismiss is one thing, but Rule 11 is another.

In a five-page single-spaced letter sent to the trustee before the complaint was filed, the supplier argued there was a valid lien obviating a preference. What if the supplier prevails on a motion for summary judgment? What's the standard to decide whether the trustee is liable for sanctions under Rule 11 for filing a complaint that's knocked out on undisputed facts when the trustee was required to perform due diligence before filing the complaint?

The opinion is *Rebein v. NutriQuest LLC (In re Sandy Road Farms LLC)*, 25-7001 (Bankr. D. Kan. Oct. 22, 2025).

***Truck Insurance* notwithstanding, an insurer that has denied coverage for abuse claims doesn't have the right to object to claims.**

Judge Grabill Discusses an Insurer's Standing for Objecting to Abuse Claims

In confirming the chapter 11 plan for the Archdiocese of New Orleans, Bankruptcy Judge Meredith S. Grabill suggested that an insurance company that had not admitted liability to pay sexual abuse claims did not have the right to object to the allowance of claims.

In her December 9 opinion, Judge Grabill explained that the plan created a trust with a total of $230 million, including $30 million from settling insurers who purchased the policies they had issued "free and clear" under Section 363.

A non-settling insurer objected to confirmation of the plan unless the insurer's rights to object to the allowance of abuse claims were "fully preserved." Judge Grabill noted that none of the funds in the creditors' trust came from the objecting insurer. However, the debtor's claims against the objecting insurer would be transferred to the trust.

The Objecting Insurer's Standing

The insurer's objection raised the issue of standing, a concept covered by Bankruptcy Rule 1109(b). The subsection provides that a "party in interest, including the debtor, the trustee, a creditors' committee, . . . a creditor, . . . or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter."

With standing being the pivotal issue, Judge Grabill naturally began by citing the Supreme Court's dissertation on standing last year in chapter 11, *Truck Insurance Exchange v. Kaiser Gypsum Company, Inc.*, 602 U.S. 268 (June 6, 2024). She said that the Supreme Court "recognized . . . that the use of § 1109(b)'s broad language was part of an 'effort to encourage and promote greater participation in reorganization cases,' as Congress was concerned that 'a few insiders, whether representatives of management or major creditors, could use the reorganization process to gain an unfair advantage.' 602 U.S. 268, 280 (2024)." To read ABI's report, click here.

On the other hand, Judge Grabill quoted a bankruptcy judge from New York who decided that someone without a "financial interest" in the case is "generally excluded" from the definition of a party in interest. Indeed, the Supreme Court said that the insurer in *Truck Insurance* had "financial responsibility for bankruptcy claims."

In the archdiocese's case, Judge Grabill said that hundreds of claimants had filed claims against the debtor, but not against the objecting insurer. Unlike the insurer in *Truck Insurance*, she said that the objecting insurer's "liability to defend and pay on abuse claims here has neither been adjudicated nor has [the objecting insurer] formally accepted responsibility to pay for those claims."

Judge Grabill went on to say that the objecting insurer was asking her for authority "to file a declaratory action in federal district court challenging insurance coverage for abuse claims filed against the Debtor." In that regard, she paraphrased a bankruptcy judge from upstate New York who asked how insurers can have "standing to object to proofs of claim on the basis that they are likely to contribute to the bankruptcy distribution while simultaneously claiming they are under no obligation to make said contribution."

"Nevertheless," Judge Grabill decided to follow a bankruptcy judge in Delaware who recently held in a close case that the court should err on the side of considering an objection on the merits when standing is at issue.

The Merits

Judge Grabill dealt with the merits in less than one page.

The objecting insurer was concerned that some claims would be allowed although they were filed after the bar date.

Judge Grabill said that the insurer's "own rights are well preserved," because the "settlement trust will not be funded by any contribution by [the objecting insurer] without [the objecting insurer's] consent via settlement or adjudication by a court of competent jurisdiction." In addition, the plan specifically preserved all of the insurer's rights and defenses.

Should the trust sue the objecting insurer, Judge Grabill said that it "is free to assert a defense pertaining to the timeliness of the filing of any proof of claim in this bankruptcy case before that tribunal."

Judge Grabill overruled the objection and confirmed the plan, while deleting a provision in the plan that could have been read to give the objecting insurer the right to object to proofs of claim.

The opinion is *In re Roman Catholic Church of the Archdiocese of New Orleans*, 20-10846 (Bankr. E.D. La. Dec. 9, 2025).

Embezzlement from an LLC conferred standing to sue on an owner, not only on the LLC.

Creditor With a Derivative Claim Has Standing to Sue, Fifth Circuit Says

Based on the broad definition given the word "claim," a creditor has standing to bring a nondischargeability suit against an individual debtor for embezzlement when the debtor didn't embezzle from the creditor but embezzled from a company co-owned by the creditor and the debtor.

In other words, an owner of an embezzled LLC had standing to sue, not just the embezzled LLC itself.

The creditor and the debtor were co-owners of an LLC that operated an evidently profitable business. When the creditor believed he was not receiving profit distributions to which he was entitled, he sued the debtor in state court, prompting the debtor to file a chapter 7 petition.

Alleging that the debtor had transferred some $300,000 from the LLC to another entity that the debtor owned, the creditor filed a complaint in bankruptcy court alleged that the $300,000 debt was nondischargeable as embezzlement under Section 523(a)(4).

Bankruptcy Judge Jeffrey Norman of Houston decided that the creditor had a personal interest in the funds and ruled that the debt was nondischargeable. After the district court affirmed, the debtor filed a second appeal to the Fifth Circuit.

The Fifth Circuit affirmed in a nonprecedential, *per curiam* opinion on February 3.

Broad Definitions Confer Standing

On appeal, the debtor primarily argued that the creditor had no standing to sue because she had not allegedly embezzled from the creditor, but from the LLC.

The Fifth Circuit panel reasoned that the question about standing turned on the definitions of "claim" and "creditor."

Under Section 101(10)(A), a "creditor" is someone who has a "claim." In turn, "claim" is defined in Section 101(5)(A) as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."

From Supreme Court authority, the circuit panel said that "claim" has the "'broadest available definition'" and encompasses "'all legal obligations of the debtor, no matter how remote or contingent.'"

Based on the creditor's ownership interest in the LLC, the panel held that the debtor "possessed a 'claim' against . . . the debtor [] within the meaning of § 101(5), and he thus qualified as a 'creditor' of [the debtor's] estate under § 101(10)."

The panel affirmed, holding that Bankruptcy Judge Norman "correctly determined that [the creditor] had standing to pursue his [nondischargeability] claim."

Observations

The opinion is important. There can be many instances in which the direct victim of fraud is incapable of suing. In this writer's opinion, the opinion should be published and precedential.

Consider the following, however: Had the LLC itself been in bankruptcy, the embezzlement claim would have belonged to the LLC, not the creditor. Would the claim be derivative, not direct, thus precluding the creditor's standing to sue?

By ruling that the $300,000 claim was nondischargeable as to the owner, was the Fifth Circuit holding that the claim belonged to the owner, presumably as a direct claim, not a derivative claim?

The opinion is *DiBassie v. Reeves (In re DiBasse)*, 25-20170 (5th Cir. Feb. 3, 2026).

So long as the lender has made a prima facie showing of lien validity, the lender is entitled to adequate protection, a Houston district judge says.

Cash Collateral Motions Can't Rule on the Validity/Invalidity of a Secured Claim

If a secured creditor makes a *prima facie* showing that the security interest in valid, the creditor "is entitled to adequate protection [for the use of cash collateral] until an adversary proceeding determines the validity, extent, and priority of the asserted property interest," according to an appellate ruling by District Judge Lee H. Rosenthal of Houston.

Judge Rosenthal's January 31 opinion means that the bankruptcy court may not consider the likelihood of success on the merits about the validity of the security interest when it comes to granting the use of cash collateral.

The appeal stemmed from the chapter 11 reorganization of First Brands Group LLC begun in Houston in late September. According to unverified news reports, the debtor may have sold or financed the same receivables several times or financed receivables that did not exist.

Under Section 363(c)(2), the debtor sought to use $63 million in cash collateral. Judge Rosenthal described the secured creditor as objecting on the grounds that not enough would remain after usage of cash collateral to satisfy its asserted secured claim of $60.5 million.

The bankruptcy court authorized the use of $60 million in cash collateral. Judge Rosenthal described the bankruptcy court as finding that $49 million would remain in the receivables account after usage of cash collateral. The lender contended that the account would then be $20 million short of protecting its claim in full.

Judge Rosenthal said that "the bankruptcy court did not definitively rule on the validity or nature of [the lender's security interest] and cautioned that its assessment was preliminary." Judge Rosenthal went on to say that the bankruptcy court "was not convinced that [the lender] had priority over other creditors." However, she described the bankruptcy court as authorizing "the release of the funds because, whoever held the priority interest, that interest was adequately protected."

The lender appealed. Judge Rosenthal granted an expedited hearing.

Procedure on Interim Cash Collateral Usage

Appointed by Chief Justice Roberts in 2007, Judge Rosenthal chaired the Judicial Conference Committee on Rules of Practice and Procedure. Not surprisingly, her opinion focuses on procedure.

Before turning to procedure, Judge Rosenthal cited Section 363(c)(2) for prohibiting a debtor from using cash collateral unless, "after notice and a hearing, [the bankruptcy court] authorizes such use . . . in accordance with the provisions of this section." Then, Section 363(e) kicks in to provide that the court must "condition such use, sale, or lease as is necessary to provide adequate protection of such interest."

Turning to procedure, Judge Rosenthal alluded to Bankruptcy Rule 4001(b)(2). "After a preliminary hearing," the rule provides in part that "the court may authorize using only the cash collateral necessary to avoid immediate and irreparable harm to the estate pending a final hearing."

In the case on appeal, Judge Rosenthal said,

> The bankruptcy court did not consider its ruling authorizing [the debtor] to use up to $60 million in funds to be an "interim" determination. . . . Nor did the bankruptcy court make findings that allowing [the debtor] to use the funds was necessary to avoid immediate and irreparable harm to the estate pending a final hearing . . . . The ruling allowing [the debtor] to spend up to $60 million in cash collateral was a final determination under § 363(e).

Further on procedure, Judge Rosenthal said "that bankruptcy courts ruling under § 363(e) may conduct some examination of lien validity," because Section 363(p)(2) provides that "the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest."

Judge Rosenthal cited cases where "[c]ourts appear to resolve some disputes under § 363(e) on the ground that the entity asserting a property interest could not bear its burden of proving that interest." However, she said that those cases were

> in tension with the Bankruptcy Rules and other case law, which suggest that, in the absence of an adversary proceeding, bankruptcy courts addressing requests for relief that raise questions about an asserted property interest should assess only whether the party asserting the interest has made a *prima facie* showing of the validity and scope of that interest. Consistent with this limited burden, courts may consider whether there is evidence that "clearly refutes a creditor's claim to the property."

Quoting the Eighth Circuit Bankruptcy Appellate Panel, Judge Rosenthal said that "the substantive consideration of such evidence should stop as soon as it appears that the" party asserting the property interest "has a 'colorable claim' to the property in question."

Judge Rosenthal explained why the court cannot determine the validity of a lien on a cash collateral motion:

> Permitting a broader or deeper inquiry into the validity of an asserted property interest at a preliminary hearing on the use of cash collateral would bypass Rule 7001(b)'s general requirement that parties must challenge lien validity through an adversary proceeding, not an adequate protection hearing.

Judge Rosenthal gave further justification for her ruling:

> Weighing the likelihood of success on the merits of establishing a secured interest against the likelihood of success in showing that available cash collateral would adequately protect that interest would also bypass § 363(c)(3)'s and Rule 4001(b)(2)'s rules and regulations for preliminary hearings on the use of cash collateral.

Judge Rosenthal therefore held:

> [A]bsent clear evidence or legal precedent that refutes the claimant's right to an asserted property interest, the claimant is entitled to adequate protection until an adversary proceeding determines the validity, extent, and priority of the asserted property interest.

On Remand

Based on the record as of the time of the cash collateral hearing, Judge Rosenthal decided that the lender was not adequately protected because the account would not contain sufficient funds to cover the lender's $60.5 million claim. During the appeal, however, the debtor had submitted later-developing facts tending to show that the collection of receivables after filing was replenishing the account with funds to cover the claim in full.

Judge Rosenthal did not reverse. Rather, she remanded for the bankruptcy court to conduct further proceedings in accordance with her order, including, "appropriate procedures" to determine whether the lender had a valid and enforceable lien and whether the lender was adequately protected by the collection of accounts receivable.

If the bankruptcy court on remand finds adequate protection, Judge Rosenthal said that the court "must state specifically what funds or other property, whether currently in the estate or projected to be in the estate (and on what basis), adequately protect [the lender]."

The opinion is *Evolution Credit Partners v. First Brands Group LLC (In re First Brands Group LLC)*, 26-73 (S.D. Tex. Jan. 31, 2026).

Copyright termination rights not exercisable for decades remained estate property because they were not scheduled as assets.

Inalienable Copyright Termination Rights Were Bankruptcy Estate Property

In a case "of first impression at the intersection of copyright and bankruptcy," the Eleventh Circuit held that the "termination interest" in a copyright is a property interest that remains in the bankruptcy estate after discharge if it was not scheduled as an asset and was therefore not automatically abandoned.

At the time of bankruptcy, a copyright termination interest is a property right that might not be exercisable for many years. The circuit's holding presents problems: (1) Holders of copyrights and their bankruptcy lawyers may be unaware of termination rights; (2) termination rights might not be exercisable until years after bankruptcy; and (3) a termination right that might have value years later probably had negligible value at the time of bankruptcy.

Termination Rights Under Copyright Law

To appreciate the significance of the facts in the appeal, Circuit Judge Andrew L. Brasher explained the workings of Section 203(a) of the Copyright Act, 17 U.S.C. § 203(a).

Without delving into all of the details, understand that the author or authors can exercise termination rights by serving a written notice two to 10 years before the effective date of the termination. A majority of the copyright holders must sign the termination notice.

Judge Brasher said that "the effective date [of the termination] must fall during a five-year window that begins no earlier than thirty-five years after a grant of the copyright."

In his June 2 opinion for the circuit, Judge Brasher said that Section 203 makes termination rights "inalienable by agreement" and can be effected "'notwithstanding any agreement to the contrary.'" The section, he said, "restricts the inheritors of the interests to close family members or the author's executor, administrator, personal representative, or trustee."

Summarizing, Judge Brasher said that an "artist's termination interests are personal and inalienable, although they can be passed to an artist's heirs."

Rap Albums' Termination Rights

A rap group with four members recorded five albums between 1986 and 1989. The four members gave copyrights in the master recordings to a record company. One of the band members owned the record company.

In 1995, five years after the record company's last option to extend the copyright agreement, the record company and its owner, the band member, filed joint chapter 11 cases where they sold all of their copyrights to a company we shall refer to as the buyer.

In 2000, another band member filed a chapter 7 bankruptcy. We shall refer to him as the debtor.

The debtor did not schedule his copyright termination interests as being among his assets. That was no surprise, because the year 2000 was more than nine years after the last possible effective date of the copyright agreement but more than 10 years *before* the band members could terminate copyright interests.

In 2020, within the window for noticing termination rights, the debtor and two other band members served a termination notice purporting to terminate the buyer's copyright interests.

After receiving the termination notice, the buyer sued and sought a declaration that the copyrights had not been terminated because the debtor's interests in the copyrights still belonged to the debtor's bankruptcy trustee, who had not signed the termination notice. For not having been scheduled as an asset, the owner theorized that the copyright interests remained in the debtor's bankruptcy estate under Section 554(d).

Following denial of cross motions for summary judgment, the district court held a trial. Based on the jury's findings, the district court held that the termination was valid. The buyer appealed to the circuit.

Termination Rights Remained Estate Property

Judge Brasher reversed, holding that "the termination notice was ineffective" because it had not been signed by a majority of those who held the termination rights.

On the law, Judge Brasher held that a termination right is an "interest . . . in property" under Section 541(a) because "it is a contingent right to regain intellectual property." Similarly, he said that "termination interests are contingent rights to regain that intellectual property years after transferring it away."

Closing the circle under Section 541(a), Judge Brasher ruled that termination rights existed at the commencement of the bankruptcy case and thus were property of the debtor's estate.

Judge Brasher rejected the idea that the termination rights could not become estate property because they were personable and inalienable. He said, "[B]ankruptcy law sweeps termination interests into a debtor's estate under section 541 'notwithstanding any provision in . . . applicable nonbankruptcy law' that 'restricts or conditions transfer of such interest[s] by the debtor.' 11 U.S.C. § 541(c)(1)."

On the question of inalienability, Judge Brasher quoted the Eleventh Circuit for saying that "specific law is ordinarily 'treated as an exception to the general rule.'" He held that the Copyright Act's Section 203 was the general rule overcome by Section 541 and its "specific exception to that rule that permits those interests to enter bankruptcy estates."

Because a majority of band members had not signed the termination notice, Judge Brasher reversed and remanded "for further proceedings consistent with this opinion."

Judge Brasher left the door open for the court on remand to find a valid termination because he said that the circuit did "not address how termination interests should be treated in bankruptcy. And we do not decide today what [the debtors'] heirs need to do to exercise those interests in the light of his bankruptcy."

Observations

What's a specific law and what's a general rule can be in the eyes of the beholder. Nonetheless, this writer tends to see the statutory inalienability of copyright reversionary interests as specific law, while Section 541(a)'s sweep of "all legal or equitable interest" is a general law applicable to all types of contingent or future rights, not just copyright interests.

Had the debtor or counsel known about termination rights, and had those rights been scheduled as assets in the debtor's bankruptcy case, termination rights would have had negligible value, would not have been administered and would have been abandoned. In other words, termination rights had no value to the debtor's creditors in 2000 but did have value for creditors 26 years after bankruptcy.

Developing those thoughts, Prof. Robert M. Lawless provided ABI with the following commentary:

> Perhaps no debtor in the history of bankruptcy law has scheduled these termination rights, especially years before the debtor had a right to exercise them. Even if this debtor had scheduled the termination rights, they held no value to repay creditors. Their disclosure would not have made any difference in the outcome of the bankruptcy filing.

The holding is a cousin to the judicial estoppel doctrine, currently pending before the Supreme Court in *Keathley*, where a nondisclosure of no consequence becomes a game of "gotcha" to deprive a debtor of valuable rights outside the bankruptcy case.

The courts might consider developing a "harmless error" framework to distinguish between cases where debtors rightfully suffer the consequences of a knowing nondisclosure and cases where missing information stems from an inadvertent omission of filling out more than sixty pages of forms demanding information on all aspects of a debtor's financial situation.

Prof. Lawless is the Max L. Rowe Professor of Law and co-director of the Program on Law, Behavior & Social Science at the University of Illinois College of Law.

The opinion is *Lil' Joe Records Inc. v. Ross*, 24-13978 (11th Cir. June 2, 2026).

The 'faltering company' exception to WARN Act liability excused the liquidating debtor from giving a 60-day notice of mass layoffs.

Delaware District Judges Describes How to Avoid WARN Act Liability in Shutting Down

A district judge in Delaware wrote a handbook telling managers how to shut down a failing business and draft a notice to employees that will avoid Worker Adjustment and Retraining Notification Act (WARN Act) liability for not giving a 60-day notice of mass layoffs.

The Precipitous Trucker Liquidation

The debtor was Yellow Corp., one of the country's largest truckers. In precarious financial condition, the company hired an investment banker to negotiate with new investors or modify existing loan agreements. Liquidity almost exhausted, the company asked the union pension fund for a deferral of a pension contribution. The union pension fund refused.

When the company didn't make the pension contribution, the union gave notice of a strike in 72 hours. Both sides saw the strike notice as a bluff, but customers reacted otherwise. Daily shipments fell from 50,000 to almost nothing in a matter of days. The union called off the strike, but the damage was done.

New financing or modification of loan agreements no longer feasible, the company stopped accepting new loads, planned on making the last deliveries by July 29, 2023, and shut down on July 30. At the time of the shutdown, the company sent a WARN Act notice to the union and the workers. In relevant part, it read,

> The Company was not able to provide earlier notice of the Shut Down as it qualifies under the "unforeseeable business circumstances," "faltering company," and "liquidating fiduciary" exceptions set forth in the WARN Act. The Company expects all layoffs and location closures relating to the Shut Down to be permanent. The Company had hoped to complete one or more transactions and secure funds and business to prevent the closing of these locations but was unable to do so. These circumstances were not reasonably foreseeable at the time notice would have otherwise been required and notice is further excused because the business is being liquidated.

One week later, the company filed a chapter 11 petition in Delaware to liquidate. The union filed claims under the WARN Act, 29 U.S.C. §§ 2101-2109, because workers were not given a 60-day notice of the mass layoffs. After discovery, the debtor and the union filed cross motions for summary judgment.

The bankruptcy judge decided that the company qualified for the "faltering company" and "unforeseeable business circumstances" exceptions under the WARN Act. However, he gave partial summary judgment to the union, ruling that the company could not avail itself of the exceptions because the notice had not given workers enough facts to justify the shutdown on short notice.

However, the bankruptcy judge found factual disputes as to whether the company was an "employer" under the WARN Act when it gave the layoff notices. A short time later, the judge held a trial and decided that the company was not an "employer" subject to the WARN Act when it issued the layoff notices, because the trucker had completed the last deliveries when the workers were fired. He therefore concluded that it was no longer a "business enterprise" but had become a "liquidating fiduciary."

The decision after trial meant that the union had no WARN Act claim. Cross notices of appeal brought the dispute before District Judge Jennifer L. Hall of Delaware.

Faltering Company

In her June 29 decision, Judge Hall first looked into whether the debtor was a "faltering company." She said,

> The faltering company exception excuses the WARN Act's 60-day notice requirement if, at the time notice would have been required, the employer was "actively seeking capital or business" that would have "enabled the employer to avoid or postpone the shutdown," and the employer "reasonably and in good faith believed" that providing the required WARN notice "would have precluded the employer from obtaining the needed capital or business." 29 U.S.C. § 2102(b)(1).

Judge Hall agreed "with the Bankruptcy Court that Yellow was a faltering company at the time notice was required" because it "was actively seeking capital at the required time."

Barely Adequate Notice

Next, Judge Hall turned to the question of whether the notice to workers contained sufficient reasons for short notice. She described the statutory provision as follows:

> The WARN Act provides that "[a]n employer relying on [one of the statutory exceptions] shall give as much notice as is practicable and at that time shall give a brief statement of the basis for reducing the notification period." 29 U.S.C. § 2102(b)(3).

Judge Hall said that the "Third Circuit has not delineated the minimum contents of the required 'brief statement.'" However, she went on to say that "both the Third and Ninth Circuits have suggested that a statement is compliant where it sufficiently 'assist[s]' the employees in 'understand[ing] the employer's situation and its reasons for shortening the notice period.' *Alarcon v. Keller Indus., Inc.*, 27 F.3d 386, 389 (9th Cir. 1994)."

Quoting the Ninth Circuit, Judge Hall said that notice is sufficient if it

> (i) cited the subsection of the WARN Act containing the faltering company exception and (ii) explained that the business's performance "has been disappointing and the substandard working capital required of business does not make it a viable entity," that the employer "pursued several options for possible purchase, but was unable to secure a qualified buyer," and that the employer "was unable to find parties interested in supplying the enormous working capital for such a high risk and under performing business." *Alarcon*, 27 F.3d at 388.

Judge Hall said that the "question is close," but she found that the debtor's notice "complied with the statute," because the "notice makes clear which statutory exception is being relied upon —the 'faltering company' exception — and it explains that Yellow had hoped to complete one or more transactions and secure funds and business to prevent the closing of its locations but was unable to do so."

Judge Hall admitted that the notice in the Ninth Circuit case "had more words," but she held that "Yellow's notice conveys the same substance." An employee, she said, "would understand, at a minimum, that he or she was receiving the notice on a shortened period because the company's efforts to obtain financing and business necessary to survive failed."

Because Judge Hall held that the debtor's notice contained "the requisite brief statement" required for the faltering company exception, she "affirm[ed] the Bankruptcy Court's disallowance of the Unions' federal WARN Act claims."

Observation

To avoid presenting the court with a "close" case, Judge Hall's is recommending that counsel in future cases draft notices with "more words" along the lines of the notice in *Alarcon*.

The opinion is *International Brotherhood of Teamsters v. Yellow Corp.*, 25-307 (D. Del. June 29, 2026).

Small Biz. Reorg. Act

Bankruptcy Judge Jason Burgess agrees with Bankruptcy Judges John Mastando and Meredith Grabill that Purdue doesn't preclude a five-year injunction as part of a Subchapter V plan.

Another Court Approves a Nondebtor Injunction for the Five-Year Life of a Sub V Plan

A bankruptcy court has approved another Subchapter V plan enjoining lawsuits against a nondebtor for the five-year life of the plan.

Bankruptcy Judge Jason A. Burgess of Jacksonville, Fla., said that *Harrington v. Purdue Pharma L.P.*, 603 U.S. 204 (2024), "targeted non-consensual third-party permanent releases, not temporary injunctions that are at issue here." In a September 2 opinion, he said that the U.S. Trustee was seeking "to stretch [the] implications [of *Purdue*] beyond their intended reach."

The corporate debtor recruited engineers. The owner was the only employee and the only person who brought in new clients. An employer would pay the debtor a percentage of the salary of someone placed by the debtor.

Evidently, the owner had guaranteed some of the debtor's debts. The plan included an injunction barring suits against the owner for the five-year life of the plan. The injunction would dissolve on discharge, dismissal, plan default or the owner's termination of employment by the debtor.

The only objection to confirmation came from the U.S. Trustee, who argued that the injunction was barred by *Purdue*. To read ABI's report on *Purdue*, click here.

Judge Burgess said that courts have "narrowly construed" *Purdue* and that the Supreme Court was dealing with "non-consensual third-party permanent releases rather than temporary injunctions."

Purdue, Judge Burgess said, "found that § 1123(b)(6), in conjunction with § 105, does not permit bankruptcy courts to issue non-consensual third-party releases." He added, "The Supreme Court did not consider § 1123(a)(5), which the Court finds distinguishable from § 1123(b)(6)."

Judge Burgess pointed out how Section 1123(a)(5) contains a nonexhaustive list of means for implementing a plan, not a catchall phrase like Section 1123(b)(6). In the case at hand, he said that "the Plan Injunction is necessary for implementation of the plan and thus is authorized by § 1123(a)(5) in conjunction with § 105."

"Other courts," Judge Burgess said, "have also found a temporary injunction like the one here to be necessary 'to facilitate the successful implementation of the Plan.'" He cited *In re Hal Luftig Co.*, 667 B.R. 638 (Bankr. S.D.N.Y. Feb. 24, 2025), by Bankruptcy Judge John P. Mastando, III, and *In re Miracle Restaurant Group LLC*, 24-11158, 2025 BL 163588, 2025 Bankr Lexis 1188 (Bankr. E.D. La. May 13, 2025), by Bankruptcy Judge Meredith S. Grabill. To read ABI's reports, click here and here.

Having decided that temporary injunctions are not categorically prohibited in Subchapter V plans, Judge Burgess addressed the Fifth Circuit's two *Zale* factors and the four-factor test for temporary injunctions to determine whether a temporary injunction was appropriate in the case at hand. *See Feld v. Zale Corp. (In re Zale Corp.)*, 62 F.3d 746 (5th Cir. 1995).

Judge Burgess decided that *Zale* was satisfied, in part because the debtor's ability to perform the plan was entirely dependent on the owner. Regarding the test for temporary injunctions, he said that the plan injunction "will merely delay the enjoined creditors from collecting," because the plan would toll statutes of limitations. In fact, he said that the owner "may be better situated to pay a meaningful distribution towards his debts" five years from now when the plan is over.

Having found compliance with *Zale* and the requirements for a temporary injunction, Judge Burgess overruled the objection to the five-year injunction and confirmed the plan.

The opinion is *In re Engineering Recruiting Experts LLC*, 24-03292 (Bankr. M.D. Fla. Sept. 2, 2025).

Contrary to the language in Section 1190(3), the bankruptcy court did not allow bifurcation of a lien that wasn't used to acquire a home but was used for the debtor's small business.

Section 1111(b) Election Held Applicable in Sub V Despite Section 1190(3)

In Subchapter V of chapter 11, an individual debtor has the unique ability under Section 1190(3) to modify a home mortgage if the mortgage was "not primarily used" to acquire the home and instead was used "primarily in connection" with the debtor's small business.

In an opinion on October 2, Bankruptcy Judge Ashley Austin Edwards of Charlotte, N.C., sided with the *Collier* treatise in holding that the more general rule in the Section 1111(b) election enables a lender to prevent a Subchapter V individual debtor from using Section 1190(3) to modify a home mortgage.

Home Mortgage Secured a Small Business Loan

In 2017, a couple purchased their home. Six years later, the husband's corporate business borrowed $1 million from a bank. The lender and the Small Business Administration required the husband and his wife to issue personal guarantees on the loan, secured by a lien on their home. Following default, the lender obtained a judgment in state court against the husband and wife and the husband's corporation.

The husband and wife filed a chapter 11 petition in 2025, electing to proceed under Subchapter V. The lender filed a proof of claim for more than $1.2 million, asserting that about $465,000 was secured and $775,000 was unsecured.

Under Section 1111(b)(2), the lender filed an election to have the entire claim treated as secured. The debtors filed an objection to the election, contending that the ability to modify a lien on a home under Section 1190(3) takes precedence over the Section 1111(b) election. Judge Edwards agreed with the lender and overruled the debtors' objection.

Section 1111(b) Wasn't Excluded from Sub V

Judge Edwards was tasked with deciding "whether a Subchapter V debtor's unique ability to modify a claim secured by their primary residence under § 1190(3) overrides a creditor's right to make the § 1111(b) election to have its entire claim treated as secured."

Pointing to Section 1123(b)(5), Judge Edwards said that debtors in chapter 11 "cannot modify a claim secured only by a security interest in the debtor's primary residence."

Applicable only in Subchapter V, though, Section 1190(3) provides that a debtor "may modify the rights of the holder of a claim secured only by a security interest in real property that is the principal residence of the debtor if the new value received in connection with the granting of the security interest was — (A) not used primarily to acquire the real property; and (B) used primarily in connection with the small business of the debtor."

Section 1111(b) is on the other side of the fence. Ordinarily under Section 506(a)(1), a secured claim is allowed as a secured claim to the extent of the value of the collateral, with the deficiency allowed as an unsecured claim. When a claim otherwise would be bifurcated in that matter, a secured creditor in chapter 11 may make the election under Section 1111(b). "[T]hen notwithstanding section 506(a) of this title," the subsection provides that "such claim is a secured claim to the extent that such claim is allowed."

Judge Edwards explained the effect of Section 1111(b) as follows:

> It is well understood that notwithstanding the plan's ability to modify claims secured by other types of collateral under § 1123(b)(5), § 1111(b)(2) allows creditors who have a partially secured claim to elect to have their entire claim treated as secured.

Although Section 1190(3) "gives individual Subchapter V debtors a unique opportunity to modify the liens of creditors secured by their primary residence," Judge Edwards saw "no evidence that it overrides or takes away the creditors' right to elect under § 1111(b)." She was following the *Collier* treatise, which says that an undersecured creditor in Subchapter V, "like any undersecured creditor, [may] elect the application of section 1111(b) to have its entire claim treated under the plan as secured by its collateral."

Although conceding that "§ 1190(3) is more specific and that the legislative intent behind Subchapter V was to protect small business owners," Judge Edwards decided that "§ 1181(a) [is] dispositive as to this issue." While Section 1181(a) "identifies general Chapter 11 provisions that do not apply in Subchapter V cases," she said, "[n]otably, § 1111 is not included."

Overruling the debtors' objection to the debtor's Section 1111(b) election, Judge Edwards held "that an § 1190(3) election — whether proper or not — does not override an § 1111(b) election."

Observations

Section 1190(3) seems designed for precisely the type of case confronting Judge Edwards. As she pointed out, however, Section 1181(a) did not exclude Section 1111(b) from Subchapter V cases. Was the omission of Section 1111(b) a mistake in drafting Section 1181(a) of Subchapter V?

By applying Section 1111(b) in all Subchapter V cases, Section 1190(3) serves virtually no purpose because it could be applicable in a plan only when the secured creditor consents. If Section 1190(3) only works when the secured creditor consents to bifurcation, why include Section 1190(3) in the first place? Was it included in Subchapter V only to cover cases when the secured creditor is inattentive? Perhaps Section 1190(3) would have utility when the lender consents, but the bankruptcy court wouldn't otherwise approve the plan for violating Section 1123(b)(5).

The inclusion of Section 1190(3) seems peculiar if it's only effective when the secured creditor consents.

Sections 1190(3), 1111(b) and 1181(a) could be read together in a fashion where they are not at war.

Take a more typical case of a corporate debtor in Subchapter V with secured debt. Likely as not, the drafters did not exclude Section 1111(b) from Subchapter V to prevent a corporate debtor from bifurcating secured debt over objection from the lender. The drafters could have included Section 1190(3) for application in atypical cases where the debtor is an individual with a home mortgage. In those cases, bifurcating a mortgage makes sense when the lien on a home was not used to acquire the home.

Perhaps the more specific Section 1190(3) can apply to individual Subchapter V debtors without doing violence to Section 1111(b) in typical corporate reorganizations. Time will tell how courts come down on the issue.

The opinion is *In re Joiner*, 25-30396 (Bankr. W.D.N.C. Sept. 2, 2025).

Lack of a required demand meant that a debt was contingent and not counted in Subchapter V eligibility.

Equitable Mootness Inapplicable to Subchapter V, Third Circuit Says

The Third Circuit said that the doctrine of equitable mootness is not available in Subchapter V cases and described what "noncontingent, liquidated" means in terms of eligibility for Subchapter V of chapter 11.

A corporate debtor filed a petition under Subchapter V of chapter 11 when the debt limit was $7.5 million at the time under Section 1182(a)(A)(2022). The schedules showed debt totaling more than $3.4 million, including a judgment.

The debtor was liable on a guarantee of an affiliate's obligations under a lease. When the lease was in default, the lease was amended before bankruptcy to provide that the amount owing would vary from time to time and that the landlord would "make written demand" for a "specified amount."

At the time of the Subchapter V filing, the landlord had made no written demand. However, the landlord filed a claim for more than $3.7 million.

The judgment creditor filed a motion challenging the Subchapter V election, contending that debt exceeded $7.5 million. The bankruptcy court decided that the lease guaranty obligations were contingent and unliquidated, allowing the debtor's perseverance in Subchapter V.

The bankruptcy court also approved a settlement where insiders were given releases in return for $25,000. When the bankruptcy court approved the debtor's plan, the judgment creditor appealed both confirmation and approval of the settlement.

Equitable Mootness

The debtor argued for dismissal of the appeal based on equitable mootness.

The Third Circuit's July 28 opinion by Circuit Judge Patty Schwartz dealt with equitable mootness in a footnote. She said,

> [E]quitable mootness is "only available in complex bankruptc[ies] where the reorganization involves intricate transactions." *In re Boy Scouts of Am.*, 137 F.4th 126, 160 (3d Cir. 2025).

Subchapter V, Judge Schwartz said, "is less complicated by design." Since the debtor's plan involved a single, integrated transaction, she said that the Subchapter V case "lacks the complexity to which equitable mootness has been applied, [s]o the appeal here will would not be deemed equitably moot."

No Demand Meant Debt Was Contingent

Turning to eligibility for Subchapter V, Judge Schwartz said that the debtor "was required at the time] to have less than $7.5 million in liquidated, noncontingent debt as of the Petition Date." She held that the debt "was contingent on the Petition Date," because "the debtor's obligation to pay does not come into being until some future event occurs, even if the parties could have predicted the event when their relationship began."

Judge Schwartz went on hold that the debt was contingent because the landlord "did not make any written demand until after [the debtor] filed its bankruptcy petition."

Similarly, Judge Schwartz said that the debt was unliquidated because the amount was not "readily and precisely determinable," since the debtor "had not received any invoices, and the monthly amount due under the leases fluctuated based on several factors." She therefore ruled that "the Bankruptcy Court correctly determined that the . . . debt was unliquidated as of the Petition Date."

Proceeding to decide that the bankruptcy court had not abused its discretion in approving the settlement, Judge Schwartz affirmed the confirmation order and the order approving the settlement.

The opinion is *Reed Action Judgment Creditors v. Alecto Healthcare Services LLC (In re Alecto Healthcare Services LLC)*, 25-1853 (3d Cir. July 28, 2026).

Some courts have said that Sub V status can be revoked involuntarily by the court in 'narrow circumstances.'

No Statutory Power for Revoking a Sub V Election Unless the Debtor Consents

If the Code doesn't authorize the court to "convert" a Subchapter V case to a "regular" chapter 11, what relief can the court give when the debtor is dysfunctional? Is the court limited to dismissing the Subchapter V case, converting to chapter 7 or expanding the powers of the Subchapter V trustee?

That's a question answered by Bankruptcy Judge Michael E. Romero of Denver in a December 15 opinion.

The corporate debtor had elected to proceed as a small business under Subchapter V of chapter 11. Contending that the debtor was mismanaged and the board of directors was deadlocked, several creditors filed a motion asking Judge Romero to revoke the Subchapter V election and appoint a trustee in "regular" chapter 11.

None of the creditors wanted the case dismissed or converted to chapter 7.

The U.S. Trustee objected to the motion, taking the position that the court had no authority for revoking a Subchapter V election.

'Narrow Circumstances' to Revoke a Sub V Election

Judge Romero said he was confronted with "unique circumstances" and addressing "requests [for] equally unusual relief." On the merits, he began by laying out the governing statutes.

Section 1104 permits the court to appoint a trustee in chapter 11, and Section 1106 allows a chapter 11 trustee to file a plan. However, Section 1181(a) makes neither section applicable in Subchapter V.

Judge Romero therefore said that "the Court cannot appoint a Chapter 11 trustee unless and until the Debtor's Subchapter V election is revoked." So, he looked for authority in the Code for revoking the Subchapter V election.

Section 103(i) was of no help, Judge Romero said, because "Subchapter V of Chapter 11 only applies in cases in which the debtor has elected to proceed under it." Quoting Bankruptcy Rule

1020(a), he said that the debtor's election meant that "'[t]he case must proceed in accordance with the debtor's statement, unless and until the court issues an order finding that the statement is incorrect.'"

"Because a debtor makes its Subchapter V election on its petition, no provision in the Bankruptcy Code provides a mechanism for conversion from a regular Chapter 11 to a Subchapter V and *vice versa*," Judge Romero said.

Confronting the same dilemma, Judge Romero said that "few courts have addressed the relief [that the creditor] requests here, that is, whether the Court can use Rule 1009 to compel the Debtor, who is otherwise statutorily eligible to proceed under Subchapter V, to amend its bankruptcy petition to remove the designation so that the Debtor proceeds in a regular Chapter 11 case and a Chapter 11 trustee may be appointed."

Judge Romero identified one bankruptcy court that "has held that an otherwise eligible Subchapter V debtor's designation may be revoked under certain circumstances." The court, he said, "noted that § 105(a) empowered it to revoke the debtor's election when doing so was necessary to carry out other provisions and goals of the Bankruptcy Code."

Judge Romero found other courts that "declined to issue a definite opinion one way or the other, but generally agree that there are a few, narrow circumstances that may warrant the revocation of an otherwise eligible Subchapter V debtor's election."

Synthesizing the sparse caselaw authority, Judge Romero decided that there "are narrow circumstances in which an otherwise eligible Subchapter V debtor's election may be revoked." He then turned "to the question of whether the Debtor's case fits such circumstances."

Of most significance, Judge Romero found that the debtor had not shown itself incapable of proposing a confirmable plan, because the deadline had not elapsed. However, he said he "will likely grant any future motion to revoke the Debtor's designation and appoint a Chapter 11 trustee" if "the Debtor fails to comply with the obligations of Subchapter V, including filing a timely plan."

Expanding the Sub V Trustee's Powers

Judge Romero turned to the question of whether dispossessing the debtor in possession under Section 1185 or expanding the powers of the Subchapter V trustee under Section 1183 would respond to the needs of the case. Neither would suffice, he said, because the "Debtor would still retain the sole power to file a plan."

Judge Romero denied the motion to revoke the Subchapter V election and appoint a chapter 11 trustee without prejudice. Even so, he said that the "Subchapter V Trustee can still aid the Debtor by facilitating the development of a consensual plan without having his powers expanded."

The opinion is *In re USA Cricket*, 25-16318 (Bankr. D. Colo. Dec. 15, 2025).

Sub V committees are appropriate when issues cannot be addressed by expanding the powers of the trustee or removing the debtor in possession.

Judge Isicoff Describes Limited Times When Committees Are Appointed in Subchapter V

Almost writing on a clean slate, Bankruptcy Judge Laurel M. Isicoff of Miami described the limited circumstances under which a court can or should appoint an official creditors' committee in a Subchapter V case.

Basically, there should be an official committee only when problems in the case cannot be addressed by either expanding the powers of the Subchapter V trustee or removing the debtor in possession.

The debtor was an operator of 28 movie theaters in eight states. Other than a $50 million secured claim held by the debtor's parent, the noncontingent liquidated claims amounted to $1.9 million. The debtor was planning on conducting a traditional restructuring by rejecting or renegotiating executory contracts and leases.

One creditor filed a motion for the appointment of an official committee of unsecured creditors. The creditor believed that a committee was needed because there was a question about the debtor's eligibility for Subchapter V, unsecured creditors had no unified voice, and the $50 million claim owing to the parent should be investigated.

The motion for a committee was controlled by Sections 1102(a)(3) and 1181(b). "Unless the court for cause orders otherwise," the former says, "a committee of creditors may not be appointed in a small business case or a case under subchapter V of this chapter." Section 1181(b) provides that Section 1102(a) does not apply in a Subchapter V case "[u]nless the court for cause orders otherwise . . . ."

In short, there is an official committee in Subchapter V only for "cause."

The Paucity of Authority

In her August 28 opinion, Judge Isicoff said that a "benefit" of Subchapter V "is that there is 'no mandatory appointment of a creditors' committee.'" In place of a committee, she said that "Subchapter V provides for the automatic appointment of a Subchapter V trustee, whose mandatory duties include examining proofs of claim, furnishing information to parties in interest, and facilitating the development of a consensual plan."

Although the Bankruptcy Code does not define "cause," Judge Isicoff said that a decision on the motion was committed to her discretion. In terms of precedent, she said "there is very little case law addressing what a court should consider in determining whether there is 'cause' necessary to appoint a creditors' committee."

In terms of applying caselaw by analogy, Judge Isicoff said that authorities on "appointment of additional committees in traditional chapter 11 cases" were "inapplicable . . . and unpersuasive" because "the statutory framework for appointing a committee in a Subchapter V case arises in a different context."

Judge Isicoff cited *dicta* from a decision handed down shortly after the adoption of Subchapter V where a bankruptcy court in California said that appointment of a committee "requires a showing that its 'existence will improve recoveries to creditors, will assist in the prompt resolution of this case, and is necessary to provide effective oversight of the debtors.'"

Following the adoption of Subchapter V, Judge Isicoff found only one case where a committee was appointed. *In re Sharity Ministries Inc.*, Case No. 21-11001 (JTD), Tr. of Aug. 9, 2021 Hr'g. ECF #130 at 61-63 (Bankr. D. Del. Aug. 10, 2021). In *Sharity*, however, the debtor had 10,000 "members." In addition, there was "evidence that the debtor had misled its members, was an insurance company operating without licensure and regulation, and that a substantial amount of the members' contributions were used to pay a third party rather than the members' medical expenses."

In addition to appointing a committee in *Sharity*, the court expanded the powers of the Subchapter V trustee to investigate the debtor's financial affairs.

Guidance from the Trustee's Duties and Removal of a DIP

Having identified no authority except from *Sharity* on the elements of "cause," Judge Isicoff found that "guidance comes from the provisions relating to the expansion of a Subchapter V trustee's duties pursuant to section 1183(b)(2) and the provisions addressing the extreme circumstances of removal of a Subchapter V debtor in possession pursuant to 11 U.S.C. § 1185."

Regarding the appointment of a committee under Section 1102(a)(3), Judge Isicoff quoted the *Collier* treatise:

> The duties of the subchapter V trustee under section 1183(b)(1), together with the trustee's additional duties under section 1183(b)(2) that the court can order for

> cause, will enable the subchapter V trustee to protect the interests of unsecured creditors in most small business debtor cases without the need for a committee.
>
> The provisions authorizing the court to appoint a committee for cause allows the court to take into account all of the relevant facts and circumstances. The court will balance the potential cost of a committee against the need to protect the interests of creditors in the reorganization process, taking into account the enhanced role of the United States trustee or the appointment of a subchapter V trustee.

7 *Collier on Bankruptcy* ¶ 1102.04[1] (Richard Levin & Henry J. Sommer eds., 16th ed.).

In deciding whether to appoint a committee in Subchapter V, Judge Isicoff decided that "a court should take into consideration factors that cannot, or logically should not, be addressed by the remedies provided by section 1183(b)(2) or factors which rise to the level of cause for removal of a debtor in possession under section 1185." She listed seven factors to consider:

> (a) the size and complexity of the case (whether the case is one which more closely resembles a traditional chapter 11 case);
> (b) the number of creditors involved in the case and the nature of their debt;
> (c) the nature of the debtor's assets;
> (d) the nature of the debtor's business and how it is regulated;
> (e) the amount of secured debt, the number of secured creditors, and the nature of the collateral in which such creditors assert a lien;
> (f) whether and to what extent any other creditor or other party in interest supports the relief requested; [and]
> (g) whether there are any other factors present in the case which, notwithstanding section 1183(b)(2), would interfere with the ability of the Subchapter V trustee to perform his or her normal statutory duties effectively.

Applying the factors to the case at hand, Judge Isicoff said it was "not a complex case." Even if the debt was near the cap, she said that factor was "not persuasive." The need for a "unified voice," she said, "is not supported by the number of creditors in these cases or the nature of their debt."

Denying the motion for a committee, Judge Isicoff noted that no other creditor had joined the motion said that the Subchapter V trustee could investigate the parent's secured claim.

The opinion is *In re Cinemex Holdings USA Inc.*, 25-17559 (Bankr. N.D. Fla. Aug. 28, 2025).

Unlike chapters 11 and 13, a chapter 12 plan allows stretching out fully secured claims for more than five years.

On a Split, Kansas Judge Allows Chapter 12 Plan Amendment to Stretch Secured Claims

On a question where bankruptcy courts are divided, Chief Bankruptcy Judge Dale L. Somers of Topeka, Kan., decided that a debtor can modify a confirmed chapter 12 plan calling for payments to a secured creditor extending more than five years after the first plan payment.

If he were to rule that chapter 12 "prohibits modification of payments on secured claims longer than five years after the first payment," Judge Somers said in his February 26 opinion, "a family farmer who pays longer than five years on a secured claim in his original plan could never modify the plan."

Judge Somers explained how his ruling was aligned with the advantages chapter 12 provides for family farmers, compared to difficulties faced by debtors in chapters 11 and 13:

> [T]he ability of a Chapter 12 debtor to pay on the family farm over a period longer than five years is one of the key advantages family farmers enjoy by utilizing Chapter 12 — relief that is unavailable in Chapter 13, which prohibits longer than 5-year payment of arrearages on claims secured by the debtor's primary residence . . . . Chapter 12 also allows debtors to avoid the debt limits of Chapter 13 and the absolute priority rule of Chapter 11 which make those chapters unavailable or highly problematic to family farmers.

The Secured Creditor Stretchout

The bank had liens on basically all of the farmer's real and personal property to secure a debt of about $850,000. The debtor confirmed a chapter 12 plan in 2021 calling for the bank to be paid in full with interest over seven years. The last payment was to be due in 2028.

A drought required the debtor to exit the cattle ranching business. However, the sale of the herd only reduced the bank debt to some $400,000. Without income from ranching, the farmer couldn't make the annual payments of $127,000 owing under the plan as confirmed.

So, the farmer filed a motion to modify the confirmed plan by stretching out payments to the bank for 10 years with interest, with the last payment due in 2035. The bank objected, contending that chapter 12 doesn't permit payments on an amended plan for longer than five years after the first payment.

Deferring other confirmation issues for later consideration, Judge Somers stated the question as:

> [T]he limited legal issue [is] whether § 1229(c) prohibits modification of a confirmed Chapter 12 plan that would extend payments of a secured creditor's claim over a period longer than five years after the time that the first payment under the original confirmed plan was due.

Confounding Statutes

To achieve any of four permissible objectives, Section 1229(a) permits modifications of confirmed plans "[a]t any time after confirmation of the plan but before the completion of payments under such plan . . . ." Subsection (b)(1) then provides that "Sections 1222(a), 1222(b), and 1223(c) of this title and the requirements of section 1225(a) of this title apply to any modification under subsection (a) of this section."

The bank principally relied on Section 1229(c), which provides:

> A plan modified under this section may not provide for payments over a period that expires after three years after the time that the first payment under the original confirmed plan was due, unless the court, for cause, approves a longer period, *but the court may not approve a period that expires after five years after such time*. [Emphasis added.]

But that's not the end of the story. For secured creditors, Sections 1222(c) and (b)(9) allow initial confirmation of a chapter 12 plan with payments exceeding five years. Subsection (c) reads:

> Except as provided in subsections (b)(5) and (b)(9), the plan may not provide for payments over a period that is longer than three years unless the court for cause approves a longer period, but the court may not approve a period that is longer than five years.

Pointing in another direction, Subsection (b)(9) permits a plan to "provide for payment of *allowed secured claims* consistent with section 1225(a)(5) of this title, *over a period exceeding the period permitted under section 1222(c)*." [Emphasis added.]

The opinion by Judge Somers is an explication of the arguments for and against modification of chapter 12 plans extending payments on a fully secured claim beyond five years after the first payment. He identified two bankruptcy courts that prohibited modifications of the sort and one bankruptcy court that allowed them.

The Specific Controls the General

Judge Somers said it was "curious" that "Section 1229(b)(1) includes subsections (a) and (b) of § 1222 but not subsection (c)." He concluded that "that Congress's inclusion of § 1223(c) in § 1229(b)(1) was in error."

"Fortunately," Judge Somers said, "the Court need not rely on its suspicions because explicit inclusion of § 1222(c) in § 1229(b)(1) is not necessary. Section 1222(b) is already subject to § 1222(c)." He added, "[A]ll the provisions of § 1222(a)-(c) apply to § 1229 modifications," meaning that plan amendments may extend beyond five years in light of Section 1222(b)(9).

To buttress his reading of the statute, Judge Somers alluded to *Morton v. Mancari,* 417 U.S. 535, 550-51 (1974), where the Supreme Court held that "a specific statute will not be controlled or nullified by a general one." He therefore concluded that Section 1229(c) "will not control or nullify § 1222(b)(9)" and held "that modifications may provide for payments to secured claimants longer than five years after the first payment in the original plan."

Judge Somers allowed the debtor to proceed to confirmation of the amended plan, finding that stretching out the fully secured claim to 2035 was "consistent with the statutory scheme and underlying policy of Chapter 12."

The opinion is *In re Niemeier*, 19-41158 (Bankr. D. Kan. Feb. 26, 2026).

Modifying the requirement that an acceptance or rejection of a plan must be in writing, an upcoming amendment to Bankruptcy Rule 3018 may permit a judge to take an oral statement in court as acceptance of the plan.

Following the Majority, Judge Gasparini Won't Take a Nonvoting Class as Accepting

Bankruptcy Judge Elisabetta G.M. Gasparini of Columbia, S.C., joined what she called the majority of courts by holding that a nonvoting class in Subchapter V is a class voting against the plan. However, she alluded to an upcoming amendment to Bankruptcy Rule 3018 to mean that a judge might take a statement in court as a vote in favor of the plan.

The corporate debtor in Subchapter V had a plan with four classes of impaired creditors. Creditors in three classes voted in favor of the plan by the required majorities.

The U.S. Small Business Administration was in a class of its own and did not vote, one way or the other. Responding to the objection of the U.S. Trustee to treat the plan as nonconsensual, the debtor importuned Judge Gasparini to confirm the plan as consensual under Section 1191(a). She declined the invitation in her April 24 opinion but confirmed the plan as nonconsensual under Section 1191(b).

The Four Approaches to Nonvoting Classes

Covering the merits, Judge Gasparini listed the benefits from confirming a consensual plan. The advantages include immunity from nondischargeable debt, earlier and broader discharge, and termination of the Subchapter V trustee on confirmation.

To enjoy the benefits of a consensual plan, Judge Gasparini explained that "a subchapter V debtor must satisfy the requirements of § 1129(a)(8) and (a)(10)." The former requires that each class of creditors has "accepted" the plan or is not impaired. Bankruptcy Rule 3018(c)(1) provides that an "acceptance or rejection of a plan must: (A) be in writing . . . ."

Judge Gasparini stated the issue as "whether a subchapter V plan can be consensually confirmed under § 1191(a) when an impaired class of creditors does not vote," because the class with only the Small Business Administration was impaired and had not voted. She said that courts have had four different answers to the question.

Judge Gasparini dealt with the approaches one by one, beginning with what she called the "deemed acceptance" view as exemplified in the Tenth Circuit's 1988 decision in *In re RutiSweetwater, Inc.*, 836 F.2d 1263 (10th Cir. 1988). She said that the Tenth Circuit was the only circuit to have dealt with the issue, but in the context of "regular" chapter 11.

The Denver-based appeals court noted in *RutiSweetwater* that the former Bankruptcy Act said that a failure to vote was deemed a rejection of the plan. Because the provision was omitted on adoption of the Bankruptcy Code, Judge Gasparini described the Tenth Circuit as "conclud[ing] that non-voting classes will be deemed to have accepted the plan."

The second approach, which Judge Gasparini also called "deemed acceptance," only applies when the court has approved solicitation materials informing creditors that silence is the equivalent of acceptance. *See In re AIO US, Inc.*, 24-11836, 2025 WL 2426380, at *31 (Bankr. D. Del. Aug. 21, 2025). To read ABI's report on *AIO*, click here.

Judge Gasparini described the third approach as one where a nonvoting class is simply disregarded. *See In re Franco's Paving LLC*, 654 B.R. 107 (Bankr. S.D. Tex. 2023); and *In re Hot'z Power Wash, Inc.*, 655 B.R. 107 (Bankr. S.D. Tex. 2023). To read ABI's reports on the two Texas cases, click here and here.

The fourth approach, which Judge Gasparini called the "majority view," "requires affirmative acceptance of all impaired classes for a plan to be confirmed as consensual under § 1191(a)." As examples, she cited, among others, *In re M.V.J. Auto World, Inc.*, 661 B.R. 186 (Bankr. S.D. Fla. 2024); and *In re Florist Atlanta*, 24-51980, 2024 Bankr. LEXIS 1842 (Bankr. N.D. Ga. Aug. 6, 2024). To read ABI's reports, click here and here.

Reasons for Following the Majority

Judge Gasparini explained why she found the majority view "both compelling and well-reasoned." She began by distinguishing *RutiSweetwater*, and it was "vastly different than the case before this Court" because the debtor in *RutiSweetwater* had a complex capital structure and a plan with 80 classes of creditors.

Judge Gasparini gave several reasons for holding that the failure of the Small Business Administration to accept the plan "is not equivalent to acceptance of the plan as required by § 1126(c)." She began by citing three bankruptcy courts in the Fourth Circuit for holding that silence was not acceptance.

Judge Gasparini could not reconcile the notion of deemed acceptance with Section 1126(f), which provides that an unimpaired class is "conclusively presumed to have accepted the plan." That section, she said, "is the only provision of the Bankruptcy Code specifying when a creditor is deemed to have accepted a plan without having submitted a ballot."

The case before her, Judge Gasparini said, is "more analogous to that of *M.V.J. Auto World*," where the court "rejected the approach that failure to vote allows the class to be disregarded for purpose of § 1129(a)(8) finding the Bankruptcy Code to be unambiguous."

No Special Rule for the SBA

The debtor wanted Judge Gasparini to ignore the class with the Small Business Administration because the debtor believed that the SBA had a policy of not voting on plans.

Judge Gasparini observed that "neither the Bankruptcy Code nor the Bankruptcy Rules provides a government carve-out to these requirements." Although "sympathetic" to the idea of a special rule, she said that the court "lacks the authority to fashion a remedy that would alter the statutory requirements at issue."

Salvation on the Horizon?

Although "it does not help Debtor in this case," Judge Gasparini said that "the upcoming amendment to Federal Rule of Bankruptcy Procedure 3018, expected to go into effect on December 1, 2026, may provide some relief on this issue."

Currently, Rule 3018(c) requires acceptance or rejection "in writing." The amended rule will read, in pertinent part:

> The court may also permit an acceptance — or the change or withdrawal of a rejection — in a statement that is: i. part of the record, including an oral statement at the confirmation hearing or a stipulation; and ii. made by the creditor or equity security holder — or its attorney or authorized agent.

Judge Gasparini said that "the proposed amendment authorizes a court to additionally treat as an acceptance of a plan a statement on the record by a creditor or the creditor's attorney or authorized agent."

Judge Gasparini denied the debtor's request to confirm the plan as consensual but confirmed the plan as nonconsensual under Section 1192(b).

The opinion is *In re 5 Star Home Care Inc.*, 25-04786 (Bankr. D.S.C. April 24, 2026).

Consumer Bankruptcy

Discharge/Dischargeability

Without a threat or a claim from the IRS, there was no 'injury in fact' allowing a debtor to sue in bankruptcy court for a determination about discharge of a tax debt.

Second Circuit Says Debtor Can't Sue the IRS on Dischargeability of Tax Debts

The Second Circuit held that the bankruptcy court must ignore the reality of later-arising events in deciding whether a plaintiff has standing to initiate an adversary proceeding concerning the nondischargeability of tax debts for having arisen from a willful attempt to evade taxes.

The July 28 Second Circuit decision means that the Internal Revenue Service can decide when and where to sue a debtor over nondischargeable tax debts. If the debtor sues first before there was a threat from the IRS, the Second Circuit says there is no case or controversy and therefore no subject matter jurisdiction in the bankruptcy court.

If the IRS sues first outside of the bankruptcy court to declare a tax debt nondischargeable, the Second Circuit tells us that the first-to-file rule prevents the debtor from attempting to prove dischargeability in the bankruptcy court.

In other words, the relief afforded debtors for the bankruptcy court to determine dischargeability of a tax debt under Section 523(a)(1)(C) is unavailable unless the IRS has made a threat. If the debtor is in fear the IRS will eventually assert nondischargeability, the debtor cannot resolve the question by suing first in bankruptcy court.

Two Suits over the Same Tax Claims

The individual debtor filed a chapter 7 petition owing more than $500,000 in taxes to the Internal Revenue Service. Before discharge, the debtor filed an adversary proceeding against the IRS seeking a declaration that her tax debt was discharged under Section 523(a)(1).

Although not stated in the complaint, the debtor evidently was in fear that the IRS would allege that the tax debt was nondischargeable for having arisen from a "willful" attempt to "evade" taxes under Section 523(a)(1)(C). Two months after filing the complaint, the debtor received her general discharge.

While the debtor's complaint was pending in bankruptcy court, the IRS filed a complaint in federal district court in the same district, aiming to reduce the unpaid taxes to judgment along with a declaration that the taxes were not discharged under Section 523(a)(1)(C).

One month later, the IRS moved in bankruptcy court to dismiss the debtor's adversary proceeding. The IRS contended that the adversary proceeding was undertaken in violation of the Declaratory Judgment Act under 28 U.S.C. § 2201(a) and that there was no case or controversy when the debtor filed her complaint.

Although the complaint may not have been "ripe" on the date it was filed, the bankruptcy court denied the government's motion to dismiss by granting the debtor leave to file an amended complaint mentioning the suit by the IRS in district court to establish the existence of a case or controversy regarding the dischargeability of the debt.

The IRS sought leave from the district court to undertake an interlocutory appeal, but the district court instead authorized a direct appeal to the Second Circuit. The appeals court accepted the direct appeal.

While the appeal was pending in the circuit, the district court stayed the adversary proceeding in bankruptcy court.

The Initial Complaint Didn't Allege Imminent Injury in Fact

Circuit Judge Debra Ann Livingston described the IRS as contending on appeal that the debtor's complaint in bankruptcy court "did not plausibly allege an injury in fact because it provided no facts indicating that the IRS intended to collect on [the debtor's] debts post-discharge." More particularly, she said,

> A debtor's concern that the IRS might someday assert that various debts were excluded from discharge does not suffice, on its own, to create an Article III case or controversy.

To establish standing, Judge Livingston cited the Supreme Court for requiring a showing of an "'injury in fact'" that is "'concrete, particularized, and actual or imminent.'" In other words, the injury may not be "speculative."

Judge Livingston said that the debtor's "initial complaint did not plausibly allege that she faced a substantial risk of harm." Even after discharge, when the automatic stay would expire, she said that the debtor "faced the prospect of personal liability on her debts only if a creditor could successfully argue the debts were nondischargeable."

"Whether [the debtor] faced a substantial risk of harm thus depended on the likelihood that an exception to dischargeability applied," Judge Livingston said. Furthermore, she said that the "complaint 'set forth no specific facts' suggesting that the IRS believed [that the debtor] met either element of § 523(a)(1)(C) or that the IRS otherwise manifested a concrete intention to assert that [the debtor's] debts were nondischargeable." [Citation omitted.]

Absent facts showing "substantial risk," Judge Livingston held that the debtor's "fear" of a later complaint by the IRS under Section 523(a)(1)(C) was "conjectural" and did not establish injury in fact.

Because the debtor's first complaint "did not plausibly allege an injury in fact," Judge Livingston decided that the bankruptcy court lacked jurisdiction.

Contingent Liabilities Don't Always Confer Standing

Judge Livingston dealt with the debtor's counter arguments but found that "none persuades."

Although Section 505(a)(1) enables the bankruptcy court to determine the amount or legality of a tax, Judge Livingston said that the "courts' ability to make such determinations as part of deciding otherwise justiciable cases does not relieve plaintiffs of their burden plausibly to allege the existence of an injury in fact."

Similarly, Judge Livingston said that a "plaintiff must still have Article III standing" even though bankruptcy is an *in rem* proceeding.

Although the Second Circuit has held that a contingent debt is a cognizable legal injury, Judge Livingston said that the appeals court "never suggested . . . that a contingent liability *always* qualifies as an injury in fact." [Emphasis in original.] When there is an allegation of a "future injury," she said there must be "'an imminent threat of injury,'" quoting the Ninth Circuit.

In the case on appeal, Judge Livingston said that the debtor "failed to identify any actual or imminent consequences in her complaint."

The First-to-File Rule

Judge Livingston ended her opinion by deciding that the debtor could not cure the jurisdictional defect to show imminent injury by filing an amended complaint alluding to the lawsuit by the IRS in district court.

Quoting a 2020 decision by the Second Circuit, Judge Livingston said, "[W]e have never squarely addressed whether events occurring after the filing of a complaint may cure a jurisdictional defect that existed at the time of initial filing."

The question, Judge Livingston said, "'has divided our sister circuits,'" again quoting the Second Circuit.

Judge Livingston said that she need not take sides on the split even if the debtor could have cured a jurisdictional defect, because "'the first court to obtain jurisdiction of the parties and of the issues should have priority over a second court to do so.' *AEP Energy Servs. Gas Holding Co. v. Bank of Am., N.A.*, 626 F.3d 699, 722 (2d Cir. 2010)."

Drilling down, Judge Livingston said that the first-to-file rule looks to "'who first brings an issue into a court of *competent jurisdiction*.'" [Emphasis in original.] "'Normally,'" she said, quoting the Second Circuit, "'[s]ound judicial discretion dictates that the second court decline its consideration of the action before it until the prior action before the first court is terminated.'''

Judge Livingston said that the IRS had "the first jurisdictionally proper suit." Even if the debtor could cure the jurisdictional defect, she said that "the bankruptcy court would only obtain jurisdiction over the case at that time and would still be obligated to defer to the district court."

Consequently, Judge Livingston held that "the bankruptcy court should have dismissed [the debtor's] complaint for lack of subject matter jurisdiction rather than authorize the filing of a supplemental complaint." Likewise, she said that Section 524, describing the effect of discharge, "does not grant the bankruptcy court superior jurisdiction over litigation regarding nondischargeable debts."

Judge Livingston vacated the bankruptcy court's order and remanded, because the debtor's original complaint "did not plausibly allege an injury in fact," and "the bankruptcy court should have deferred to the district court as the first court to obtain jurisdiction over the case."

Observations

The Second Circuit held there is no case or controversy permitting a suit by the debtor against the IRS under Section 523(a)(1)(C) until the IRS has made a threat or filed suit seeking a declaration of nondischargeability. When the IRS has sued, the Second Circuit goes on to say that the first-to-file rule effectively bars the debtor from seeking a declaration about dischargeability in bankruptcy court.

The opinion means that the IRS can sue in federal district court and have a similar suit dismissed in bankruptcy court, even when the debtor has sued first in bankruptcy court. To have a case or controversy for suing in bankruptcy court, the Second Circuit opinion means that the debtor's complaint must allege some type of threat from the IRS.

Absent a threat from the IRS, a debtor in fear of an IRS suit under Section 523(a)(1)(C) has no recourse to sue in bankruptcy court and put its anxieties to rest.

A debtor in a similar predicament might ask the district court to refer the IRS suit to the bankruptcy court.

Or, a court might come down contrary to the Second Circuit by exercising discretion and bypassing the first-to-file rule based on Rule 15, which says that leave should be "freely given" to allow amended pleadings.

Thanks

We salute Thomas Moers Mayer and Rachel Blumenfeld, who represented the debtor *pro bono*, and the National Association of Consumer Bankruptcy Attorneys and the National Consumer Bankruptcy Rights Center for submitting an *amicus* brief on behalf of the debtor, prepared by attorneys from Kirkland & Ellis LLP.

The opinion is *I.R.S. v. Goebel (In re Goebel)*, 25-103 (2d Cir. July 28, 2026).

ABI's president, Judge Bruce Harwood, is affirmed by the First Circuit.

Unexplained Loss of Assets Needn't Be Substantial to Mean Loss of Discharge, Circuit Says

To deny an individual's discharge under Section 727(a)(5) for failure "to explain satisfactorily" a loss of assets, the First Circuit held that the missing assets need not be substantial.

Objecting to the debtor's discharge, a secured creditor established at trial that the debtor had not explained the disappearance of almost $57,000 from a total of about $700,000 that the debtor had received from the corporation he controlled in the year before his chapter 7 filing.

After trial, retired Bankruptcy Judge Bruce A. Harwood of Concord, N.H., denied the debtor's discharge under Section 727(a)(5). (Note: Judge Harwood is the 2025-26 president of the American Bankruptcy Institute.)

After the district court affirmed, the debtor appealed to the First Circuit.

Substantial Unexplained Loss Not Required

In her February 27 opinion, Circuit Judge O. Rogeriee Thompson began by quoting Section 727(a)(5), which provides that the debtor will be denied a discharge if "the debtor has failed to explain satisfactorily . . . any loss of assets or deficiency of assets to meet the debtor's liabilities."

Judge Thompson explained how the burden of proof shifts under Section 727(a)(5):

> [T]he party seeking to prevent a discharge must first show that the debtor has not accounted for previously owned assets or income, then, after that showing, the burden shifts to the debtor to satisfactorily explain the deficiency (as in, tell us what happened to the money).

In the case on appeal, Bankruptcy Judge Harwood concluded that the debtor had failed to explain the loss of $57,000 after the burden had shifted to the debtor. Judge Thompson described how the debtor argued in rebuttal that "the statute only permits denial of a discharge when the lost assets at issue are substantial."

Reviewing a legal question *de novo*, Judge Thompson began by noting that the word "substantial" does not appear in the statute. She went on to say that the debtor's reading of the statute "would not only insert a new term (and an elusive new standard for courts to apply) but also render the phrase 'any loss of assets or deficiency' superfluous."

Judge Thompson ruled that Bankruptcy Judge Harwood did not err in interpreting the statute.

A 'Common Sense' Interpretation

Focusing on the subsection's words "to meet the debtor's liabilities," the debtor contended, as Judge Thompson said, "that § 727(a)(5) does not require a debtor to satisfactorily explain unaccounted-for funds if the missing funds wouldn't be enough to pay back the debtor's outstanding liabilities." In other words, the debtor took the position that the missing assets didn't require denial of discharge because the missing assets wouldn't have been enough to pay claims in full.

In response, Judge Thompson said that the debtor's statutory "interpretation rapidly falls apart in the context of the statute, caselaw, and common sense."

The words "to meet the debtor's liabilities," Judge Thompson said, mean that that debtor has no "obligation to explain lost assets that otherwise did not belong to the bankruptcy estate and would not have been available to pay creditors." The words, she said, "merely [refer] to the class of assets available to meet a debtor's liabilities." She therefore concluded that the statute itself is contrary to the debtor's notion that the missing assets must be sufficient to pay claims in full before discharge is denied.

As for caselaw, Judge Thompson found "no support in the caselaw."

"And third," Judge Thompson said, "we hasten to add that the [the debtor's] interpretation of § 727(a)(5) contravenes common sense." She explained,

> Taken to its extreme, under the [the debtor's] requested interpretation, a debtor with $1,000,000 in outstanding liabilities would not need to satisfactorily explain a $999,999 deficiency because that total unaccounted-for money would be insufficient to meet the debtor's liabilities.

Discerning "no legal error in the bankruptcy court's interpretation of § 727(a)(5)," Judge Thompson found no error in Bankruptcy Judge Harwood's findings of fact. She affirmed the denial of discharge.

The opinion is *Savage v. Coastal Capital LLC (In re Savage)*, 25-1249 (1st Cir. Feb. 27, 2026).

The Ninth Circuit gives state legislatures the ability to decide whether costs of attorneys' disciplinary proceedings are dischargeable, or not.

Disciplinary Costs Are Nondischargeable in California But Dischargeable in Nevada

Affirming the Bankruptcy Appellate Panel, the Ninth Circuit explained why the costs of an attorney's disciplinary proceeding *are not dischargeable* in California. Paradoxically, similar costs from disciplinary proceedings *are dischargeable* in Nevada.

The circuit's July 31 opinion explains how state legislatures could draft attorney disciplinary legislation so costs will be excepted from discharge under Section 523(a)(7). In other words, the Ninth Circuit's decisions allows state legislatures to skirt the language in Section 523(a)(7), which provides that a debt is not discharged if it is "compensation for actual pecuniary loss. . . ."

Suspensions

An attorney in Nevada was twice disciplined for mishandling client funds. Ultimately, the Nevada Supreme Court suspended the lawyer and directed him to pay more than $21,000 in fees and costs arising from the disciplinary proceedings.

Ten days after the suspension ended, the lawyer filed a chapter 7 petition, listing $25,000 owing to the Nevada Bar Association as a nonpriority unsecured debt. The state bar did not participate in the proceedings. The lawyer received a general discharge.

While the bankruptcy was pending, the lawyer applied for reinstatement. Eventually, the Nevada Supreme Court decided that the lawyer could be provisionally reinstated on the condition that he pay the disciplinary costs. The state high court reasoned that the costs were part of disciplinary proceedings to protect the public and deter misconduct.

A year later, the lawyer reopened his chapter 7 case and moved for sanctions against the bar. The lawyer reasoned that the bar was discriminating against him in violation of Section 525(a), which provides that "a governmental unit may not deny . . . a license . . . to . . . a person that is or has been a debtor under this title. . . , solely because such bankrupt or debtor is or has been a debtor under this title. . . ."

The bankruptcy court denied the motion for sanctions and held that the disciplinary costs were not discharged. The debtor appealed to the Ninth Circuit Bankruptcy Appellate Panel, which reversed and remanded. *Wike v. State Bar of Nevada (In re Wike)*, 660 B.R. 683 (B.A.P. 9th Cir. July 3, 2024). To read ABI's report, click here.

The bar appealed to the Circuit but lost again in an opinion by Circuit Judge M. Margaret McKeown.

Jurisdiction

Judge McKeown first decided that the *Rooker-Feldman* doctrine did not deprive the appeals court of subject matter jurisdiction. Named for two Supreme Court cases, the doctrine applies when someone calls on federal jurisdiction to appeal a state court judgment. *Rooker-Feldman* is based on the constitutional principle that only the Supreme Court has jurisdiction to review state court judgments.

For Judge McKeown, the inapplicability of *Rooker-Feldman* was evident under Ninth Circuit precedent, *Gruntz v. County of Los Angeles (In re Gruntz)*, 202 F.3d 1074 (9th Cir. 2000). There, the Ninth Circuit held *en banc* that a state court judgment modifying the automatic stay is not binding on federal courts. The appeals court reasoned that "Congress has expressed its intent that bankruptcy matters be handled exclusively in a federal forum." *Id*. at 1077-78.

Judge McKeown held that *Rooker-Feldman* did not deprive the court of appellate jurisdiction, explaining,

> Therefore, the Nevada Supreme Court's order conditionally reinstating [the debtor] to the Bar is not preclusive under *Rooker Feldman*, because otherwise it "would constitute an unauthorized infringement upon the bankruptcy court's jurisdiction." *Gruntz*, 202 F.3d at 1082.

The Evolution of Disciplinary Nondischargeability in the Ninth Circuit

On *de novo* review of the merits regarding dischargeability of disciplinary costs, Judge McKeown turned to Section 523(a)(7), which provides that a debt is not discharged if it is "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss. . . ." She said that the dispositive question was "whether the fees and costs [that the debtor] owes to the Nevada State Bar comprise 'a fine, penalty, or forfeiture' and not 'compensation for actual pecuniary loss.'"

Judge McKeown traced the history of Ninth Circuit authority on Section 523(a)(7) primarily dealing with California law, beginning in 2001 with *State Bar of Cal. v. Taggart (In re Taggart)*, 249 F.3d 987 (9th Cir. 2001). There, the appeals court held that disciplinary costs were discharged. Reading the California statute, the circuit concluded that costs were not fines or penalties but were compensation for actual pecuniary costs.

Responding to *Taggart* two years later, the California legislature amended the California Business and Professions Code by adding Section 6086.10(e). The amendment says that disciplinary costs are "penalties . . . to promote rehabilitation and protect the public." The amendment was a "gamechanger," Judge McKeown said.

In 2010, the next case on point was *State Bar of Cal. v. Findley (In re Findley)*, 593 F.3d 1048 (9th Cir. 2010), where the Ninth Circuit held that California disciplinary costs had become nondischargeable, because the amendment classified costs as "penalties."

Judge McKeown distinguished other Ninth Circuit authorities holding monetary impositions in connection with disciplinary proceedings by concluding that they were discharged because they were not penalties but were for recovery of pecuniary losses.

Nevada Isn't California

Applying Ninth Circuit precedent, Judge McKeown pointed out the differences between California law and Nevada law, because the case on appeal came from Nevada. She noted that fees and costs under Nevada Supreme Court Rules "do not constitute fines or penalties under § 523(a)(7)" because the Nevada rules do "not sufficiently" establish that the payments serve penal and rehabilitative costs and do not qualify as fines.

Judge McKeown held "that the fees and costs assessed against [the debtor] under [Nevada's] Rule 120 are not exempt from discharge." She remanded "with instructions for the bankruptcy court to grant [the debtor's] motion for sanctions against the State Bar of Nevada."

The opinion is *Wike v. State Bar of Nevada (In re Wike)*, 24-4402 (9th Cir. July 31, 2025).

Automatic Stay+

Even if the nondebtor were not a creditor, the Fifth Circuit said the nondebtor would be eligible for stay violation damages under Section 362(k)(1).

Fifth Circuit Gives a *Nondebtor* $104,000 in Damages for a Stay Violation

The Fifth Circuit affirmed the right of a *nondebtor* to sue and recover about $104,000 in damages for violation of the automatic stay.

In her July 16 opinion, Circuit Judge Jennifer Walker Elrod attributed the stay violation to a continuation of an arbitration against the nondebtor on a claim based on breach of fiduciary duty that belonged to the estate of the chapter 7 corporate debtor.

The nondebtor in question was a founder of a financial technology startup that ended up in chapter 7. Before its bankruptcy, the corporation initiated an arbitration against investors. The investors filed counterclaims against the debtor and the founder.

When the corporation filed a chapter 7 petition, the investors ceased prosecution of the arbitration against the debtor, but they continued the arbitration against the founder. Three times after the bankruptcy filing, the founder failed to appear for a deposition in the arbitration. Before the fourth arbitration ordered by the arbitrator, the founder moved in bankruptcy court to enforce the automatic stay.

Bankruptcy Judge Michelle V. Larson of Dallas found a willful violation of the automatic stay and awarded the founder about $104,000 in actual damages. The investors appealed, but the district court affirmed, leading to a second appeal to the Fifth Circuit.

Standing

The founder was a creditor, but the investors contended that he had no standing to sue for violation of the automatic stay because his status as a creditor was not the cause of his damages.

Under Fifth Circuit authority, Judge Elrod said that a creditor can sue for violation of the automatic stay. Because the founder was a creditor, she said that "he can enforce the automatic stay" by "simple transitive property."

The investors contested Judge Elrod's "simple logic" by saying that the claims they were pursuing "did not affect the rights of the creditors."

Judge Elrod took exception to the argument, saying that "at least one of the claims [breach of fiduciary duty] belongs to the estate and therefore has a direct impact on creditors' recovery."

Even if the founder were not a creditor, Judge Elrod said that he "falls within the plain language of the statute," because Section 362(k)(1) provides that "an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages."

Because the founder "expended substantial resource[s] dealing with the willful violation," Judge Elrod held that he had standing and the right "to recover damages."

Willful Stay Violation

In the Fifth Circuit, Judge Elrod said there is a willful stay violation when the defendant knew about the stay, and their actions were willful and violated the stay. She said that the only dispute was whether continuation of the arbitration against the founder violated the stay.

Judge Elrod held that the breach of fiduciary duty claims against the founder "are subject to the automatic stay." Why? Because the claims were property of the estate, and Section 362(a)(3) enjoins "any act to obtain possession of property of the estate or . . . to exercise control over property of the estate."

Judge Elrod therefore affirmed the bankruptcy judge's decision to award damages.

Damages

Regarding damages, Judge Elrod began by saying that attorneys' fees "are available under Section 362(k), including fees incurred in enforcing the automatic stay." She reviewed the quantum of damages for abuse of discretion.

Judge Elrod noted how the bankruptcy judge reviewed time records "line by line," using typical fee allowance standards searching for unrelated work and duplicative staffing. Concluding that the investors "have not pointed to anything suggesting that the bankruptcy court clearly erred in its incorporation of their suggestions, beyond their continued dissatisfaction with the fee award," she affirmed Bankruptcy Judge Larson's award of some $104,000 in damages.

The opinion is *Ayres v. Neugebauer (In re With Purpose Inc.)*, 25-10572 (5th Cir. July 16, 2026).

A creditor may not avoid contempt by violating an injunction and later claiming the injunction was invalid.

Knowing About a Discharge Order Is Enough for Contempt, Third Circuit Says

Declining to read *Taggart* expansively, the Third Circuit held that a creditor's knowledge of confirmation and discharge orders was enough to hold the creditor in contempt of the discharge injunction, even though the creditor had not been served with the debtor's chapter 13 plan.

The appeal concerned the 22-year history of the debtor's chapter 13 case and its aftermath. We won't even attempt to summarize the gruesomely complex facts.

The pertinent facts pretty much boil down to this: The creditor was a municipality with tax liens on the debtor's two parcels of real estate. (Actually, there were three parcels of real estate, but we're only dealing with two of them.) Eventually, the bankruptcy court confirmed the debtor's chapter 13 plan, under which the municipality's claims had bifurcated into secured and unsecured claims.

The debtor had served its bifurcation motion on the municipality. The motion was granted when the municipality did not respond or oppose bifurcation. However, the *pro se* debtor had not served the plan on the municipality.

Circuit Judge Emil J. Bove said in his June 9 opinion for the Third Circuit that the docket showed mailings of 11 other notices about the bankruptcy to the municipality. The notices included the debtor's bifurcation motion, claims that the debtor filed regarding the municipality's liens, the confirmation hearing, the confirmation order and the discharge order.

Years after discharge, the debtor moved to hold the municipality in contempt for attempting to enforce the lien against one of the real properties. Ruling *sua sponte* on an issue that neither party raised, the bankruptcy court said there was no contempt because failure to serve the plan on the municipality was a denial of due process.

Still later, the debtor moved to hold the municipality in contempt for attempting to enforce a lien on another real property. Although conceding it had general notice of the bankruptcy, the municipality contended there was no contempt because it reasonably relied on the bankruptcy court's prior *sua sponte* ruling about the lack of due process regarding a different parcel.

Affirmance in district court brought the appeal to the Third Circuit.

The Requisites of a Contempt Finding

In the first page after stating the facts, Judge Bove said that the bankruptcy court's "narrow alternative constitutional ruling . . . was wrong." Two paragraphs later, he said, "Discharge orders are too important to the modern bankruptcy process to be casually ignored by creditors."

Next, he laid out what are now the four requisites for contempt of bankruptcy orders: (1) the existence of a valid order; (2) the creditor's knowledge of the order; and (3) the creditor's disobeyance of the order.

Taggart added a fourth element necessary for contempt. *Taggart v. Lorenzen*, 587 U.S. 554 (2019). Judge Bove described *Taggart* as requiring "the debtor to demonstrate that there was 'no fair ground of doubt as to whether the order barred the creditor's conduct.' *Taggart*, 587 U.S. at 557." He went on to say that the "standard is 'generally an objective one'" and that "[s]ubjective good faith is of exceedingly limited relevance." To read ABI's report on *Taggart*, click here.

Judge Bove held that the creditor satisfied the first two tests because the "discharge order was a 'valid order' that applied to the City, and the City 'had knowledge of the [discharge] order.'" He proceeded to explain why there could be contempt even in circumstances when the injunction was not valid.

Citing Third Circuit precedent, Judge Bove said, "[W]e have essentially forbidden a litigant from violating a final injunction and then challenging the injunction's validity in the resulting contempt proceedings." Referring to the bankruptcy court's finding of a due process violation, he said, "'strong policy reasons' support the general prohibition on collateral attacks as a defense to civil contempt."

Rather than violate an injunction and later raise a defense based on a constitution violation, Judge Bove required "the party subject to the injunction to bring a legal challenge before intentionally violating the final order." Given the municipality's "actual notice of the confirmation and the discharge," he held that "the City was foreclosed from collaterally attacking the final § 524(a) injunction in [the debtor's] contempt proceedings."

No Due Process Violation

Next, Judge Bove decided that the municipality didn't have a valid constitutional objection conferring absolution from contempt. He held that "the City's actual notice [of the bankruptcy meant that] the City's constitutional challenge to the discharge order was also meritless. *See United States Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 272 (2010)."

Why was there no valid constitutional challenge when the bankruptcy court had decided that failure to mail the plan to the municipality was a denial of due process? Judge Bove said "that the City received all of the notice that any 'person' was due under the Constitution." In terms of notice, he listed 11 filings sent to the city, including the confirmation and discharge orders.

In the contempt proceedings, Judge Bove said that the "operative document" was "the discharge order rather than earlier filings in the bankruptcy." Having been given notice of the confirmation hearing, he said that the municipality should have taken steps to learn what was in the plan.

Judge Bove held that there was no due process violation because the municipality had "general notice of the bankruptcy," had "selectively" participated in proceedings and had notice of the confirmation and discharge orders.

Taggart

The "closest question," Judge Bove said, was the municipality's claim of absolution under *Taggart*. Among other things, he said that the municipality's reliance on the bankruptcy court's constitutional ruling "is, at most, suggestive of subjective good faith," but that "mindset is of no help to the City right now."

What matters in the appeal, Judge Bove said, "is that good faith alone is not a meritorious response to [the debtor's] showing on the contempt elements. The City's violation of the discharge resulted from a conscious choice that was 'not technical or inadvertent.'" He therefore held that the debtor "met his burden of establishing contempt."

Regarding contempt, Judge Bove reversed and remanded "to the District Court with instructions to remand to the Bankruptcy Court for purposes of determining the scope of the violation and calculating damages after developing an evidentiary record consistent with the concerns raised in this opinion."

Observation

Judge Bove did not cite *Margolin v. National Association of Immigration Judges*, 25-767, 2026 BL 191548, 2026 WL 1463466 (Sup. Ct. May 26, 2026), where the Supreme Court held last month that the Fourth Circuit violated the "party presentation principle" by reversing and remanding "based on an issue the parties had not raised." To the same effect as *Margolin*, Judge Bove seemed critical of the bankruptcy court for having found a constitutional violation *sua sponte*. To read ABI's report on *Margolin*, click here.

Acknowledgment

On appeal, the debtor was proceeding *pro se*. Before oral argument, the Third Circuit entered an order finding "that further briefing is required to assist the Court with the issues presented in this appeal." The court proceeded to appoint Claire R. Cahill of Williams & Connolly LLP in Washington D.C. as *amicus* counsel for the court.

Ms. Cahill argued and submitted an *amicus* brief along with Charles L. McCloud and R. Shane Roberts, Jr., raising issues featured in Judge Bove's opinion. Ms. Cahill had clerked on the Eleventh Circuit and for Circuit Judge Thomas Ambro on the Third Circuit. She recently completed a clerkship on the Supreme Court for Justice Brett Kavanaugh. Mr. McCloud had clerked on the Fourth and D.C. Circuits and for Justice Sonia Sotomayor on the Supreme Court. Mr. Roberts also recently clerked on the Third Circuit.

The opinion is *Thomas v. City of Philadelphia (In re Thomas)*, 24-1861 (3d Cir. June 9, 2026).

A county was hit with $44,000 in sanctions for 13 instances of willful discharge violations.

After *Taggart*, an Erroneous Decision by an 'ALJ' Is No Defense to a Discharge Violation

Even after *Taggart v. Lorenzen*, a county's reliance on a state administrative law judge's erroneous decision that a debt was not discharged didn't insulate the county from sanctions for 13 instances of "continuing and persistent contumacy" for violating the discharge injunction.

Saying in his May 28 opinion that the county "continues to run amok in a manner that smacks of Franz Kafka," Judge Christopher M. Klein of Sacramento, Calif., imposed $39,000 in sanctions on the county ($3,000 for each of the 13 violations), plus $5,000 for the debtors' emotional distress damages. He said the county was "fortunate" that the debtor had not engaged counsel for the discharge violation, because "the likely compensable professional fees would have exceeded $20,000."

The Erroneous ALJ Decision

A couple had two adult children in their home who were more than 18 years of age. Before the parents' bankruptcy, the county in California determined that the couple and their children were jointly and severally liable for about $3,200 in overpayments of food benefits. The county had decided that the overpayment was the result of "Inadvertent Household Error."

The parents filed a joint chapter 7 petition and received discharges in early 2022, after the trustee determined it was a "no asset" case. Because there were no assets, creditors were not required to file proofs of claim.

Originally, the parents did not schedule the county's claim. About a year later, after the county attempted to collect the debt, the couple reopened their chapter 7 case and amended the schedules to list the county's claim. At the time, the couple told the county that they had received a bankruptcy discharge.

Later still, the county intercepted a tax refund owing to one of the adult children. The couple protested before an administrative law judge, or ALJ. In the protest, the debtors showed the ALJ their two-page bankruptcy discharge order, among other papers.

Although the ALJ also had been shown the amended schedule listing the debt to the county, the ALJ decided that the debt to the county had not been discharged because the discharge order did not list the county as a creditor with a discharged debt.

Thereafter, the county began collection activities against the parents whose debts had been discharged. The debtors moved for sanctions in the reopened bankruptcy case.

The Ninth Circuit's *Beezley* Decision

For Judge Klein, the first order of business was to decide whether the debt to the county had in fact been discharged and whether the failure to schedule the claim at the outset made any difference. He found answers to most of his questions in the Ninth Circuit's decision in *Beezley v. California Land Title Co. (In re Beezley)*, 994 F.2d 1433 (9th Cir. 1993).

Beezley, Judge Klein said, is "settled law" for the principle "that a discharge in a so-called 'no asset, no bar date' case is good against the World, including otherwise dischargeable debts that are merely omitted from schedules. 11 U.S.C. § 523(a)(3)(A)." *Id*. at 1422.

Why is that so? Judge Klein explained,

> The rationale for that application of the omitted creditor provision of § 523(a)(3)(A) is that if no claims bar date has been set, then after the case is closed it nevertheless remains timely for a creditor to file a proof of claim that will enable participation in any distributable assets that may surface in the future.

Id. at 1435 – 37.

What was the significance, if any, of the debtors' amendment of their schedules after discharge to list the county's debt? Judge Klein explained,

> Although the Debtors amended their schedules to include the [county] after the case was reopened, *Beezley* teaches that an after-the-fact scheduling of an omitted debt is 'useless,' *i.e.*[,] of no legal consequence with respect to whether the debt is discharged.

With regard to the discharge injunction, Judge Klein said that the husband gave the county notice of the bankruptcy after amending the schedules. The county claimed it wasn't good enough and said it could still pursue the debtors for a nondischargeable debt arising from fraud. Judge Klein responded, saying, "[I]t is unclear whether the County could meet Rule 9011 fraud pleading standards for what has been determined to reflect 'Inadvertent Household Error.'"

With regard to whether the county should have known that the originally unscheduled debt was discharged, Judge Klein said,

> *Beezley* is a widely-known, oft-cited Ninth Circuit precedent (100s of Westlaw case citations) that could not have escaped the notice of any competent lawyer interested in the question of discharge of omitted debts.

Having been notified of the bankruptcy discharge, the county was "on inquiry notice," Judge Klein said, "to ascertain the status and effect of the discharge."

Taggart

Next, Judge Klein analyzed whether *Taggart v. Lorenzen*, 587 U.S. 554 (2019), gave the county a defense regarding contempt of the discharge injunction. To read ABI's report on *Taggart*, click here.

Judge Klein summarized *Taggart's* holding as follows:

> [T]he Court announced a "no fair ground of doubt" civil contempt standard for when sanctions may be appropriate when a creditor violates a discharge order based on an objectively unreasonable view of the discharge order or the statutes that govern its scope.

Id. at 561-62.

The county's "persistent" discharge violations "justifies placing the burden on the County to demonstrate that its conduct was not objectively unreasonable," Judge Klein said.

Before deciding whether the county had violated the parents' discharge, Judge Klein found that the debts owing to the county by the two adult children were not discharged as a consequence of Section 524(e).

Objective Good Faith

Arguably, the county was acting in subjective good faith by relying on the decision of the ALJ. After *Taggart*, Judge Klein said that the county "cannot be insulated by subjective good faith" when it comes to the debtor-parents' claim for discharge violations. *Id*. at 557-65.

On the issue of objective good faith, the county claimed through layers of hearsay that the debtor's own lawyer had told the county that the debt had not been discharged. Judge Klein was incredulous. He dismissed the idea, saying,

> It is exceedingly unlikely that a debtor's attorney confronted with an omitted garden-variety debt in a "no asset, no bar date" case would admit that the debt was not discharged. This Court's experience of the subject attorney is that he is not manifestly incompetent.

Relevant to sanctions, Judge Klein noted that the debtors' effort to obtain administrative relief for the interception of their son's tax refunds prompted the county "to counter-attack [the debtor-parents] and to contend they were not protected by their chapter 7 discharge. That direct assault on the discharge was egregious civil contempt."

The county contended that having been given the discharge order was not good enough because the ALJ had ruled that the county was not given a discharge order listing the discharge of the county's debt.

As a matter of law, Judge Klein rejected the idea on several grounds. He said that the county had a duty to consult the docket of the bankruptcy court and that it was "not acceptable for County bureaucrats to rope-a-dope a debtor by claiming the debtor has not proved the existence of the discharge to the satisfaction of the County bureaucrats." He added,

> No chapter 7 discharge order issued by a Bankruptcy Court ever contains the name of a creditor. No County bureaucrat can impose an additional requirement on the Bankruptcy Court.

The county's position, Judge Klein said, was "preposterous" and the ALJ's findings of fact were clearly erroneous.

Sanctions

For 13 reasons, or "strikes," as he called them, Judge Klein went on to rule that there was "no objectively reasonable basis for concluding that the County's conduct might be lawful." For each of the 13, he decided that the "amount necessary to coerce the County into compliance with the bankruptcy discharge is $39,000 ($3,000 per strike)." Finding "that this prolonged and frustrating dispute has caused considerable emotional distress to" the debtors, he awarded $5,000 for emotional distress damages.

Judge Klein noted that "*Taggart* had nothing negative to say about the *Taggart* bankruptcy court's awards of emotional distress damages and punitive damages." He cited *PHH Mortgage Corp. v. Valdellon*, 25-538, 2026 BL 198936, 2026 Westlaw 1068902 (9th Cir. April 20, 2026), where the Ninth Circuit held in April that a claim for intentional infliction of emotional distress from a violation of the discharge injunction survived the Supreme Court's *Taggart* decision. To read ABI's report on *Valdellon*, click here.

Judge Klein ended his opinion with a warning. If the county were to take an appeal and if the debtors engage counsel, "a fee award for a successful appellate defense also would be available."

The opinion is *In re Graves*, 21-23788 (Bankr. E.D. Cal. May 28, 2026).

The inability to modify a Section 524(a) discharge put the Ninth Circuit BAP in a bind.

A Promise Not to Enforce a Judgment Meant There Was No Discharge Violation

The Ninth Circuit Bankruptcy Appellate Panel painted itself into a corner in 2002 when it held that a bankruptcy court has no discretion to modify a discharge injunction under Section 524(a).

To avoid perceived injustice, two judges on a Ninth Circuit BAP panel decided there was no discharge violation when a plaintiff was suing the debtor on a wrongful death claim but said it would not attempt to collect a judgment from the debtor. To preserve joint and several liability against nondebtors, the plaintiff could not and did not sign any legally enforceable document waiving enforcement against the debtor.

The BAP's June 13 opinion is the result of an unfortunate coincidence between bankruptcy law and Washington State tort law.

The Wrongful Death Action

Through alleged negligence in driving an automobile, the debtor caused a death. Two years after the accident, the debtor filed a chapter 7 petition and received a discharge three months later, there being no assets.

The debtor listed the decedent as a creditor at his former address, but the debtor did not schedule the decedent's personal representative as a creditor. Claiming she was unaware of the bankruptcy, the personal representative sued the debtor and nondebtor third parties in state court three months after discharge.

The debtor's insurance carrier tendered the policy limit of $50,000 in settlement, but the personal representative-plaintiff declined the offer and continued the suit.

After learning of the bankruptcy, the plaintiff believed she was constrained by state law to continue the suit against the debtor personally. As the plaintiff and the BAP read state law, the debtor needed a judgment against the debtor personally to win a joint and several judgment against the debtor and the nondebtor defendants. Had the plaintiff signed a legally enforceable document agreeing to collect nothing from a judgment against the debtor, the possibility of joint and several liability against the other defendants would be lost under the peculiarities of state tort law.

Truncating the procedural history, here's what happened.

The debtor brought an action in bankruptcy court and a motion for summary judgment to enforce discharge.

The plaintiff did not contend in bankruptcy court that the wrongful death suit was not discharged. However, the plaintiff cross moved for summary judgment, contending that the discharge injunction did not preclude her from obtaining a judgment against the debtor as a vehicle for the nondebtors' joint and several liability.

The bankruptcy court granted summary judgment in favor of the debtor, believing that the debtor's discharge barred the plaintiff from pursuing the lawsuit in state court against the debtor and the nondebtor defendants. The plaintiff appealed to the BAP.

A Promise Was Enough

All would have been well if the bankruptcy court could have modified the discharge injunction to allow the suit to continue nominally against the debtor, but Ninth Circuit BAP precedent said otherwise. In his June 13 opinion for the majority, Bankruptcy Judge Gary Spraker cited *Ruvacalba v. Munoz (In re Munoz)*, 287 B.R. 546 (B.A.P. 9th Cir. 2002)., for the principle that "that bankruptcy courts cannot modify the statutory discharge injunction imposed by § 524(a)(2)."

However, Judge Spraker went on to say that "our precedent also establishes that not every post-discharge action against a debtor violates this injunction." He identified a "nuance" based on the idea that "§ 524(e)'s directive that a debtor's discharge does not impact the liability of third parties even if it is premised on a debt that has been discharged as to the debtor."

Judge Spraker explained that "§ 524(a) does not eliminate the debtor's discharged debt as if it never existed; it only enjoins creditors' efforts to recover that debt from the debtor personally." He said that the "question under § 524(a) therefore becomes not simply whether the creditor seeks a judgment against the discharged debtor, but whether she seeks that judgment as part of an effort to recover against the debtor personally."

Sections 524(a)(1) and (2), Judge Spraker said, only preclude seeking a judgment "as part of an effort to recover against the debtor personally." The plaintiff took the position that she was not violating the discharge because she would not seek to recover from the debtor.

Although *Munoz* precluded the bankruptcy court from modifying the discharge injunction to permit joining the debtor as a nominal defendant, Judge Spraker said that *Munoz* opened the door for the idea that a lawsuit against a debtor does not always violate the discharge injunction.

Judge Spraker said that the lawsuit in *Munoz* "did not violate the discharge injunction because the creditors did not seek to collect or recover the resulting judgment from the discharged debtor." *Id*. at 554-55. He explained what *Munoz* means:

> *Munoz* shows that § 524(a)(2) does not enjoin every action against a discharged debtor. Nor does § 524(a)(1) void a judgment against a discharged debtor to the extent that it is not directed at collecting that debt personally from the debtor.

Applying the *Munoz* principles to the case on appeal, "Section 524(a) simply does not enjoin a post-discharge action or void a resulting judgment against a debtor used as a pass-through to impose liability on nondebtors."

Finding "no meaningful difference between" *Munoz* and the case on appeal, Judge Spraker reversed the bankruptcy court and remanded for the entry of summary judgment in favor of the wrongful death plaintiff.

The Dissent

Bankruptcy Judge H. Gan dissented. He said that the plaintiff "has not filed a binding covenant not to enforce the judgment against Debtor, and she cannot do so if she intends to establish joint and several liability," given the peculiarities of Washington State tort law.

Judge Gan believes that the plaintiff's "lawsuit is clearly enjoined by § 524(a)," because the plaintiff "requires a personal judgment against Debtor, and she cannot effectively release Debtor from that personal liability." He was unwilling "to take [the plaintiff] at her word that she will not seek to enforce the judgment against Debtor."

Judge Gan said he would have affirmed, believing that "the bankruptcy court correctly held the lawsuit violates the discharge injunction."

Observation

The difference between the majority and the dissent boils down to this: The majority would accepted the plaintiff's promise that she would not enforce a judgment against the debtor personally, while the dissenter needed an iron-clad, legally enforceable concession that would have barred the plaintiff from enforcing a judgment for joint and several liability.

In this particular case, the plaintiff would be certifiably stupid if she were to attempt to enforce a judgment against the debtor. To avoid manifest injustice, was the majority justified in taking the plaintiff at her word?

The opinion is *Porcel v. Blackwell (In re Blackwell)*, 24-1087 (B.A.P. 9th Cir. June 13, 2025).

Jurisdiction

Sixth Circuit shows why Bullard didn't leave a chapter 13 debtor unable to appeal denial of confirmation of a plan.

Appealing Confirmation of a Chapter 13 Plan Isn't Equitably Moot, Fourth Circuit Says

In *Bullard v. Blue Hills Bank*, 575 U.S. 496 (2015), the Supreme Court held that denial of confirmation of a chapter 13 plan is not a final, appealable order.

After *Bullard*, one assumed that an aggrieved chapter 13 debtor could appeal denial of confirmation in one of three ways:

> (1) The debtor could allow the court to dismiss the case and argue on appeal that denial of confirmation was in error. Debtors are unlikely to take the dismissal route for loss of the automatic stay.
>
> (2) The debtor could seek leave to pursue an interlocutory appeal under 28 U.S.C. § 158(a)(3), but interlocutory appeals are seldom allowed.
>
> (3) Most likely, a debtor would confirm a dislikable plan and appeal the confirmed plan, hoping the district court would decide that the bankruptcy court shouldn't have denied confirmation of the prior plan.

A district judge in Virginia blocked the third alternative, the route to appeal that most debtors would take. The district court held that equitable mootness barred a chapter 13 debtor from appealing a confirmed plan.

The debtor appealed. The Fourth Circuit reversed in an April 13 opinion by Circuit Judge Nicole G. Berner, who held that "equitable mootness is reserved for complex cases where relief would be impractical, inequitable, or both. It is not appropriately applied in simple, small dollar cases such as this one."

A Simple Plan

Filing a chapter 13 petition with $330,000 in debt, the debtor's first plan called for payment of $200 a month, for a total of $7,200 over the life of a three-year plan. The bankruptcy court denied confirmation, finding that the plan had been filed in bad faith.

After filing second and third plans that also failed, the debtor submitted a fourth-amended plan paying $625 a month, for a total of $20,550. The debtor objected to his fourth plan, but the bankruptcy court confirmed the plan.

The debtor appealed, but the district court dismissed the appeal under the doctrine of equitable mootness, never reaching the merits.

The debtor appealed to the circuit and won a battle, but lost the war. Judge Berner decided that the confirmation order was not equitably moot, but she affirmed confirmation of the fourth plan on the merits.

What's Equitable Mootness

Judge Berner began her opinion with an exegesis on what equitable mootness is and isn't.

First, Judge Berner said that equitable mootness is "a doctrine applied only in the context of bankruptcy." Unlike Article III mootness, which is jurisdictional, she said that equitable mootness is a "discretionary" or "pragmatic doctrine." Quoting the Ninth Circuit, she said it allows a court to "dismiss an appeal when 'changes to the status quo following the order being appealed make it impractical or inequitable to unscramble the eggs.'"

For Judge Berner, the "key inquiry" is "whether the requested relief is available as a practical matter."

Standard of Review

Judge Berner said that the Fourth Circuit has not decided whether appellate review of equitable mootness is *de novo* or for abuse of discretion. She observed that the Sixth, Fifth, Ninth and Eleventh Circuits conduct *de novo* review, while Third Circuit review is for abuse of discretion.

Judge Berner saw no reason to take sides on the split because she would reverse by "applying either standard."

The Four or Five Tests for Equitable Mootness

"Practicality lies at the core of the equitable mootness doctrine," Judge Berner said. Under the circuit's leading authority, *Mac Panel Co. v. Va. Panel Corp.*, 283 F.3d 622 (4th Cir. 2002), courts consider four factors.

Judge Berner said that the "central inquiry" under *Mac Panel* is whether "'effective relief' has become 'impractical, imprudent, and therefore inequitable.'" *Id*. at 625. In the case on appeal, there was "no egg to unscramble" because the debtor was only aiming to reduce his payments going forward. She observed that equitable mootness has "invariably" been applied in cases involving "far greater sums of money, tangible property, and more parties."

After the overview (which could be read to add a fifth test alongside *Mac Panel's* four), Judge Berner applied the four *Mac Panel* tests, beginning with the debtor's pursuit of a stay pending appeal.

If equitable mootness were invoked whenever a debtor failed to seek a stay, Judge Berner said that "courts would functionally be imposing through judicial fiat a requirement that debtors always seek a stay to preserve their right of appeal." She declined to require a motion for a stay, because the "bankruptcy code does not impose such a requirement."

Substantial consummation of the plan is *Mac Panel's* second test. Because the debtor only sought to lower payments going forward and was not asking to claw back payments already made, Judge Berner said that substantial consummation did not weigh in favor of equitable mootness.

Whether relief on appeal would affect the success of the plan is the third *Mac Panel* test. Since the debtor only wanted to lower his monthly payments, Judge Berner said that plan success weighed against equitable mootness.

The fourth *Mac Panel* question is the effect on third parties. Judge Berner said it was "neutral," although creditors would receive a smaller recovery. Despite the fact that monthly payments would decline by $425, she noted that the "proposed changes are solely forward-looking."

Appearing to adopt a rule where size matters, Judge Berner said,

> The number of third parties involved in this case, however, as well as the dollar amount at issue, is significantly smaller than the instances where this factor has weighed in favor of equitable mootness.

Concluding that relief on appeal "would be practically and pragmatically available" and "that the *Mac Panel* factors weigh against application of the doctrine of equitable mootness," Judge Berner "reverse[d] the district court's finding that the matter is equitably moot."

The Merits

In less than a page, Judge Berner found no clear error in the bankruptcy court's finding that the first plan was not proposed in good faith. She therefore reversed the district court's dismissal of the appeal and affirmed the bankruptcy court's judgment confirming the debtor's fourth plan.

Acknowledgment

On behalf of the National Association of Consumer Bankruptcy Attorneys and the National Consumer Bankruptcy Rights Center, Richard P. Cook of Wilmington, N.C., submitted an *amicus* brief in support of the debtor, urging the Fourth Circuit to rule that equitable mootness did not apply in the consumer debtor's chapter 13 case. Mr. Cook did not take a position regarding the merits of the debtor's first plan.

The opinion is *Cook v. Chapter 13 Trustee*, 25-1048 (4th Cir. April 13, 2026).

The First Circuit sympathized with debtors whose discharges left them without a forum to pursue a lawsuit.

Dismissal or Discharge Doesn't Automatically End 'Related To' Jurisdiction, Circuit Says

A decision from the First Circuit demonstrates the principle that a bankruptcy court does not automatically lose "related to" jurisdiction when a bankruptcy case is dismissed or discharge is granted.

The March 4 opinion by Circuit Judge O. Rogeriee Thompson stands for the rule that the bankruptcy court's post-discharge or post-dismissal "related to" jurisdiction is a case- and fact-specific inquiry.

20 Years of Disputes and Litigation

A couple took down a mortgage in 2005 to purchase a home. After they defaulted in 2015, the bank agreed to consider accepting a short sale in lieu of foreclosure. The bank turned down the first three short sale offers but agreed to the fourth proposal. However, the debtors were unable to close before the bank's deadline.

The bank foreclosed and sold the home to the buyer who had made the fourth short sale offer. The bank obtained a deficiency judgment from the debtors amounting to some $115,000, prompting the couple to file a chapter 13 petition in 2017.

The litigation history after bankruptcy was lengthy and complex. Assume that the debtors sued the bank in bankruptcy court under Puerto Rico and federal law. While the adversary proceeding was pending, a relative died, giving the couple an inheritance sufficient to pay creditors in full.

The debtors filed a separate lawsuit against the bank in federal district court and a motion to withdraw the reference from the bankruptcy court, asserting a right to a jury trial. Now, it gets complicated, but we simplify.

The district court denied the motion to withdraw the reference and granted the bank's motion to dismiss the lawsuit in district court. The district court reasoned that comity and efficiency required having the same claims resolved in one court, the bankruptcy court. While the motion to dismiss was pending in district court, the bankruptcy court granted the debtors' discharges.

Following denial of the motion to withdraw the reference, the bankruptcy court, *sua sponte*, dismissed the adversary proceeding without prejudice, reasoning that the grant of discharges left the bankruptcy court bereft of "related to" jurisdiction. The debtors appealed, but the bank won in district court.

For reasons we don't need to explain, the debtors were able to appeal to the First Circuit, raising the question of whether the district and bankruptcy courts erred in failing to withdraw the reference and in dismissing for lack of jurisdiction.

Jurisdiction

We will skip over Judge Thompson's explanation for how there was appellate jurisdiction and how the debtors preserved issues for appeal. Addressing the merits, we begin with "related to" jurisdiction under 28 U.S.C. § 1334(b).

"In general," Judge Thompson said, "'related to' adversary proceedings will be dismissed following the termination of the underlying bankruptcy proceedings . . . . But this rule is not a command set in stone, and nothing in the Bankruptcy Code requires the automatic dismissal of a related adversary proceeding following the termination of an underlying bankruptcy case."

Citing the Second Circuit, Judge Thompson held that the bankruptcy court erred in "finding that the court's previously vested jurisdiction had automatically dissipated following the [debtors'] discharge." She went on to say that "we (like other courts) specifically declined to adopt a blanket rule that jurisdiction automatically terminates following the dismissal of an underlying bankruptcy petition."

"Instead," Judge Thompson cited the First Circuit in saying that "we concluded that the question of a bankruptcy court's post-dismissal (or discharge) jurisdiction is 'a case- and fact-specific inquiry.'" Elaborating, she said "that the case-specific inquiry should be gauged by several familiar factors: judicial economy, convenience to the parties, fairness, and comity." However, she "decline[d] to decide how those factors should be applied."

Nonetheless, Judge Thompson added commentary indicating that the bankruptcy court should seriously consider finding post-discharge jurisdiction. She said, "[T]he bankruptcy court was primed to exercise its jurisdiction and accompany its 65 findings of fact with conclusions of law for the district court's review."

Withdrawal of the Reference

The debtors had made two motions to withdraw the reference. The district court had denied the first as being untimely and denied the second because the first was untimely.

Judge Thompson said that the district court's "opinion [was] ambiguous as to whether it considered the changes in that status following the rejection of the [debtors'] first motion for withdrawal." She found "no authority . . . for the proposition that once a party's motion for withdrawal is deemed untimely, that party is forever barred from filing a timely motion in the future."

Instead, Judge Thompson said that "the district court should have considered the present status of proceedings in the bankruptcy court." Remanding, she said, "[W]e expect the district court to address the [debtors'] request for a jury trial." Although not specifying how the district court should rule on withdrawal following remand, she said, "[T]he fact remains that the [debtors] sought a withdrawal of reference on this basis, and the district court did not engage their request."

Judge Thompson vacated and remanded for the bankruptcy court to reconsider the question of subject matter jurisdiction and for the district court to reconsider withdrawal of the reference.

The opinion is *Guallini-Indij v. Banco Popular de Puerto Rico (In re Guallini-Indij)*, 23-1705 (1st Cir. March 4, 2026).

Beware the super discharge in Section 1328(a) where debts discharged under Section 523(a)(10) may be dischargeable in a future chapter 13 bankruptcy.

Denial of Discharge Doesn't Moot a Dischargeability Complaint or End Jurisdiction

The Ninth Circuit Bankruptcy Appellate Panel held that denial of a debtor's discharge does not moot or terminate jurisdiction for a pending dischargeability suit seeking to liquidate the amount of the allegedly nondischargeable debt.

The BAP's April 13 opinion is nonprecedential. Given the importance of several holdings, the panel might consider reissuing the opinion as precedential.

The Debtors Lose Their Discharges

The debtors owned and ran a business of renovating and flipping homes. They borrowed $50,000 from a creditor on the promise of 12% interest. After the loan matured without repayment, the creditor declared a default.

The debtors filed a voluntary chapter 7 petition but failed to file tax returns and correct their schedules. The Section 341 meeting was continued 10 times on account of the debtors' failure to provide information.

Eventually, the U.S. Trustee filed a complaint to deny the debtors' discharge under Section 727 for failure to keep adequate records, among other allegations. On the same day, the creditor filed a complaint to except the $50,000 debt from discharge. The complaint also sought to liquidate the amount of the debt.

The debtors and the creditor stipulated to stay the dischargeability suit pending the outcome of the discharge action by the U.S. Trustee. Either party had the right to request a lifting of the stay once there was a conclusion to or dispositive motion practice in the discharge action.

After three years of litigation, the bankruptcy court denied the debtors' discharges. The denial of discharge became final as to both debtors.

The creditor believed that the denial of discharge mooted the creditor's dischargeability action. (As we shall see later, the BAP decided that dischargeability did not become moot.) The creditor, though, asked the bankruptcy court to vacate the stay on the dischargeability suit to permit liquidation of the amount of the debt.

The debtors opposed lifting the stay, based on the idea that dischargeability was moot and that the bankruptcy court lacked jurisdiction following the denial of discharge. After the bankruptcy court lifted the stay, the creditor moved for summary judgment as to the amount of the debt.

The debtors did not dispute the creditor's undisputed facts but contended that the bankruptcy court no longer had jurisdiction because dischargeability had become moot. The bankruptcy court disagreed and awarded the creditor $95,500 by granting summary judgment.

The debtors appealed to the BAP.

Not Moot

The BAP first wrestled with the question of whether denial of discharge mooted the dischargeability suit. The BAP recounted how the bankruptcy court and the debtor both believed that dischargeability had become moot.

Citing Section 523(a)(10), the BAP said, "[N]o debts are discharged in the current bankruptcy and no debts which were listed or could have been listed can be discharged in any future *chapter 7 case*" when the debtor has been denied a discharge under Section 727. [Emphasis in original.]

The exception to the general rule in chapter 13 cases is what kept the dischargeability suit from becoming moot.

As the BAP said, the so-called super discharge in Section 1328(a) "continues to discharge § 523(a)(10) Debts." Therefore, the panel said, "§ 523(a)(10) Debts may be dischargeable in a future chapter 13 bankruptcy unless there is an independent basis for excepting that debt. Applicable to this case are the exceptions added to § 1328(a)(2) which now except from the super discharge[] § 523(a)(2) debts."

In somewhat more plain English, the BAP said, "§ 523(a)(10) Debts may be discharged in a future chapter 13 bankruptcy . . . unless a creditor obtains an independent reason to preclude the debt from being discharged (*e.g.*, § 523(a)(2) nondischargeability determination)."

The panel also concluded that dischargeability was not moot because the creditor "is likely precluded from seeking such a determination in future proceedings" by the doctrine of claim preclusion that prohibits relitigation of claims that were previously available.

Jurisdiction

When the creditor filed the dischargeability complaint, the bankruptcy court had core and exclusive jurisdiction. After the debtors' discharges were denied, the creditor elected to proceed with liquidating the amount of the debt on the mistaken belief that dischargeability was moot.

The BAP held that the creditor's "decision to litigate only part of its claim did not deprive the bankruptcy court of jurisdiction *as jurisdiction is determined at the time a complaint is filed*." [Emphasis added.]

Although there was jurisdiction, the BAP said that the bankruptcy court should have considered whether retaining jurisdiction was proper, because the remaining claim for a money judgment didn't exist outside of bankruptcy. Even so, the panel cited the Ninth Circuit for the idea that "bankruptcy courts are not automatically divested of jurisdiction over related cases when the underlying bankruptcy case has been dismissed."

The BAP decided not to remand because the record was sufficient for the BAP itself to determine whether retention of jurisdiction was proper. The BAP found no abuse of discretion in retaining jurisdiction because forcing the parties to start again in another court would entail additional expense and inconvenience. Also, requiring the creditor to sue anew in another court would be "unfair," because the creditor elected to litigate in the forum selected by the debtors.

Since liquidation of the contract claim was not complex, comity did not weigh against retaining jurisdiction.

Having found that the exercise of jurisdiction was proper, the BAP affirmed after finding no error in granting summary judgment.

The panel consisted of Bankruptcy Judges Frederick P. Corbit, Jennifer E. Niemann and Scott H. Gan.

The opinion is *Rigon v. Europakids Preschool LLC (In re Rignon)*, 25-1072 (B.A.P. 9th Cir. April 13, 2026).

The Sixth Circuit majority and dissent have an intriguing debate over appellate jurisdiction.

In '13,' a Motion to Dismiss Must Precede Entry of a Conversion Motion, Circuit Says

Section 1307(a) gives a chapter 13 debtor the right to dismiss when confronted with a motion for conversion to chapter 7.

The majority in a recent Sixth Circuit opinion held that the right to dismiss evaporates if the chapter 13 debtor's motion to dismiss is filed after entry of the conversion order.

In the circuit's February 11 opinion, the dissenter believed there was no appellate jurisdiction. It appears to this writer that the dissenter was concurring in affirmance of the judgment of the bankruptcy court.

The Warning to Dismiss

The U.S. Trustee filed a motion to dismiss the chapter 13 case or convert to chapter 7. The debtor responded by opposing dismissal.

At the hearing, Bankruptcy Judge Scott W. Dales found that conversion to chapter 7, not dismissal, was in the better interest of creditors. Telling the debtor's counsel that he would sign a conversion order, Judge Dales warned the debtor's counsel to file a dismissal motion before entry of the conversion order, else the case would be converted, not dismissed.

At the end of the day, the bankruptcy judge entered the conversion order. Less than two hours later, the debtor filed a motion to dismiss under Section 1307(a). The section provides: "The debtor may convert a case under this chapter to a case under chapter 7 of this title at any time. Any waiver of the right to convert under this subsection is unenforceable."

The bankruptcy judge denied the motion to dismiss the day after it was filed. Within two weeks, the debtor appealed neither the conversion order nor the order denying the debtor's motion to dismiss.

About two months later, the debtor filed a motion for reconsideration under Rule 60(b)(1). After Judges Dales denied the motion, the debtor appealed, but the district court affirmed, prompting the debtor's appeal to the circuit.

Dismissal Motion Came Too Late

The majority opinion by Circuit Judge Karen Nelson Moore found appellate jurisdiction and concluded that the debtor's appeal from the rehearing motion allowed the appeals court to review both the conversion order and the order denying the debtor's motion to dismiss.

Rule 60(b)(1) provides for relief arising from "mistake, inadvertence, surprise, or excusable neglect." Quoting Sixth Circuit precedent, Judge Moore said that the rule permits relief only "'(1) when a party has made an excusable mistake or an attorney has acted without authority, or (2) when the judge has made a substantive mistake of law or fact in the final judgment or order.'"

Judge Moore said that the circuit's authority requires the court to consider three factors: (1) culpability — that is, was the neglect excusable; (2) prejudice to the opposing party; and (3) a meritorious underlying claim.

Given the warnings by the bankruptcy court about the need for filing a dismissal motion before entry of the conversion order, Judge Moore held that the debtor had "not shown that his failure to move for dismissal before the case was converted was the result of excusable neglect."

Regarding the debtor's substantive argument based on the right to dismiss under Section 1307(a), Judge Moore quoted *Harris v. Viegelahn*, 575 U.S. 510, 520 (2015), where the Supreme Court held that "no Chapter 13 provision holds sway" after a case is converted.

Because the case had been converted, Judge Moore held that "§ 1307 was no longer applicable and [the debtor] no longer had the right to dismiss voluntarily under that provision." In that respect, she quoted the Sixth Circuit Bankruptcy Appellate Panel for correctly holding that Section 1307(a) "'does not grant a debtor an absolute right to dismiss a case after the case has been converted.'" *Skandis v. Moyer (In re Skandis)*, 648 B.R. 918, 923 (B.A.P. 6th Cir. 2023).

The majority affirmed, finding no abuse of discretion in denying the motion for reconsideration.

The Dissent

Circuit Judge John K. Bush dissented, believing there was no appellate jurisdiction. In his view, the conversion order was not within the scope of the notice of appeal, and denial of the motion to dismiss was not a final order.

In this writer's view, the dissenting opinion *might* be cited for the principle that denial of an order in a contested matter (as opposed to an adversary proceeding) is not a final order.

The opinion is *O'Hara v. Vara (In re O'Hara)*, 25-1203 (6th Cir. Feb. 11, 2026).

A final judgment on an issue in state court doesn't by itself deprive federal courts of subject matter jurisdiction under the Rooker-Feldman doctrine, the Third Circuit explains.

Circuit Judge Ambro Scribes the Boundaries Between *Rooker-Feldman* and Preclusion

Circuit Judge Thomas L. Ambro has written another gem.

For the Third Circuit in an opinion on September 3, Judge Ambro drew the boundaries between the rules of preclusion and the *Rooker-Feldman* doctrine, a jurisdictional principle. He held:

> The *Rooker-Feldman* doctrine is narrow, and it applies only when a federal plaintiff improperly invokes the jurisdiction of a district court to appeal — in fact or in effect — a state-court judgment.

In the case on appeal, preclusion based on a final state court judgment barred the debtor from asserting a claim in bankruptcy court. However, *Rooker-Feldman* did not deprive the bankruptcy court of subject matter jurisdiction.

Multiple Bankruptcies

As Judge Ambro put it, a couple filed "bankruptcy again and again" to forestall home foreclosure.

Before their first bankruptcy, the couple defaulted on their home mortgage. In foreclosure, they contended that the plaintiff wasn't the holder of the mortgage and had no standing to foreclose. The state court overruled the objection and entered a judgment of foreclosure. The same day, the couple filed a chapter 7 petition and later received a discharge.

A year later, the wife filed a chapter 13 petition and obtained permission from the bankruptcy court to challenge the foreclosure judgment. The state trial court denied rehearing and was affirmed by the state appellate court. The state supreme court denied review, meaning that the foreclosure judgment was final and that the lender had standing to foreclose.

The wife withdrew her chapter 13 petition, but the husband filed one of his own. The wife filed another chapter 13 petition, in which the lender sought relief from the automatic stay.

The wife resisted the lift-stay motion by contending that the lender didn't hold the mortgage, the same issue that had been litigated unsuccessfully in state court. After the bankruptcy court lifted the stay, the wife appealed, but the district court affirmed the lift-stay motion and also ruled that there was no jurisdiction in view of *Rooker-Feldman*.

The wife appealed to the circuit. Judge Ambro agreed that the wife loses, but not on account of *Rooker-Feldman*. Rather, he found jurisdiction and said, "[W]e exercise it to hold that her claims are precluded."

The Evolution of *Rooker-Feldman*

Judge Ambro traced the history of *Rooker-Feldman* from Supreme Court opinions in 1923 and 1983. The doctrine is based on the constitutional principle that only the Supreme Court has jurisdiction over final judgments of state supreme courts.

Quoting *Exxon Mobil Corp. v. Saudi Basic Indus.*, 544 U.S. 280, 283 (2005), Judge Ambro said that "mischief ensued" over the years "as 'the lower courts' '[v]ariously interpreted' the *Rooker-Feldman* doctrine 'to extend far beyond the contours of the *Rooker* and *Feldman* cases, overriding Congress' conferral of federal-court jurisdiction concurrent with jurisdiction exercised by state court.'" Again quoting *Exxon Mobil*, he said that "'federal jurisdiction over an action does not terminate automatically on the entry of judgment in the state court.' *Id.* at 293."

"*Rooker-Feldman* captures only a simple, if not elusive, rule of federal jurisdiction," Judge Ambro said. The narrow rule "does not 'supersed[e] the ordinary application of preclusion law' when a plaintiff relitigates a matter decided in another forum."

Preclusion

Judge Ambro explained how rules governing issue and claim preclusion arise from the Constitution's Full Faith and Credit Clause. Quoting the Supreme Court, he said that claim preclusion means that "a prior final judgment forecloses 'successive litigation of the very same claim.'" In contrast, he said that issue preclusion "bars 'successive litigation of an issue of fact or law'" that was "'actually litigated[,] resolved in a valid court determination[, and] essential to th[at] prior judgment,' even if the issue recurs in the context of a different claim."

Judge Ambro said "it is easy to imagine how a matter barred by preclusion — a suit in district court, for example, that attempts to relitigate a prior state-court claim — looks a lot like something that might offend *Rooker-Feldman*." Quoting the Supreme Court, he said, "*Rooker-Feldman* does not 'stop a district court from exercising subject-matter jurisdiction simply because a party attempts to litigate in federal court a matter [precluded because it was] previously litigated in state court.'"

Rooker-Feldman in Bankruptcy

Although courts unanimously hold that *Rooker-Feldman* applies in bankruptcy cases, Judge Ambro quoted the Third Circuit in saying that "'bankruptcy courts are empowered to avoid state judgments'" under Sections such as 544, 547 and 548, "in an 'apparent contradiction to *Rooker-Feldman*.'"

Judge Ambro went on to explain that "those bankruptcy-court powers over state-court judgments are not based on separate invocations of jurisdiction that violate *Rooker-Feldman*." Rather, he held:

> *Rooker-Feldman* applies only when two additional conditions are met: (a) procedurally, the claim is alleged as part of an adversary proceeding . . . ; and (b) the federal bankruptcy plaintiff's claim, even if 'one that denies a legal conclusion that a state court has reached in a case to which [the plaintiff] was a party,' is not otherwise 'independent' of her state-court claims.

For a proper application of the principles, Judge Ambro pointed to *Philadelphia Entertainment & Development Partners*, 879 F.3d 492 (3d Cir. 2018), where a state court had terminated a gaming license that had been purchased for $50 million. In bankruptcy, the debtor sought to avoid the termination as a fraudulent transfer, but not because the termination had been improper as a matter of state law. To read ABI's report on *Philadelphia Entertainment*, click here.

Judge Ambro explained that there was no violation of *Rooker-Feldman* in *Philadelphia Entertainment* because the avoidance action did not challenge the "bona fides" of the state court judgment. Instead, the issue in bankruptcy court was whether license revocation was avoidable under the Bankruptcy Code as a fraudulent transfer.

Holding

In the case on appeal, the debtor was not the plaintiff on the lift-stay motion in bankruptcy court. Judge Ambro therefore held that *Rooker-Feldman* did not apply. However, the debtor's defense to stay modification was based on the lender's lack of standing. The standing defense was precluded, given the state court's final judgment confirming the lender's right to foreclose.

"Even though [the debtor's] claims are not barred by *Rooker-Feldman*," Judge Ambro affirmed "the District Court's order insofar as it affirmed the Bankruptcy Court's granting of [the lender's] motion to lift the automatic stay" because "they are precluded under New Jersey law."

The opinion is *In re Adams*, 24-1212 (3d Cir. Sept. 3, 2025).

Ninth Circuit questions continuing validity of BAP opinions on finality handed down before Ritzen.

Reimposing the Stay Is a Final Order to Be Appealed Immediately, Ninth Circuit Says

The U.S. Supreme Court held in *Ritzen* that an order granting or denying relief from the automatic stay is a final, appealable order under 28 U.S.C. § 158(a)(1). *Ritzen Group Inc. v. Jackson Masonry LLC*, 589 U.S. 35 (2020). Reversing the district court, the Ninth Circuit held that revocation of a prior order modifying the automatic stay is also a final order requiring an immediate appeal.

In murky areas where it's unclear whether a bankruptcy court's order is final or not, the Ninth Circuit's Sept. 15 opinion means that counsel should take a cautious approach by filing a notice of appeal. An appellate court down the road might decide that the order was final and that an immediate appeal was necessary to preserve appellate jurisdiction.

Stay Modification Revoked

A mother created an irrevocable trust in 2011 and named her daughter as trustee. In 2017, the mother sued her daughter in state court, alleging misuse of trust property. In 2019, the daughter filed a chapter 13 petition, imposing an automatic stay on the suit in state court.

Three months after filing, the mother filed a motion to modify the automatic stay. The bankruptcy court granted the motion, modifying the stay and permissively abstaining in favor of the suit in state court.

During the COVID-19 pandemic, the state court announced that a trial could not be held for almost two years. On motion by the daughter under Rule 60(b)(6), the bankruptcy court revoked the prior order abstaining and modifying the stay.

The mother had filed a complaint in bankruptcy court raising the same claims that were pending in state court. A year after reimposing the stay, the bankruptcy court held a trial and entered judgment in favor of the daughter.

The mother appealed but only challenged the bankruptcy court's order reimposing the stay and vacating abstention. The notice of appeal came one year after the bankruptcy court's order, but the mother took the position that reimposing the stay and revoking abstention was an interlocutory order that could be appealed only after judgment in the underlying adversary proceeding.

The district court concluded that stay reimposition indeed was an interlocutory order, giving appellate jurisdiction. On the merits, the district affirmed the bankruptcy court's order, concluding that revocation was proper under Rule 60(b)(6) rather than Rule 60(b)(1). The mother appealed to the circuit.

In the circuit, neither party questioned appellate jurisdiction, but Circuit Judge Bridget S. Bade did, because a court must assure itself of jurisdiction.

Reimposing the Stay Was Final

Judge Bade began her analysis of appellate jurisdiction by citing *Ritzen* and its predecessor on finality in the bankruptcy context, *Bullard v. Blue Hills Bank*, 575 U.S. 496 (2015). She described *Ritzen* as holding "that an order granting or denying relief from the automatic stay is a 'final, appealable order' under 28 U.S.C. § 158(a)(1) because it 'forms a discrete procedural unit within the embracive bankruptcy case' and 'occurs before and apart from proceedings on the merits of creditors' claims.'" To read ABI's report on *Ritzen*, click here.

Judge Bade quickly disposed the notion that *Ritzen* did not control because *Ritzen* dealt with imposition of a stay, not reimposition of a stay. She said, "Although the [order reimposing the stay] did not, strictly speaking, grant or deny a party relief from the automatic stay, but instead *reimposed* the automatic stay, that is a distinction without a difference for purposes of finality." [Emphasis in original.]

Quoting *Bullard*, Judge Bade said that the order vacating "stay relief and abstention … and reimposing the automatic stay definitively disposed of a discrete dispute because it 'alter[ed] the status quo and fixe[d] the rights and obligations of the parties.' *Bullard*, 575 U.S. at 502." Her conclusion that the order reimposing the stay "disposed of a discrete dispute within the bankruptcy case, and thus was final, necessarily follows from *Ritzen*'s holding that orders granting or denying relief from the automatic stay are final, 589 U.S. at 42."

Abstention Was Also Final

To counter the conclusion that reimposition of the stay was a final order, the mother argued that the circuit should characterize the order as two orders, not one. In other words, the mother argued that revocation of abstention was a not final order, even if reimposition of the stay was final.

In response, Judge Bade said, "we do not think that the March 2021 order can be severed in this way." She explained,

> Both aspects of the order — addressing abstention and stay relief — are based on the same decision: whether it would be "in the interest of justice, or in the interest of comity with State courts or respect for State law," to have the Massachusetts state court resolve the state-law claims. 28 U.S.C. § 1334(c)(1). The two parts of the order rise and fall together.

Moreover, abstention revocation by itself was final. "[E]ven if considered separately from the adjudication of stay relief, the order rescinding abstention," she said, "'dispose[d] of a procedural unit anterior to, and separate from, claim-resolution proceedings' and is thus final in its own right."

Judge Bade vacated the district court's order affirming the bankruptcy court's revocation order and remanded with instructions to dismiss the appeal for lack of jurisdiction.

Footnote

Late in the opinion, Judge Bade suggested that a pair of decisions on finality by the Ninth Circuit Bankruptcy Appellate Panel may no longer be valid because they were decided before *Ritzen*. *See Krasnoff v. Marshack* (*In re Gen. Carriers Corp.*), 258 B.R. 181 (B.A.P. 9th Cir. 2001), and *Certain Underwriters at Lloyds, Syndicates 2623/623 v. GACN Inc.* (*In re GACN Inc.*), 555 B.R. 684 (B.A.P. 9th Cir. 2016).

The opinion is *Fantasia v. Diodato*, 23-3742 (9th Cir. Sept. 15, 2025).

Plans & Confirmation

ROCHELLE'S DAILY WIRE

Once a chapter 13 plan is confirmed, a debtor in the Sixth Circuit may not surrender collateral and treat the deficiency as an unsecured claim.

Sixth Circuit Restricts Ability to Surrender Collateral and Modify a Chapter 13 Plan

Unlike the majority of courts, the Sixth Circuit doesn't permit a chapter 13 debtor to surrender collateral, modify a confirmed plan and classify the deficiency as an unsecured claim.

Bound by Sixth Circuit precedent, Bankruptcy Judge Nancy B. King of Nashville, Tenn., devised a partial workaround in her June 24 opinion. She allowed the debtors to surrender the car while paying the remainder of the secured claim without interest. In other words, surrendering the car after confirmation allowed the debtor to avoid paying interest, despite still being required to pay the depreciated value of the car in full.

The Old Car

The debtors filed a chapter 13 plan in 2023 and confirmed a plan. Their ten-year-old car had an agreed value of almost $14,000. The plan treated the car loan as fully secured with interest payable under the plan at 10.5%.

The debtors had acquired the car within 910 days of filing, precluding them from bifurcating the auto loan under the hanging paragraph following Section 1325(a)(9).

After confirmation, the car had mechanical problems, and the debtor had financial difficulties. The debtors moved to modify the confirmed plan by surrendering the car and paying the $10,000 remaining agreed value of the car, but without interest.

The lender objected, contending that the debtor must continue paying interest under authority of two Sixth Circuit decisions, *Chrysler Fin. Corp. v. Nolan (In re Nolan)*, 232 F.3d 528 (6th Cir. 2000), and *Ruskin v. DaimlerChrysler Servs. N. Am. (In re Adkins)*, 425 F.3d 296 (6th Cir. 2005).

Nolan and *Adkins*

Judge King quoted *Nolan* as holding that a chapter 13

> "debtor cannot modify a plan under section 1329(a) by: (1) surrendering the collateral to a creditor; (2) having the creditor sell the collateral and apply the

proceeds toward the claim, and (3) having any deficiency *classified as an unsecured claim*." 232 F.3d 528, 535 (citation omitted) (emphasis added).

Judge King described the Sixth Circuit in *Nolan* as having focused "on debtors manipulating the system by using the collateral post-confirmation until all the value has been wrung out of it, then surrendering the collateral and modifying the plan to reduce the payment to the secured creditor."

Judge King went on to say that the circuit in *Adkins* "doubled down on the holding in *Nolan*" by "extend[ing] the holding to include not just voluntary surrender, but also the more prevalent circumstance of debtors seeking to modify the treatment of a secured creditor who has obtained relief from the automatic stay and foreclosed."

"The majority of courts outside the Sixth Circuit have found *Nolan* and *Adkins* unduly restrictive," Judge King said. She quoted Bankruptcy Judges David D. Cleary and William R. Sawyer as having said that the decisions were "simply wrong." She quoted Judge Sawyer as saying that "the Sixth Circuit erected several artificial restrictions on post confirmation plan modification." *In re Scarver*, 555 B.R. 822, 833-834 (M.D. Ala. 2016).

Judge King described the "two main criticisms of *Nolan* and *Adkins*" as follows:

> (1) The Sixth Circuit's interpretation of 11 U.S.C. § 1329 is unnecessarily narrow and/or restrictive, and (2) *Nolan* and *Adkins* do not leave room for reconsideration of a claim under 11 U.S.C. § 502(j).

Quoting *In re Disney*, 386 B.R. 292, 304 (Bankr. D. Colo. 2008), Judge King said, "Most courts . . . point out that when 11 U.S.C. § 1329(a) 'is read in context with claim reconsideration under § 502(j), it is apparent that § 1329(a) permits modifications to be made to a plan that reflect the reality of changed circumstances.'"

The Partial Workaround

Judge King said she was bound by Sixth Circuit precedent unless there "is a legitimate distinguishable basis to rule otherwise."

Distinguishing the case before her, Judge King said that "the Debtors are not seeking to 'reclassify' [the lender's] claim, not seeking to foist depreciated collateral values on [the lender], and not seeking to discharge the balance owed to [the lender]."

Instead, Judge King said that the debtors were "proposing to pay [the lender] **the value of the claim determined at confirmation**, albeit without additional post-surrender interest." [Emphasis in original.] As a result, she said that the lender "bears no greater risk than any other Chapter 13 creditor who no longer has collateral to protect its claim."

Consequently, Judge King said that the "concerns of *Nolan* and *Adkins* are not present under the facts of this case."

Judge King found a "meaningful distinction." Where *Nolan* focused on preventing a debtor from thrusting the economic burden on the lender, she said, "That policy concern does not arise when the debtor is paying the value of the claim as determined at confirmation, albeit without further interest." She went on to say that "modification to surrender collateral is expressly authorized in 11 U.S.C. § 1329(a)(1) and (3)" and "nothing in *Nolan* nor *Adkins* holds to the contrary."

Distinguishing the two circuit decisions, Judge King said that the "Debtors are not attempting to reclassify but are instead seeking only to modify the amount of the payment to take into account the surrender and sale of the collateral" and "are still paying the secured creditor the full value of its allowed claim as was set at confirmation, but without post-surrender interest."

Judge King held that the proposed plan modification "fits squarely within 11 U.S.C. § 1329 and within the boundaries of what is permissible in the Sixth Circuit under *Nolan* and *Adkins*." She overruled the objection and granted the motion to modify the plan.

Observations

A direct appeal would give the Sixth Circuit an opportunity to sit *en banc* and consider aligning the circuit's authority with the majority of courts.

A decision by former Bankruptcy Judge Keith M. Lundin contrary to *Nolan* and *Adkins* is cited in Judge King's decision. She also quotes and cites Judge Ludin's treatise, LundinOnChapter13.com.

Judge Lundin provided the following commentary to ABI:

> If Judge King's decision goes up, it would offer the Sixth Circuit an opportunity to create a small space for chapter 13 debtors around its (mistaken) decisions in *Nolan* and *Adkins*. More than two decades of contrary decisions from other courts amply demonstrates that *Nolan* was misguided. As much as I wish for *en banc* correction of *Nolan*, *Adkins* signals that the Sixth Circuit will stubbornly stick to its lonesome path.

The opinion is *In re Bain*, 23-03205 (Bankr. M.D. Tenn. June 24, 2025).

Bankruptcy Judge Hunt in Salt Lake City split with the Sixth Circuit, which held that a debtor can't modify a plan by surrendering a car but must continue paying the auto lender in full.

Courts Split on Modifying a '13' Plan to Surrender a Car with the Deficiency Unsecured

"Respectfully" disagreeing with the Sixth Circuit and several lower courts, Chief Bankruptcy Judge Peggy Hunt of Salt Lake City allowed a chapter 13 debtor to surrender a car after confirmation and modify the plan by making the deficiency on the secured claim an unsecured claim.

The debtors owned a car, for which the lender filed a partially secured and unsecured claim. The claim was allowed.

When confirming their chapter 13 plan, the debtors intended to retain the car. Their plan contained a nonstandard provision allowing the debtors to pay the full amount of the lender's secured and unsecured claim directly to the lender. Unsecured creditors were to receive no distribution.

Not long after confirmation, the debtors decided they couldn't afford the car and moved under Section 1329 to modify the plan by allowing them to surrender the car to the lender and stop making payments to the lender. The modified plan allowed the lender to modify its unsecured claim after selling the car to determine the amount of the deficiency.

The lender did not object to the plan modification, but the chapter 13 trustee did. In her October 27 opinion, Judge Hunt overruled the trustee's objection and disagreed with *In re Nolan*, 232 F.3d 528 (6th Cir. 2000).

Section 1329(a)(3)

Judge Hunt stated the issue as

> whether the confirmed Plan may be modified under § 1329 to allow the Debtors to surrender the [car] to the [secured lender] to sell, with liquidation proceeds applied to its claim, and the deficiency claim treated as a general unsecured claim.

After confirmation "but before the completion of payments under such plan," Section 1329(a) provides that "the plan may be modified, upon request of the debtor, the trustee, or the holder of an allowed unsecured claim. . . ." For the case at hand, subsections (a)(1), (a)(2) or (a)(3) of Section 1329 were potentially applicable. Judge Hunt began with subsection (a)(3), which allows an amendment to "alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan."

For subsection (a)(3), the question was whether payments by the debtors directly to the auto lender were "provided for by the plan." Judge Hunt said that "§ 1329(a)(3) applies if a claim is in any way dealt with in the plan, including being paid through or outside of the plan, and the distributions may be ones made by a trustee or a debtor." More plainly in a footnote, she said, "The fact that the claim that is classified in the plan is paid directly does not mean it is not provided for by the plan."

The "only restriction," Judge Hunt said, "is that the amount of a distribution may only be altered 'to the extent necessary to take account' of 'any payment' on a secured and/or unsecured claim 'other than under the plan.'"

"These phrases," Judge Hunt said, "plainly encompass payments on a claim resulting from a secured creditor's liquidation of its collateral as the liquidation is accomplished outside the authority of the confirmed plan." Consequently, she held that the proposed amendment "is one allowed under the plain language of § 1329(a)(3)."

Section 1329(a)(1) and (a)(2)

Next, Judge Hunt decided that the proposed amendment "also is permissible under the plain terms of § 1329(a)(1) and (a)(2)." Subsection (a)(1) permits an amendment to "increase or reduce the amount of payments on claims of a particular class provided for by the plan," and subsection (a)(2) allows a modification to "extend or reduce the time for such payments."

In the case at hand, the secured auto lender was in a class of its own with full payment of the secured and unsecured claim. The amendment would both reduce the payments and the time over which the payments would be made, because the secured claim would be paid by selling the car following surrender.

Judge Hunt therefore held that the amendment is "permitted under § 1329(a)(1) and (a)(2)."

Differing with *Nolan*

Several lower courts and the Sixth Circuit in *Nolan* held that "modifying a confirmed plan to surrender a vehicle is not allowable," Judge Hunt said. She critiqued *Nolan* by saying that it "does not consider how claims are defined and allowed in bankruptcy and the treatment of allowed claims in a Chapter 13 plan."

Judge Hunt described *Nolan* as having been

> based primarily on the premise that § 1329 does not mention and therefore does not allow a debtor to "reclassify a previously allowed secured claim" or to "add a claim to the class of unsecured creditors[,]" but only to change the amount and timing of payments under subsection (a)(1) (subsections (a)(2) and (a)(3) of § 1329 were not considered).

Judge Hunt observed that Section 1329(a) does not mention reclassification or bifurcation, "but this wording is not required," because a "modification to surrender a vehicle does not reclassify or bifurcate a 'fully secured' claim." She elaborated,

> Accordingly, contrary to *Nolan*, modifying a confirmed plan to allow a collateral surrender does not result in a "reclassification" or "bifurcation" of an allowed secured claim or the "addition" of an unsecured claim. It merely modifies the treatment under the confirmed plan of the existing secured and unsecured portions of the creditor's allowed claim.

Judge Hunt went on to find support from the hanging paragraph in Section 1325(a)(5) which, she said, "states that if the debtor purchased and financed a vehicle within 910 days of the petition date, the creditor's claim is not valued under § 506."

By having excluded claims on recently-purchased cars from Section 506, Judge Hunt said that "Congress recognized that that section applies to cases, such as this case, where the hanging paragraph does not apply — thus requiring bifurcation of a secured claim into secured and unsecured components."

Judge Hunt found support in *In re Ballard*, 526 F.3d 634, 641 (10th Cir. 2008), where she described the Tenth Circuit as holding "that a creditor whose claim is secured by a vehicle will always have an allowed claim that is bifurcated into secured and unsecured components even when § 506 is inapplicable because of the hanging paragraph."

Judge Hunt said that "the [lender's] allowed claim . . . was already 'bifurcated'" and that the modification "did not 'reclassify' it. Surrender of the [car] in fact is an acknowledgment of the [lender's] allowed secured claim." She also took issue with *Nolan* for having said that "the modification violates § 1325(a)(5)(B), 'which mandates that a secured claim is fixed in amount and status and must be paid in full once it has been allowed.'"

Judge Hunt said there was "[n]o authority . . . in the Bankruptcy Code, including under § 1325(a)(5), to support that conclusion. In fact, . . . § 1329(a) expressly allows modification of a plan to alter payments and distributions to a secured creditor."

Alluding to courts like *Nolan* which saw *res judicata* as preventing amendments of the type, Judge Hunt said that they do "not recognize that . . . § 1329 itself allows a confirmed plan to be modified despite its binding effect."

Judge Hunt noted the courts that followed *Nolan* and those that disagreed. She cited the *Collier* and *Lundin* treatises as "rejecting *Nolan* for a variety of reasons."

Judge Nolan "respectfully" declined to follow *Nolan*, held that the modification was "permissible because it is within the express terms of § 1329(a)(3) and, alternatively, is permitted under the plain language of § 1329(a)(1) and (a)(2)."

The opinion is *In re Carter*, 214-22514 (Bankr. D. Utah Oct. 27, 2025).

The Seventh Circuit allows a procedure in chapter 13 that's similar to the payment of scheduled, undisputed claims in chapter 11 when there's no objection.

Seventh Circuit Allows a '13' Plan to Pay a Claim When the Claim Hasn't Been Filed

It is generally understood that a creditor must file a claim in order to be paid through a chapter 13 plan. If a creditor like a home mortgage lender does not file a claim, the debtor can file a claim for the lender and thus ensure that mortgage payments are deducted in the calculation of disposable income.

In Chicago, the debtor used a procedure that's known in the district as a "plan forward."

The debtor filed a plan showing the secured lender as being paid under the plan. Bankruptcy Judge Timothy A. Barnes confirmed the plan 22 days after filing and before the bar date.

The lender had notice of the plan, and no one objected to paying the lender under the plan, even though the lender didn't file a claim before or after the bar date.

More than a year after confirmation, the chapter 13 trustee filed a motion to modify the confirmed plan by removing the distribution to the lender and redirecting the payments to other creditors. Neither the lender nor the debtor objected to the modification, according to the July 31 opinion by Circuit Judge Ilana D. Rovner.

Bankruptcy Judge Barnes denied the motion and was affirmed in district court, prompting an appeal to the Seventh Circuit.

An Unfiled but Allowed Claim

Pointing to Bankruptcy Rule 3002(a), the trustee contended on appeal that a secured creditor must have an allowed claim to receive chapter 13 distributions. The rule provides that "every creditor must file a proof of claim . . . for the claim or interest to be allowed."

Beginning with Section 1327(a), Judge Rovner undertook an analysis of whether the lender had an allowed claim, although the lender had not filed a claim, nor had the debtor. The subsection provides that a confirmed plan binds "the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted, or has rejected the plan."

Judge Rovner concluded that "the trustee must distribute the funds according to the plan as written."

The trustee countered by referencing Rule 3021(a), which provides that trustees must make distributions after confirmation to "creditors whose claims have been allowed."

Conceding that a claim must be allowed, Judge Rovner asked, "how does a claim become allowed?" Then she inquired as to whether the filing of a claim by a creditor is the only way the claim may be allowed.

"Despite the fact that Congress sometimes distinguishes between 'claims' and 'allowed claims,'" Judge Rovner said that "Section 1326(a)(2) does not state that payments may only be made to creditors with allowed claims." Quoting a bankruptcy court in Wisconsin, she observed that "[the] procedural rule in 3021 is a 'generic rule in that it does not distinguish between a Chapter 11, 12, or 13 plan, nor does it specifically reference an allowed claim under Code sections 502(a) and (b)(9).'"

Judge Rovner decided that the Rules and the Code can be "reconciled," because a confirmed plan means that "the debtor and creditors are bound to the provisions of the plan. 11 U.S.C. § 1327(a)." By listing a secured creditor in a plan, she said that "the bankruptcy courts in this circuit have explained [that] the debtor effectively admits the creditor's secured claim to the extent the plan provides."

Judge Rovner therefore held that "confirmation of the plan 'allows' the secured claim to the extent it has been provided for in the plan." She explained in greater detail:

> We agree with those bankruptcy courts that conclude that confirmation of the plan makes all of the claims contained therein "allowed," because all parties are bound to the confirmation of the plan. Therefore, there is no conflict with 11 U.S.C. § 502[,] which "deems" a claim "allowed, unless a party in interest … objects." Nothing in the rule requires the filing of a claim as a prerequisite to allowance.

Distinguishing *Pajian*

For Judge Rovner, a hurdle was overcoming the language in *In re Pajian*, 785 F.3d 1161, 1163 (7th Cir. 2015), where the Seventh Circuit said, "A creditor must file a proof of claim in order to participate in Chapter 13 plan distributions."

Explaining why the language in *Pajian* was being read too broadly by the trustee, Judge Rovner said,

> The language in *Pajian* is referring to a fourth option which is not a permissible way to participate in plan distributions: a creditor may not fail to file a claim, fail to ascertain that the debtor has filed a claim on its behalf or added it to the proposed plan, and then swoop in after the bar date has passed and ask to be added to the plan. *See Pajian*, 785 F.3d at 1164.

In other words, "The *Pajian* opinion did not address the issue here at all," Judge Rovner said. She read *Pajian* as "address[ing] how to prevent the disruptive effect of tardy claims to which the debtor objects."

Judge Rovner affirmed the two lower courts for holding that the secured creditor "is not barred from receiving distributions from the Trustee under the terms of the confirmed plan[,] which specifically includes [the bank], notwithstanding the bank's failure to file a proof of claim."

Observations

Section 501(c) could be a statutory impediment to "plan forward." The subsection provides, "*If a creditor does not timely file a proof of such creditor's claim*, the debtor or the trustee may file a proof of such claim." [Emphasis added.]

Judge Rovner cited Section 501, but for the idea that a debtor may file a claim on behalf of a creditor. She did not cite subsection (c)'s italicized invocation that the debtor may file a claim "[i]f a creditor does not timely file a proof of such creditor's claim . . . ."

Assuming that providing for the creditor's claim in the plan is equivalent to filing a claim, the argument could be made that plan confirmation was statutorily premature. Even so, what's the damage? In basketball terms, is it "no harm, no foul"?

The circuit had another ground for allowing the plan to stay in place, namely, *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 272 (2010).

In violation of the statute, the plan in *Espinosa* discharged student loans without an adversary proceeding showing "substantial hardship." Despite the legal defect, the Supreme Court upheld enforcement of the plan, with Justice Clarence Thomas holding that "the confirmation order is enforceable and binding on [the lender] because it had actual notice of the error and failed to object or timely appeal." *Id*. at 275.

The trustee in the appeal before the Seventh Circuit was not contending that a plan modification was required because of changed financial circumstances. Rather, the trustee was saying that the plan did not comport with statutory requirements. *Espinosa* would require denial of the trustee's motion because the trustee had notice of the plan and did not object to the use of "plan forward."

Dissenting Commentary

Former Bankruptcy Judge Keith Lundin, the author of a leading treatise on chapter 13, provided the following commentary to ABI:

> Don't be confused: the "plan forward" process approved by the 7th Circuit is an outlier that threatens to corrupt unbroken parts of the Chapter 13 system. Most bankruptcy courts correctly read the Code and Rules to contemplate the filing and allowance of proofs of claim before trustees are authorized to make distributions under confirmed plans. The Seventh Circuit created a nonstatutory, non-Rules based pathway for creditors to get paid in Chapter 13 cases without the guardrails built into the well-defined claims allowance process.

Mr. Lundin is the author of the treatise *LundinOnChapter13.com*.

The opinion is *Hooper v. Crawford*, 25-2434 (7th Cir. July 31, 2026).

When a home is surrendered in chapter 13, the lender's claim can't be bifurcated until after the lender has foreclosed.

In a '13' Plan, Surrendering a Home Doesn't Permit the Debtor to Bifurcate the Claim

When surrendering a principal residence, a debtor's chapter 13 plan cannot bifurcate the lender's secured claim into secured and unsecured claims until the lender has foreclosed, for reasons explained in an opinion by Bankruptcy Judge John P. Mastando, III, of New York.

Absent consent by the lender, how can a chapter 13 debtor confirm a plan when surrendering a home without providing in the plan for payment of the secured claim in full? We ask readers to give us their ideas.

The Undetermined Deficiency

The chapter 13 debtor owned a home secured by a defaulted mortgage. The lender had filed a secured proof of claim for more than $570,000. The debtor's plan called for surrendering the home.

The debtor and the lender disagreed about the home's value. The debtor saw the home as worth some $490,000, but the lender pegged value at about $250,000.

Based on the debtor's valuation, the plan called for bifurcating the lender's claim into a secured claim paid in full by surrender and an unsecured deficiency claim of almost $85,000. The debtor therefore filed a motion to avoid the lien and bifurcate the mortgage claim under Section 506(a), leaving the lender with an unsecured claim of some $85,000.

The lender objected, prompting Judge Mastando to file his opinion on May 20.

Bifurcation Under Section 506(a)

The outcome turned on Section 506(a) and the relief that the subsection provides. In pertinent part, the subsection reads:

> An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the

valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

Judge Mastando paraphrased the subsection as meaning that "a claim secured by a lien on estate property is treated as secured only to the extent of the value of collateral; any amount exceeding the value of the collateral is treated as unsecured." He added, "Section 506(a), however, does not itself avoid liens."

Judge Mastando also considered Section 1322(a)(2) which, he said, "prohibits a plan from modifying 'the rights of holders of secured claims' secured only by a security interest in real property that is the debtor's principal residence." He read the Supreme Court's *Nobelman* opinion as meaning "that a Chapter 13 debtor may not strip down a partially secured mortgage on the debtor's principal residence to the value of the collateral" and "protect[ing] the mortgagee's rights from modification even if the claim is undersecured."

"Where a debtor elects to surrender collateral under § 1325(a)(5)(C)," Judge Mastando said, "the creditor retains its lien and may pursue state-law remedies, including foreclosure and sale." He added, "'Surrender' does not transfer title, extinguish the lien, or require immediate physical turnover . . . . After liquidation under non-bankruptcy law, any deficiency claim may be asserted as unsecured, subject to allowance under § 502."

No Valuation Before Foreclosure

The debtor's motion to avoid the lien, Judge Mastando said, raised two questions: (1) Could the court value the property before foreclosure, and (2) may the court value the property or establish the deficiency before foreclosure?

Judge Mastando began his analysis of the first question by observing that "Section 506(a) permits valuation only 'in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.'" He went on to say that the Supreme Court's decision in *Rash* means that "courts value collateral differently depending on whether the debtor retains or surrenders the property."

When a debtor is surrendering property, Judge Mastando said that "foreclosure value is the most appropriate valuation methodology." In addition, he said that "the deficiency amount may not be fixed by the Debtor's unilateral pre-foreclosure valuation."

To fix the amount of the deficiency, Judge Mastando held that "the creditor must first exercise its foreclosure rights under state law, liquidate the collateral in a foreclosure sale, and apply the sale proceeds to the debt." In the case before him, he said that the debtor "has that sequence backwards," because the debtor was aiming "to fix an unsecured deficiency claim, based on her own asserted valuation of the Property, before [the lender] has obtained possession of the surrendered Property or completed a foreclosure sale."

Judge Mastando held, "Any unsecured deficiency must be determined after that [foreclosure] process occurs, not by preemptive valuation on the Debtor's Motion." He said that "Section 506(a) merely classifies claims as secured or unsecured for bankruptcy purposes" and "does not itself avoid liens." Moreover, the debtor cannot "use § 506(a) to accomplish indirectly what § 1322(b)(2) prohibits."

Denying the debtor's motion to avoid the lien, Judge Mastando explained the correct process as follows:

> In light of the Debtor's proposed surrender of the Property, [the lender] retains its lien and may pursue foreclosure or other remedies under applicable state law. After foreclosure, [the lender] may then assert any resulting deficiency, if applicable, as an unsecured claim, subject to allowance under § 502. The Debtor may not use § 506(a) to determine that deficiency in advance of foreclosure.

Observations

What if the lender does not foreclose or delays foreclosure? How could the debtor confirm a plan? Could the debtor obtain any mileage by attempting to estimate the claim under Section 502(c)?

We invite readers to provide comments in the box below by suggesting how (or whether) the debtor could confirm a plan without classifying the lender as a secured creditor to be paid in full.

For example, would the debtor be entitled to proceed under chapter 7 on the theory that the lender's failure to foreclose overcomes the presumption of abuse under Section 707(b)?

The opinion is *In re Lopez*, 25-12885 (Bankr. S.D.N.Y. May 20, 2026).

Just because secured debt service is 'reasonably necessary' doesn't mean that the chapter 13 plan was filed in good faith.

Complying with Disposable Income Test Doesn't Necessarily Mean a Plan Is in Good Faith

The Fourth Circuit held that a debtor can't confirm a chapter 13 plan with 7.7% for unsecured creditors while retaining three luxury automobiles. The amorphous concept of good faith can trump technical compliance with the confirmation requirements in Section 1325(b), according to the Fourth Circuit's April 28 opinion.

The chapter 13 debtor had gross monthly income of more than $12,000. His nonfiling wife's monthly gross income was more than $4,000.

Less than three years before bankruptcy, the debtor had purchased three luxury automobiles on which he still owed about $138,000 on the filing date. In addition to a mortgage, the debtor had almost $85,000 in unsecured debt.

The debtor was above median income, but his calculation of disposable income was negative by more than $200, given debt service on the three cars.

The debtor filed a chapter 13 plan where the three auto loans would be paid off during the five-year term of the plan. Unsecured creditors would have a recovery of 7.5%.

Bankruptcy Judge David M. Warren of Raleigh, N.C., denied confirmation of the plan, holding that the plan had not been proposed in good faith under Section 1325(a)(3). Judge Warren rejected the idea that technical compliance with Section 1325(b) precluded a determination of whether the plan was filed in good faith.

Judge Warren buttressed his legal conclusion by finding no "practical need" for the debtor to retain the three luxury cars.

The district court allowed an interlocutory appeal but affirmed. The debtor appealed to the circuit.

The Dueling Code Provisions

The appeal had two subsections in Section 1325 facing off against one another. When there has been an objection to the plan, Section 1325(b) provides that the court may confirm a plan if the debtor has satisfied the disposable income test. In the case on appeal, the debtor had satisfied the disposable income test.

Section 1325(a)(3) provides that the court "shall" confirm a plan if it determines, among other things, that "the plan has been proposed in good faith and not by any means forbidden by law."

In his opinion for the court of appeals, Circuit Judge Paul V. Niemeyer characterized the debtor as contending that "his compliance with § 1325(b) [disposable income] immunized him from the bankruptcy court's consideration of whether he filed his plan in good faith under § 1325(a)(3)."

The debtor's position was not without support from legislative history. Before BAPCPA in 2005, the definition of "disposable income" was undefined in the Code, giving the courts discretion in deciding whether expenses were "reasonably necessary," Judge Niemeyer said.

Judge Niemeyer described the debtor as taking the position that BAPCPA removed discretion in fixing disposable income with "'a bright-line statutory test for debtors . . . whose income was above the median.'"

Judge Niemeyer characterized the debtor as believing "that a bankruptcy court cannot find a lack of good faith based on the debtor's decision to retain certain assets, however luxurious they might seem, when the payments for those assets are deemed to be 'reasonably necessary' under § 1325(b)."

'Good Faith' Survived BAPCPA

Judge Niemeyer found several reasons to disagree with the debtor. First, he said that "taking away that discretion does not ensure that all plans that comply with § 1325(b) were filed in good faith . . . . The scope of the good-faith requirement is much broader than simply reviewing the means-test calculation." Second, he said that the debtor "construes the good-faith requirement far too narrowly."

Third, Judge Niemeyer said that "good faith reaches beyond mere compliance to assess whether a proposed plan, even if in technical compliance, would nonetheless abuse the provision's purposes or violate the spirit of Chapter 13 or the Bankruptcy Code more broadly."

Fourth, Judge Niemeyer held that BAPCPA, "as a matter of statutory interpretation, . . . did not eliminate the requirement that a Chapter 13 plan be proposed in good faith." Again as a matter of statutory interpretation for the fifth reason, he said that "§ 1325(a)(1) requires *every* Chapter 13 plan to comply with *all the provisions* of Chapter 13, not only § 1325(b)'s disposable income requirement." [Emphasis in original.]

"Sixth and finally," Judge Niemeyer said, "the structure of the means test itself demonstrates that good faith remains a separate, independent requirement." Just because the disposable income test classifies an expense as necessary, he said it "does *not* mean that bankruptcy courts may not question the debtor's decision to retain assets serving as collateral for those secured loans when assessing, under § 1325(a)(3)." [Emphasis in original.]

Judge Niemeyer therefore held that "bankruptcy courts remain charged with considering, under *all the circumstances,* whether the debtor's proposed plan would amount to 'an abuse of the provisions, purpose, or spirit of the Chapter.'" [Emphasis in original.]

Distinguishing a Ninth Circuit Opinion

The debtor cited the Ninth Circuit in *Drummond v. Welsh* (*In re Welsh*), 711 F.3d 1120 (9th Cir. 2013), as supporting his conclusion. Judge Niemeyer said, "perhaps it does."

Judge Niemeyer described *Welsh* as having "held that a calculation made in compliance with § 1325(b) cannot be challenged," because BAPCPA removed discretion in calculating disposable income. However, he went on to observe that *Welsh* distinguished between Sections 1325(a)(3) and 1325(b) when the Ninth Circuit said, "These two inquiries are, indeed, separate and distinct." *Id*. at 1132.

Judge Niemeyer concluded that *Welsh* "does not support an argument that compliance with § 1325(b) somehow immunizes a debtor from the good-faith inquiry required by § 1325(a)(3)."

Finding no clear error in the bankruptcy court's findings about the lack of good faith, Judge Niemeyer affirmed the district court's judgment affirming the bankruptcy court's denial of confirmation.

The opinion is *Goddard v. Burnett*, 25-1303 (4th Cir. April 28, 2026).

The Ninth Circuit holds that claim preclusion doesn't prevent a debtor from claiming federal exemptions after the bankruptcy court has denied state exemption.

Claim Preclusion Didn't Preclude Making Successive Exemption Claims, Circuit Says

Reversing the district court and upholding a decision by Bankruptcy Judge Scott H. Gan of Tucson, Ariz., the Ninth Circuit held that issue preclusion does not prevent a debtor from successfully claiming a federal exemption after the bankruptcy court has previously denied exemptions under state law.

Of potentially greater significance, the circuit court recognized the bankruptcy court's discretion to grant an exemption that the debtor has not correctly claimed.

Three Shots at Exemptions

The individual chapter 7 debtor originally claimed an Arizona state exemption for real property and a recreational vehicle, or RV. When the trustee objected, the debtor amended his schedules to claim exemptions for the same property using Washington State law. When the debtor failed to oppose the trustee's objection to the Washington exemption claims, the bankruptcy court sustained both objections.

One month later, the debtor amended his schedules a third time, on this occasion claiming federal homestead exemptions for both the real property and the RV, utilizing the hanging paragraph in Section 522(b)(3). "If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption," the hanging paragraph provides that "the debtor may elect to exempt property that is specified under subsection (d)."

Under Section 522(d), the exemptions applicable to the case on appeal were the federal homestead exemption in Section 522(d)(1) and the so-called wildcard exemption in Section 522(d)(5).

At the hearing on the debtor's third exemption claim, Bankruptcy Judge Gan ruled that the debtor was entitled to the federal homestead exemption for the real property. Because the debtor had the right under Bankruptcy Rule 1009(a) to amend his schedules at any time, Bankruptcy Judge Gan dismissed the idea that the prior denial of the homestead exemption precluded an exemption under federal law.

Although the debtor had incorrectly claimed a federal homestead exemption for the RV, Bankruptcy Judge Gan granted the wildcard exemption for the RV, even though the debtor had not claimed a wildcard exemption.

Reversal in District Court

On appeal, the district court reversed, believing that claim preclusion prevented the debtor from claiming any federal exemptions after state exemptions had been denied.

The district court also ruled that the bankruptcy court should not have allowed the wildcard exemption when the debtor had not claimed that exemption.

The debtor appealed to the circuit and won in an October 14 opinion by District Judge Joan H. Lefkow of Chicago, sitting by designation.

Claim Preclusion

Addressing claim preclusion, Judge Lefkow began by paraphrasing the Ninth Circuit for holding that "unappealed orders denying exemptions are entitled to preclusive effect in later bankruptcy court proceedings." Moreover, claim preclusion bars subsequent litigation of claims that were raised or could have been raised. For claim preclusion, the Ninth Circuit requires an identity of claims, a final judgment on the merits and identity or privity between the parties.

In the case on appeal, the only issue was identity of claims. Among the four tests in the Ninth Circuit for identity of claims, the only question was whether the two suits arose from the same nucleus of facts.

More particularly in the Ninth Circuit, whether claims arose from the "same transactional nucleus of facts" turns on "'whether they are related to the same set of facts and *whether they could conveniently be tried together*.' *ProShipLine Inc. v. Aspen Infrastructures Ltd.*, 609 F.3d 960, 968 (9th Cir. 2010) (emphasis in original) (quoting *W. Sys., Inc. v. Ulloa*, 958 F.2d 864, 871 (9th Cir. 1992))."

While the Ninth Circuit had no authority regarding successive exemption claims, the Eighth Circuit had dealt with the question in *In re Ladd*, 450 F.3d 751 (8th Cir. 2006). There, the circuit reversed the lower courts for having ruled that claim preclusion barred a new exemption claim.

In *Ladd*, the Eighth Circuit noted that the debtor could not have raised a state exemption as an alternate theory to the federal exemption claim, because Schedule C does not allow pleading state and federal homestead exemptions in the alternative.

"We agree with *Ladd*," Judge Lefkow said, "that § 522(b)(1) and Schedule C prohibit raising state and federal homestead exemptions on a single schedule." She explained,

> Part 1 of Schedule C, which a debtor must use to claim exemptions, allows a debtor to claim *either* "state and federal nonbankruptcy exemptions" or "federal exemptions," but not both. [Emphasis in original.]

Judge Lefkow found "no claim preclusion here" given "the preclusion in bankruptcy of simultaneous state and federal claims of exemption." In other words, "the *availability* of a claim in an earlier proceeding is a necessary condition to claim preclusion." [Emphasis in original.]

In the case on appeal, Judge Lefkow said that "the federal claim could not have been tried with the Washington (or Arizona) claim, so no degree of similarity between the state and federal exemption statutes could result in claim preclusion."

The trustee contended that denial of the state exemption in a final order required claim preclusion. Judge Lefkow responded by saying that "a final judgment on the merits is only one element of claim preclusion."

Judge Lefkow said that her "determination is further supported by significant policy interests." She cited the House Report on Section 522 for saying that debtors are entitled to make full use of exemptions and that exemptions are to be interpreted liberally in favor of debtors. She also found "explicit support" in Bankruptcy Rule 1009(a), which allows a debtor to amend a schedule "at any time before the case is closed."

Reversing the district court for believing that claim preclusion barred the debtor from claiming federal exemptions, Judge Lefkow held "that, because the federal bankruptcy exemption could not have been raised or tried simultaneously with the exemption brought under Washington law, there is no identity of claims here and so no claim preclusion."

The Wildcard Exemption

The debtor claimed a federal homestead exemption for his RV, but Bankruptcy Judge Gan decided that the facts gave the debtor a valid wildcard exemption, even though the debtor never claimed a wildcard exemption for the RV. On appeal, the trustee argued it was error to grant an exemption that the debtor had not claimed.

Quoting the Ninth Circuit, Judge Lefkow said, "'we have the authority to identify and apply the correct legal standard, whether argued by the parties or not,'" and to consider as dispositive "'even an issue the parties fail to identify and brief.'" She therefore held that "[g]ranting the [wildcard] exemption . . . was an appropriate exercise of discretion."

Judge Lefkow nonetheless conceded that courts have declined to grant unclaimed exemptions *sua sponte*, but the matter before the bankruptcy court was a contested matter, not an adversary proceeding. In contested matters, she said, "bankruptcy courts have more discretion." Furthermore, Section 105(a) gives bankruptcy courts the right to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."

Judge Lefkow decided that the failure to claim a wildcard exemption was "a technical pleading error, not a failure to make an entirely discrete claim." Therefore, the "bankruptcy court appropriately identified the wildcard exemption within the governing federal scheme."

Reversing the district court's judgment about claim preclusion and applicability of the wildcard exemption, Judge Lefkow remanded to the district court with instructions to vacate its decision and remand to the bankruptcy court for proceedings consistent with the opinion.

Note

On behalf of the National Consumer Bankruptcy Rights Center and National Association of Consumer Bankruptcy Attorneys, James J. Haller of Chicago submitted an *amicus* brief on behalf of the debtor.

The opinion is *Nance v. Warfield (In re Nance)*, 24-2745 (9th Cir. Oct. 14, 2025).

Rochelle's Daily Wire

Bankruptcy Judge Jeffery Deller of Pittsburgh defines impermissible discrimination among unsecured creditors in a chapter 13 plan.

A '13' Plan Can't Pay Nondischargeable Debt in Full and Give Nothing to Other Creditors

Sometimes, it's impossible to find precedent for a self-evident proposition. Here's one where you won't have that problem: A chapter 13 debtor cannot pay nondischargeable debt in full while paying nothing to other unsecured creditors.

By stipulation, the chapter 13 debtor agreed that a creditor had a $27,000 nondischargeable, unsecured claim. The debtor had more than $43,000 in other dischargeable, unsecured claims.

The debtor proposed a plan where he would pay claims secured by his truck and tools. The plan would also pay the $27,000 nondischargeable claim in full but had nothing for other unsecured creditors.

The chapter 13 trustee objected to confirmation of the plan, contending that the plan discriminated unfairly against unsecured creditors with dischargeable claims. If the plan were to pay all unsecured creditors *pro rata*, the trustee calculated that unsecured creditors would recover about 35%.

Because the plan would free the debtor from the burden of the nondischargeable claim, the debtor argued that discrimination was a permissible extension of the "fresh start" policy.

Permissible and Impermissible Discrimination

The outcome turned on the interpretation of Section 1322(b)(1), which provides that a plan "may . . . designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated."

In his opinion on November 10, Bankruptcy Judge Jeffery A. Deller of Pittsburgh said that the words "may designate" connotes "flexibility," because "Congress could have forbidden all discrimination, but it did not. It allowed different treatment when fair."

Judge Deller noted how the Bankruptcy Code gives priority to certain types of unsecured claims, like domestic support obligations and some wages and taxes. "Notably absent," he said, "are nondischargeable, unsecured debts of the sort at issue here. Congress could have included them, but it did not."

"To draw the line between fair and unfair discrimination, courts therefore look to the Bankruptcy Code's overall structure and purpose," Judge Deller said. To draw the line, "courts have developed various tests." He cited the Eighth Circuit for developing a four-part test and the Seventh Circuit for requiring a result that is reasonable in light of relevant law. The Chicago-based appeals court, he said, "held that it would be unreasonable to approve a plan that fully pays a nondischargeable debt while leaving other creditors with nothing." *In re Crawford*, 324 F.3d. 539, 542 (7th Cir. 2003).

Judge Deller cited the First Circuit Bankruptcy Appellate Panel for rejecting the Eighth Circuit's four-part test and instead examining whether the plan differs from the "normative baseline," meaning what unsecured creditors would receive under the best-interests and disposable-income tests. *Bentley v. Boyajian (In re Bentley)*, 266 B.R. 229, 239 (B.A.P. 1st Cir. 2001). He went on to characterize the BAP as saying that a plan is unfair "when [it] reallocates benefits among equals." *Id*. at 240, 243.

Judge Deller cited cases from the early 1990s with "modest" discrimination in favor of student loans. In those cases, however, the debtors were paying something to other unsecured creditors.

No Justification

Applying the standards to the case at hand, Judge Deller decided that the plan could not be confirmed. The debtor's justification, that the debt was nondischargeable, "is insufficient," he said.

The "only effect" of the plan, Judge Deller said, "is to shift the cost of the Debtor's willful misconduct onto other innocent creditors." Consequently, the effect of the proposed discrimination was to "benefit" the debtor. Furthermore, he said, the "degree of discrimination is also excessive."

Regarding justification based on a "fresh start," Judge Deller said it was not designed "to shield one from the consequences of willful misconduct." Were it confirmed, the plan would "reward[] the debtor for his misconduct rather than hold him to account for it."

Standards for the Future

Judge Deller ended his opinion with "guidance" for cases coming before him in the future. He said that a plan discriminates "fairly" when there is a legitimate purpose, the discrimination is necessary, the degree of discrimination is no greater than necessary, *and* the plan is filed in good faith.

A plan is "unfair" when it results "solely" from nondischargeable debt, creates *de facto* priority among equals, diverts substantially all disposable income to one creditor, *or* penalizes innocent creditors.

Judge Deller denied confirmation of the plan.

The opinion is *In re Walko*, 24-22684 (Bankr. W.D. Pa. Nov. 10, 2025).

Courts are split on whether unsecured creditors are entitled to interest in full payment plans when debtors are paying less than monthly disposable income.

No Interest for Unsecured Creditors in Full-Payment Chapter 13 Plans

On an issue where the courts are split, Bankruptcy Judge Benjamin A. Kahn of Durham, N.C., decided that unsecured creditors are not entitled to interest on their claims under a chapter 13 plan when the debtors are paying less than their monthly disposable income.

With annual income of almost $170,000, the chapter 13 debtors had more than median income and were saddled with a five-year plan. Their disposable income under Section 1325(b)(2) was about $2,150, requiring them to pay almost $130,000 to creditors over the life of the plan.

The plan would pay unsecured creditors in full under Section 1325(b)(1)(A), but without interest. The chapter 13 trustee objected to confirmation, arguing that unsecured creditors should receive 8% interest on their claims, because the debtors were not devoting all of their monthly disposable income to plan payments.

Disjunctive Drafting of Section 1325(b)(1)

The answer to the objection lay in Section 1325(b)(1). When there is an objection to confirmation, the court may not confirm the plan unless:

> (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or (B) the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan.

At the outset of his analysis, Judge Kahn noted that the subsection "is written in the disjunctive, meaning that the plan must comply with either paragraph (A) or (B), not both." To confirm when there is an objection, he said that "a debtor may pay either the full amount of projected disposable income for the applicable commitment period under (B), or all allowed unsecured claims in full under (A)."

"Courts are split as to whether debtors opting to pay unsecured claims in full under (A) must pay interest on the unsecured claims," Judge Kahn said. As an example of a decision requiring interest, he cited *In re Gillen*, 568 B.R. 74, 77 (Bankr. C.D. Ill. 2017). To read ABI's report on *Gillen*, click here. To read ABI reports on opinions that don't require interest, click here and here.

Judge Kahn noted the circumstances when chapter 13 debtors are required to pay interest, such as to holders of fully secured claims under Section 1325(a)(5)(ii) and to unsecured creditors whose "claims hypothetically would be paid if the debtors' estates were liquidated under chapter 7 on the effective date of the plan" under Section 1325(a)(4).

In Judge Kahn's view, the answer to the puzzle lay in the placement of words. The best-interest test in Section 1325(a)(4) refers to "the value, as of the effective date of the plan." In Section 1325(b)(1), the words "as of the effective date of the plan" come before both subsections (A) and (B). However, the notion of "value" is only contained in (A), the subsection under which the debtors were pursuing confirmation.

Judge Kahn decided that the "better interpretation" was to understand that "the phrase 'as of the effective date of the plan' immediately succeeds the phrase 'the court may not approve the plan unless,' rather than 'value,' the phrase instead refers to its last antecedent — the date on which the court is to determine whether (A) or (B) is satisfied." He therefore concluded that the "plain language of the statute and the placement of the phrase reflects an intentional distinction between the meanings of the language by Congress."

Judge Kahn was inclined to follow the *Collier* treatise, which says that "Congress would presumably have used the same language as it used elsewhere to indicate a present value test," if the statute were intended to require interest on unsecured claims paid in full.

Not requiring interest, in Judge Kahn's view, "also reflects consistent bankruptcy policy."

"Although chapter 13 gives creditors access to income that they would not have in a chapter 7," Judge Kahn said, "it does not go even further to require debtors to provide the present value of property that debtors have not yet received." He added, "To require Debtors to pay interest under § 1325(b)(1)(A) would give creditors a windfall over the amounts they would receive even if Debtors were contributing all their monthly disposable income."

Holding that "§ 1325(b)(1)(A) does not require payment of interest to holders of unsecured claims who will be paid the full amount of their respective claims over the plan term," Judge Kahn overruled the trustee's objection to confirmation.

The opinion is *In re Peters*, 25-80018 (Bankr. M.D.N.C. Nov. 10, 2025).

Chapter 13 trustee can't require a debtor to maintain a 'safety net,' Bankruptcy Judge Hillen says.

Tax Refund Turnover Isn't Required When the '13' Plan Pays Creditors in Full

A chapter 13 debtor can't be required to turn over tax refunds to the trustee when the plan pays creditors in full, for reasons explained by Chief Bankruptcy Judge Noah G. Hillen of Boise, Idaho.

A couple had confirmed a five-year chapter 11 plan paying $685 a month. A year later, the debtors moved to modify their plan to pay unsecured creditors in full by raising the monthly payment to $810.

The chapter 13 trustee objected because the amended plan would not require the debtors to turn over income tax refunds to the trustee. In an opinion on November 21, Judge Hillen overruled the objection and granted the debtors' motion to modify the plan.

Section 1329 governs amendments of confirmed plans. Judge Hillen said that approvals of modifications are committed to the judge's discretion and "good judgment," after analyzing "the totality of the circumstances." The court, he said, must also balance the debtor's expenses against "what is fair to unsecured creditors."

Because the debtors were proposing to pay creditors in full, Judge Hillen said that the "Debtors have therefore met their burden of coming forward with adequate evidence that a modification of the plan may be appropriate."

The trustee nonetheless contended that the debtor should "be compelled to surrender their tax refunds during the plan term, even though the modified plan payments are sufficient to pay unsecured creditors in full," Judge Hillen said.

By turning over tax refunds, the trustee said that the debtors could complete their plan early. In other words, the trustee argued that the "Debtors should be compelled to complete their chapter 13 plan earlier than the statutorily mandated applicable commitment period under § 1325(b)(4)," Judge Hillen said.

The trustee pointed to the district's model plan that allows debtors, voluntarily, to complete their plans early. Judge Hillen found "no authority that permits a chapter 13 trustee to require a debtor to complete a plan earlier than the applicable commitment period."

Quoting one his own prior opinions, Judge Hillen said that modifying a plan "'to increase plan funding when a plan is already fully funded defies logic.'" *In re Rych*, 22-20240-BPH, 2025 WL 2730790 at *7 (Bankr. D. Idaho Sept. 24, 2025).

The trustee cited several cases for the proposition that it's appropriate for debtors to turn over tax refunds even when creditors are being paid in full. Judge Hillen said that the authorities were "distinguishable or inapplicable," for reasons he had explained in *Rych*.

One of the out-of-circuit opinions came from a court that had held "that the disposable income test applies to post-confirmation modifications," Judge Hillen said. He went on to say that the decision was "inconsistent with decisions from within the Ninth Circuit such as *In re Sunahara*, 362 B.R. 768 (B.A.P. 9th Cir. 2005)."

For a final argument, the trustee said that the debtors should turn over tax refunds to provide them "with more flexibility should they face financial difficulties in the future."

Judge Hillen said that the question was "not whether debtors obtain more flexibility if compelled to complete their chapter 13 plan earlier than the statutorily mandated applicable commitment period. Instead, the question," he said, "is whether the Code permits a trustee to require a debtor to do so. Simply put, it does not."

Again quoting his *Rych* opinion, Judge Hillen said, "'The Code does not contemplate maintenance of an economic safety net by trustees simply because the trustee harbors skepticism about future events.'" *Id.* at *6.

Overruling the trustee's objection and approving the plan amendment, Judge Hillen summed it up:

> If the value of the property to be distributed satisfies all claims, there is no additional requirement for a debtor to provide all her projected disposable income.

The opinion is *In re Fundin*, 24-20189 (Bankr. D. Idaho Nov. 21, 2025).

Compensation

Even though it was "a fortuitous result for the Debtors," Judge Krause "reverse[d] the District Court's judgment and . . . reinstate[d] that of the Bankruptcy Court."

The opinion is *In re Aquilino*, 24-1781 (3d Cir. April 24, 2025).

ROCHELLE'S DAILY WIRE

Seventh Circuit rules that the BAPCPA amendment to Section 1325(b)(1)(B) doesn't stop chapter 13 debtors' counsel from being paid during a plan.

A Confusing BAPCPA Amendment Doesn't Prevent Chapter 13 Counsel from Being Paid

Among the problems that Congress created in 2005 with BAPCPA, the amendment to Section 1325(b)(1)(B) could be read to mean that a chapter 13 debtor's counsel cannot be paid alongside unsecured creditors if there is an objection to confirmation.

Guided by astute *amicus* briefs, the Seventh Circuit affirmed Bankruptcy Judge Donald R. Cassling on direct appeals by holding that debtors' counsel can be paid over the life of a chapter 13 plan. In his June 10 opinion, Circuit Judge Michael Y. Scudder, Jr., said,

> [O]one thing is clear: Congress in 2005 did not upset decades of past practice or erase the Code's express command that debtors must pay bankruptcy attorneys' fees "[b]efore or at the time of each payment to creditors under the plan." 11 U.S.C. § 1326(b)(1).

Lawyers Paid Alongside Creditors

As an unsecured creditor, the city of Chicago had been objecting to confirmation of chapter 13 plans when there was an objection to confirmation and the plans paid debtors' counsel alongside creditors over the life of the plan. Last year, Bankruptcy Judge Cassling confirmed two plans over the city's objection.

In two later cases, the city appealed, and the Seventh Circuit accepted direct appeals.

The cases in the circuit were similar. Both debtors were below median income, and both had three-year plans. Both plans paid secured creditors, priority creditors and the debtors' counsel. One debtor's plan had disposable income left for unsecured creditors, and the other didn't. The city had unsecured claims in both cases.

On appeal, Judge Scudder described the city as contending that the plans violated Section 1325(b)(1)(B) because "the plans allocated funds to pay attorneys' fees during the three-year commitment period."

If there is an objection to confirmation and the plan isn't paying claims in full, the subsection provides that the court may not confirm the plan unless

> the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied *to make payments to unsecured creditors* under the plan. [Emphasis added.]

The city submitted that debtors' counsel are not unsecured creditors and may not be paid from disposable income.

The Amendment Didn't Change Past Practice

Although Section 1325(b)(1)(B) does prohibit confirmation over an objection unless disposable income goes for "payments to unsecured creditors under the plan," Judge Scudder said, "[W]e cannot read § 1325(b)(1)(B) in isolation. The Bankruptcy Code as a whole makes clear that Chapter 13 plans may provide payments for attorneys' fees during a commitment period."

Judge Scudder pointed to several provisions in the Code requiring payment of counsel fees. Priority claims, he said, must be paid, and attorneys' fees are in that category, pointing to "11 U.S.C. §§ 507(a)(2), 503(b)(2), 330(a)(4)(B)." Furthermore, priority claims "'shall be paid' '[b]efore or at the time of each payment to creditors under the plan,' *id*. § 1326(b)(1)." He therefore held,

> Chapter 13 plans must provide for the payment of attorneys' fees before or at the same time as any payments to nonpriority unsecured creditors during the commitment period.

Judge Scudder explained how the confusion arose. Prior to 2005, Section 1325(b)(1)(B) provided that disposable income had to be "applied to make payments under the plan" when there was a confirmation objection. The BAPCPA amendment changed the language so it now reads, "applied to make payments *to unsecured creditors* under the plan." [Emphasis added.] He described the city as claiming that the amendment was a "sea change."

Judge Scudder saw the change as "more limited" and followed the Supreme Court's instructions "not to 'read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure.'" He saw "nothing in the amendment [to] suggest[] Congress meant to displace the decades-old practice of Chapter 13 plans providing for payment of attorneys' fees prior to nonpriority unsecured claims."

Regarding the amendment, Judge Scudder said, "BAPCPA left untouched the Code sections requiring debtors to pay attorneys' fees before or at the same time as nonpriority unsecured claims." Likewise, he saw "no reason" why attorneys' fees weren't "reasonably necessary" expenses for debtors with below median income.

Seeing no reason for requiring attorneys to file proofs of claim, Judge Scudder affirmed confirmation of the plans.

Acknowledgments

The Seventh Circuit received *amicus* briefs from Thomas Moers Mayer and James J. Haller on behalf of the National Association of Consumer Bankruptcy Attorneys and from Henry E. Hildebrand, III, on behalf of the National Association of Chapter Thirteen Trustees.

The opinion is *In re Falkner*, 25-2878 (7th Cir. June 10, 2026).

The law firm's fully compliant retention application permitted an allowance of compensation, even though the court never entered a retention order.

Compensation Can Sometimes Be Allowed in the Absence of a Retention Order

Because the case moved so quickly that the bankruptcy court hadn't entered an order approving retention of the debtor's counsel, District Judge Leonie M. Brinkema of Alexandria, Va., upheld the bankruptcy court's allowance of compensation when the lack of a retention order was not counsel's fault.

Judge Brinkema's April 21 opinion includes a salutary narrowing of the Fourth Circuit's split decision in *David v. King*, 109 F.4th 653 (4th Cir. July 26, 2024), where the majority held that a former trustee had no authority to seek retroactive retention of counsel.

Legal Services Provided Without a Retention Order

Pro se, an individual filed a chapter 11 petition and immediately ran into trouble when the principal creditor filed an adversary proceeding to affirm the validity of the debt. Troubles compounded when the U.S. Trustee moved five weeks after filing for conversion of the case to chapter 7.

Recognizing the need for counsel, the debtor hired a law firm that filed a retention application some eight weeks into the chapter 7 case. Judge Brinkema said that the firm's retention papers "fully complied with § 327(a) and Rule 2014."

Due to a series of hearings on the retention application, the bankruptcy court had not entered a retention order. In the meantime, however, Judge Brinkema said that the debtor's firm "filed numerous pleadings on [the debtor's] behalf in both the main case and the adversary proceeding, including an opposition to the motion to convert."

Less than four months after filing, the bankruptcy court granted the creditor's summary judgment motion recognizing the validity of the debt and converting the case to chapter 7 one week later. There still had been no retention order.

After conversion, the firm filed an application for a final allowance of about $22,000 in compensation covering the period until the day before conversion to chapter 7.

Based on *David*, the debtor opposed the compensation application, contending there was no right to compensation in the absence of a retention order. The debtor also contended that the firm's services conferred no benefit on the estate.

The bankruptcy court granted about $20,000 in compensation, allowing counsel to draw on a disclosed retainer of $17,500 paid by third parties. The remainder would be an expense of administration in the chapter 11 case.

The debtor appealed.

David Distinguished, Compensation Allowed

On the question of whether a court could allow compensation when there was no retention order, Judge Brinkema said,

> [T]his Court has not located a single case addressing the unique facts at issue in this appeal — namely, whether a bankruptcy court may award fees to the Chapter 11 debtor's attorney where a proper employment application was filed at the beginning of the representation but where the bankruptcy court did not enter an order approving the application when it was filed and before counsel began working for the debtor.

Given the debtor's reliance on the Fourth Circuit's split decision in *David*, Judge Brinkema laid out the facts of the *David* case.

In *David*, a chapter 7 trustee had obtained an order approving the retention of counsel. When the case converted to chapter 11, the chapter 7 trustee became the chapter 11 trustee. As chapter 11 trustee, the trustee never filed an application for the continued retention of the same counsel in the chapter 11 case.

The chapter 11 case converted to chapter 13, with a new trustee. The prior trustee's counsel filed an application for compensation for services performed in the chapter 11 case. Judge Brinkema described the majority in *David* as having "held that the *former* trustee could not file a retroactive employment application under § 327(a)." [Emphasis added.]

Judge Brinkema identified how the "*David* court did not address whether an application for attorney's fees could be approved months after the law firm began providing legal services to the debtor." She noted how the "Fourth Circuit recognized that many circuits permit the retroactive approval of § 327(a) employment applications."

In *David*, Judge Brinkema said, the majority recognized that counsel's equity-based arguments "would have been 'compelling' but for the problem that the efforts to seek retroactive approval of the employment application were undertaken by the former trustee, rather than the current trustee."

Judge Brinkema distinguished the facts on appeal with those in *David*. The firm in the appeal, she said, fully complied with rules regarding retention applications. Furthermore, the bankruptcy court was "fully aware of the firm's work, and the court ultimately found that the fees requested were reasonable." To read ABI's report on *David*, click here.

"Simply put," Judge Brinkema said, "it would be unjust to deny fees to an attorney who worked 'in good faith' at the behest of the debtor-in-possession 'with the knowledge and acquiescence of the bankruptcy court.'"

"[B]ecause a proper application under § 327(a) to employ the [firm] was filed at the beginning of the representation," Judge Brinkema held that "the bankruptcy court did not err in granting the firm's Fee Petition, even though the bankruptcy court had not issued a formal order granting the application for employment."

Identifying no error in the bankruptcy court's findings of fact regarding the fee application, Judge Brinkema affirmed the bankruptcy court's order allowing compensation.

The opinion is *Schultz v. Martin Law Group PC*, 25-1598 (E.D. Va. April 21, 2026).

Estate Property

ROCHELLE'S DAILY WIRE

Majority of courts hold that the temporal limitation on inheritances in Section 541(a)(5) is nullified in chapter 13 by Section 1306(a).

An Inheritance Received More than 180 Days After Filing Is Chapter 13 Estate Property

Joining what she called the "vast majority of courts," Bankruptcy Judge Rachel M. Blise of Milwaukee decided that an inheritance received more than 180 days after filing becomes part of the chapter 13 estate and may occasion an increase in payment to creditors under a chapter 13 plan.

After the debtor confirmed her chapter 13 plan, she received a $70,000 inheritance more than 180 days after filing. The chapter 13 trustee filed a motion to dismiss the case because the debtor had not moved to modify her plan to increase payments to creditors on account of the inheritance.

Neither the trustee nor the debtor moved to modify the plan. The debtor opposed dismissal, contending that the inheritance did not come into the estate under Section 541(a)(5).

The subsection provides that the estate includes:

> Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date — (A) by bequest, devise, or inheritance.

To the debtor's way of thinking, the inheritance did not come into the estate because she acquired the right to the inheritance more than 180 days after her chapter 13 filing.

Seventh Circuit Law

Judge Blise responded to the debtor's reliance on Section 541(a)(5) by citing Section 1306(a) and saying that estate property in chapter 13 "is broader and includes property acquired post-petition." The subsection says that estate property in chapter 13 "includes, in addition to the property specified in section 541 of this title — (1) all property of the kind specified in such section that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted . . . ."

Regardless of Section 1306(a), the debtor took the position that finality of the confirmed plan barred the court from modifying the plan. Citing *Black v. United States Postal Service (In re*

Heath), 115 F.3d 521 (7th Cir. 1997), Judge Blise said that "the Seventh Circuit has held that a confirmed plan may be modified to reach property acquired post-confirmation that is not property of the estate before the modification."

Citing *Heath* and *Germeraad v. Powers (In re Powers)*, 826 F.3d 962, 971 (7th Cir. 2016), Judge Blise said that "a trustee can propose a modified plan that would increase plan payments to reach" wages or other property that comes into the estate after confirmation. To read ABI's report on *Powers*, click here.

Estate Property or Not?

The debtor had taken the position that Section 1306(a)(1) brought with it the 180-day limitation contained in Section 541(a)(5). Before reaching the question of modifying the confirmed plan, Judge Blise addressed the issue of whether the estate included the bequest.

Whether the bequest becomes estate property "ought to be settled by *In re Lybrook*, 951 F.2d 136 (7th Cir. 1991)," Judge Blise said. In *Lybrook*, the case had converted from chapter 13 to chapter 7, but the debtor had received an inheritance of farmland more than 180 days after filing.

The Seventh Circuit held that the farmland became property of the chapter 7 estate because "[t]here is no 180-day limitation." *Id*. at 137. Judge Blise therefore decided that *Lybrook* was "controlling" because the Seventh Circuit had held "that an inheritance received more than 180 days after the petition date becomes property of a chapter 13 bankruptcy estate."

Were *Lybrook* not binding authority, Judge Blise said she "nevertheless would conclude that a post-petition inheritance received more than 180 days after the petition date is property of the bankruptcy estate under § 1306(a)(1)."

Judge Blise said that Section 1306(a)(1) is itself a temporal provision extending the estate's reach until the case is closed, dismissed or converted. "Section 1306(a)(1) necessarily must nullify the time limitation in § 541(a)(1), or it would have no effect," she said.

Citing the Fourth Circuit, along with the Bankruptcy Appellate Panels for the Ninth and Tenth Circuits, Judge Blise said she joined the "vast majority of courts that have addressed the issue [and] likewise have concluded an inheritance received more than 180 days after the petition date is part of the chapter 13 bankruptcy estate by virtue of § 1306(a)(1)." Contrary decisions from bankruptcy courts, she said, "are unpersuasive."

Judge Blise held that the inheritance received "more than 180 days after the petition date is or could be property of the bankruptcy estate under §§ 541(a)(5) and 1306(a)(1)."

Amend the Plan or Not?

Even if the inheritance were estate property, the debtor argued that the plan could not be amended. That question, Judge Blise said, was "resolved" by *Powers*, *supra*. She quoted the Seventh Circuit for holding "that 'a trustee or an unsecured creditor may seek modification when the debtor's financial circumstances change after confirmation and result in the debtor's having the ability to pay more.'" *Powers, supra,* 826 F.3d at 974.

Judge Blise read *Powers* to mean that "the trustee in this case could likewise propose an additional distribution to creditors on account of [the debtor's] newly acquired assets if the new assets caused a change in her financial circumstances." However, she said that amending a plan is addressed to the discretion of the court and entails a "fact-intensive" analysis. She cited a case where the bankruptcy court decided that an inheritance was estate property but allowed the debtor to use almost half for home repairs.

Judge Blise said she had only decided the "legal question" of whether the trustee could move for a plan modification based on receipt of the inheritance. However, no one had moved to modify the plan. If there were a modification motion, she said that modifying the plan was "a factual matter [that] remains to be shown."

Judge Blise denied the motion to dismiss without prejudice.

The opinion is *In re Ulness*, 23-11345 (Bankr. W.D. Wis. Feb. 11, 2026).

Claims

ROCHELLE'S DAILY WIRE

The Seventh Circuit dissenter does not believe that purchasers of tax claims have tax claims and should have interest rates under Till, not at 18%.

Split 7th Circuit: Purchasers of Tax Claims Have Secured Tax Claims at 18%

In a split decision, the Seventh Circuit majority decided that the purchaser of a tax claim in Illinois holds a secured tax claim under Section 511 entitled to interest at 18% under a chapter 11 plan.

The dissenter made a cogent argument that that it isn't a tax claim and that the interest rate should be determined under *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004). The dissenter believes that the majority gave the creditor an "unreasonably high interest rate that bears no connection to the economic realities of the claim and the risks of nonpayment" and makes "Chapter 13 bankruptcy relief more oppressive than it should be."

The circuit majority affirmed Bankruptcy Judge Donald R. Cassling of Chicago, who retired in January.

No Payment Before Redemption

The debtor had not paid real estate taxes for three years before bankruptcy.

Illinois law imposes a lien on real property beginning on January 1. Payments extinguish the lien. If unpaid, state law eventually permits the county to foreclose the lien by selling the claim. An entity that we shall refer to as the purchaser bought the claim for the debtor's unpaid taxes.

State law permitted the debtor to redeem the property by paying the buyer the unpaid taxes plus "any penalty interest."

The debtor filed a chapter 13 petition one week before the redemption period expired. The debtor filed a plan to pay the purchaser's secured claim under Section 1325(a)(5)(B)(ii), meaning that the debtor was obliged to pay the purchaser "the value [of the claim], as of the effective date of the plan . . . ."

As Circuit Judge Michael Y. Scudder, Jr., said for the majority in his July 16 opinion, the debtor was required to pay interest because the claim would be paid over time, not in a lump sum on confirmation. The debtor and the purchaser couldn't agree on the interest rate.

Bankruptcy Judge Cassling pegged the claim as a secured tax claim under Section 511 entitled to interest at 18%. The circuit agreed to hear a direct appeal.

It's a Tax Claim

To peg the proper interest rate, the circuit was first required to determine the nature of the claim. The parties disputed whether it was a tax claim under Section 511(a). The subsection requires that "the payment of interest on a tax claim . . . shall be the rate determined under applicable nonbankruptcy law."

Although "tax claim" is not defined in the statute, Judge Scudder saw "no indication that Congress intended in § 511(a) to do anything other than extend that broad definition to a particular type of claim — a 'tax claim.'"

Judge Scudder said that his observation did not answer the question because the purchaser was not a taxing authority. Nonetheless, he said that the purchaser's "right to receive [the debtor's] payment of his overdue property taxes . . . suffices to give it a 'tax claim' within the meaning of § 511(a)." He went on to say that the circuit's decision in *In re LaMont*, 740 F.3d 397 (7th Cir. 2014), "reinforces this conclusion" by suggesting that claims of the sort are tax claims.

Having decided that the purchaser held a tax claim, Judge Scudder turned to the question of the proper interest rate under Section 511. Although Illinois law did not answer the question directly, he looked at three possibilities, none of which fit the circumstances exactly.

Judge Scudder decided that the best fit was the delinquent tax rate of 18% that applies to accrue interest on unpaid taxes when counties forego tax sales, because the purchaser "effectively steps into the position of the county" and will ultimately receive payment. He admitted that the purchaser and the county are "not situated exactly the same way within Illinois' complex property tax scheme." He went on to say,

> But they do not need to be for us to resolve the question before us . . . . This is sufficiently analogous to the situation Cook County would find itself in had there been no tax sale.

Judge Scudder affirmed the bankruptcy court, holding,

> [T]he best answer to what interest rate applies to a "tax claim" under § 511(a) comes from the "nonbankruptcy law" supplied by the Illinois General Assembly in 35 ILCS 200/21-15. That rate, in this instance, is 18% per year — a conclusion that aligns with recent bankruptcy court decisions that have confronted this same knotty question at the intersection of the Illinois Property Tax Code and the Bankruptcy

Code. *See*, *e.g.*, *In re McGuire*, 653 B.R. 558, 561 (Bankr. N.D. Ill. 2023)] [Thorne, Bankr. J]; *In re Drake*, 638 B.R. 96, 104 (Bankr. N.D. Ill. 2022) [Cleary, Bankr. J.].

The Dissent

Circuit Judge David F. Hamilton "respectfully" dissented. His opening paragraph reads, in part,

> The choice of the correct interest rate here requires the court to pick one of several square pegs to fit into a round hole. The majority, unfortunately, has chosen the worst of the alternatives. It makes Chapter 13 relief more difficult to achieve than it should be. It requires the debtor to pay this oversecured creditor a windfall, an unreasonably high interest rate that bears no connection to the economic realities of the claim and the risks of nonpayment. In fact, for a tax purchaser . . . , nonpayment is not a risk at all.

Judge Hamilton saw two mistakes. In his view, it was not a tax claim, and the interest rate should be determined under *Till*.

Regarding status as a tax claim, Judge Hamilton said that the purchaser's claim was not for taxes because the payment will "not benefit the county and cannot be used for any public purpose." He also based his decision on state law.

Under Illinois law, Judge Hamilton said the tax sale extinguished the county's tax lien and that the lien was not transferred to the purchaser, nor was the purchaser a subrogee. Rather, he said that "the tax purchaser obtains its own new, 'unique' statutory bundle of rights." As he read the decision, *LaMont* did not decide that it was a tax claim.

Instead, Judge Hamilton said he "would hold that the tax purchaser's interest is not a 'tax claim' at all" and that "a market interest rate under the *Till* method should apply to protect the value of the creditor's claim without giving it a windfall from an excessive interest rate."

Judge Hamilton did not see the state statute as "applicable nonbankruptcy law" because the 18% rate "never applies after the redemption period has run. Outside of bankruptcy, a tax purchaser is *never* entitled to that interest rate. *Only* the county can ever receive the 18% interest rate." [Emphasis in original.]

Judge Hamilton concluded that "there simply is *no* 'applicable nonbankruptcy law' that sets an interest rate for [the purchaser] under these circumstances." Instead, he would have used the "well-tested methods under *Till* [to] provide a workable solution unless and until the Illinois

General Assembly sees fit to amend somehow its property tax sale procedures in a fashion that creates law that is 'applicable' in the situation we face here."

The opinion is *In re Romero*, 25-2021 (7th Cir. July 16, 2026).

Narrowing judicial immunity for trustees in the Ninth Circuit will alter trustees' behaviors and require additional court filings and services.

En Banc, the Ninth Circuit Narrows Trustees' Judicial Immunity

Sitting *en banc*, the Ninth Circuit narrowed bankruptcy trustees' judicial immunity in the course of laying out the differences between the two versions of judicial immunity, namely, quasi-judicial immunity and derived judicial immunity.

For bankruptcy trustees to protect themselves from personal liability for simple negligence, the May 7 *en banc* opinion by Circuit Judge Jacqueline H. Nguyen means that trustees must meticulously document their findings in court filings by laying out the facts and legal rationale for proposed actions. Making conclusions and seeking relief without explanation will not confer judicial immunity, nor will disclosure without court approval.

In sum, a trustee's immunity now has the trappings of issue preclusion, at least in the Ninth Circuit.

Judge Nguyen nevertheless "doubt[ed] that subjecting trustees to liability for negligence will dissuade potential trustees from serving in that role," because trustees have protection from the business judgment rule and "can further limit [their] liability by filing regular reports of the estate's management."

Ninth Circuit Law on Immunity Is Jumbled

The appeal involved a long and complicated chapter 7 case. To comprehend the legal issues, understand that the chapter 7 estate included income-producing real property that was arguably over-encumbered. The trustee decided not to manage the property and collect rents, presumably because chapter 7 trustees, generally speaking, are not obliged to manage encumbered property for the benefit of lenders.

The trustee's position that the property was burdensome was seemingly ratified when the bankruptcy court authorized the trustee to abandon the property.

Years after the property was abandoned, creditors sued the chapter 7 trustee in bankruptcy court, alleging that the trustee had breached her fiduciary duty by allowing the property to deteriorate and by failing to collect rent. The bankruptcy court dismissed the complaint based on the statute of limitations. The bankruptcy court also decided that the trustee was entitled to dismissal based on qualified judicial immunity.

The bankruptcy judge reasoned that the complaint only alleged simple negligence, protected by qualified judicial immunity. For personal liability, the bankruptcy judge believed that the complaint must have plead gross negligence.

The creditors appealed. The district court reversed dismissal based on the statute of limitations but agreed that the trustee was protected by qualified judicial immunity. The district court remanded, allowing the creditors to amend the complaint by stating a claim for gross negligence that would not invoke judicial immunity.

The creditors appealed to the Ninth Circuit. A three-judge panel heard oral argument on June 11, 2025. Three months after argument, the panel entered a one-page order saying, "There has been a *sua sponte* request for an *en banc* vote in this case." The panel called for further briefing "on whether the matter should be heard *en banc*." In November 2025, the chief circuit judge "ordered that this case be heard *en banc*."

The circuit apparently felt compelled to sit *en banc* given the circuit's differing and possibly conflicting authorities about the nature and extent of a bankruptcy trustee's judicial immunity. Judge Nguyen even said that the Ninth Circuit's caselaw "has not always been a model of clarity."

After the filing of an amicus brief by the National Association of Bankruptcy Trustees, an 11-judge *en banc* panel heard oral argument on January 13. To read ABI's report on the call for an *en banc* hearing, click here.

Appellate Jurisdiction

Judge Nguyen first dealt with the circuit's appellate jurisdiction because the district court had remanded and given the creditors an opportunity to amend the complaint with the aim of surviving another motion to dismiss. On its face, the district court's order was not final because the remand was not for merely "mechanical tasks."

Applying the circuit's four-factor test, Judge Nguyen said that "the district court's remand order does not appear final." However, the creditors' counsel told the *en banc* panel at oral argument that it "is standing on the complaint rather than seeking leave to amend in the bankruptcy court."

"In light of counsel's representation that [the creditors] will not amend the complaint," Judge Nguyen decided that "the district court's order is effectively final," and we "have jurisdiction under § 158(d)(1)" because " there is nothing left to be done but for the bankruptcy court to enter another judgment dismissing the complaint with prejudice and the district court to affirm."

Two Brands of Immunity: Overview

On the merits regarding judicial immunity, Judge Nguyen said she was writing to "clarify the nature and limits of those immunities." She began with an overview by saying that a creditor aggrieved by a trustee's actions "can seek redress against the trustee in her official or personal capacity." If the suit is against the trustee in the trustee's official capacity, she said that "any award will be paid from the estate."

"In personal capacity suits, absent a basis for immunity," Judge Nguyen said that "the trustee is personally liable for her intentional and negligent torts." So that people won't eschew serving as a trustee, she said that "courts provide 'ways by which a trustee may effectively protect [her]self against personal liability.'"

When trustees "are acting *like* judges or *for* judges," Judge Nguyen said that "bankruptcy trustees may be entitled to immunity," citing *In re Castillo*, 297 F.3d 940 (9th Cir. 2002). [Emphasis in original.] That brand of immunity, she said, is "known as 'quasi-judicial immunity,' [and it] provides trustees absolute immunity from liability for 'functions involving the exercise of discretionary judgment' that are 'essential to the authoritative adjudication of private rights to the bankruptcy estate.'"

The second species of immunity, Judge Nguyen said, "is referred to as 'derived judicial immunity' or simply 'derived immunity.'" It provides that a "trustee will not be held liable when (1) her acts were within the scope of her authority; (2) the debtor, creditors, and other interested parties had notice of the proposed acts; (3) the trustee candidly disclosed the proposed acts to the bankruptcy court; and (4) the bankruptcy court approved the acts."

Summarizing the difference between the two versions, Judge Nguyen said,

> Quasi-judicial immunity shields a trustee who acts without court authorization when performing judge-like actions, and derived immunity protects a trustee who performs court-sanctioned acts even when the acts are non-adjudicative in nature.

Quasi-Judicial Immunity

Judge Nguyen next attempted to synthesize Ninth Circuit precedent on quasi-judicial immunity, which applies when a trustee "'is performing an integral part of the judicial process,' *Lonneker Farms, Inc. v. Klobucher*, 804 F.2d 1096, 1097 (9th Cir. 1986)." There was a "sea change" seven years later when the Supreme Court "'change[d] in the way in which we are to examine absolute quasi-judicial immunity for nonjudicial officers'" and "rejected our approach to immunity in which nonjudicial officers receive immunity merely 'because they are 'part of the judicial function,'" citing *Antoine v. Byers & Anderson, Inc.*, 508 U.S. 429 (1993).

Judicial immunity applies to nonjudges when there "has been 'performance of the function of resolving disputes between parties, or of authoritatively adjudicating private rights.'" Immunity then applies because trustees, "too, 'exercise a discretionary judgment' as a part of their function."

"To determine whether a bankruptcy trustee is entitled to quasi-judicial immunity," Judge Nguyen cited *Castillo* for saying that "'we must examine the particular function . . . at issue,'" while keeping in mind that the Supreme Court has said that the application must be "quite sparing." Quasi-judicial immunity applied in *Castillo* because it involved scheduling and giving notice of hearings.

Derived Immunity

Judge Nguyen said that derived immunity arose from trustees' practices of seeking instructions from the court. She said, "[W]e held that derived immunity protects a trustee who 'act[s] under the authority of the bankruptcy judge.'"

The Ninth Circuit "expanded the doctrine," Judge Nguyen said, in *Bennett v. Williams*, 892 F.2d 822, 832 (9th Cir. 1989), where the circuit "explained that a bankruptcy trustee 'has a duty to preserve the assets of an estate' and must 'exercise that measure of care and diligence that an ordinarily prudent person would exercise under similar circumstances.'"

When a trustee might be liable for negligence, Judge Nguyen said, "we identified 'certain standards' that, if met, will immunize her." She listed the four requirements:

> (1) [H]er acts must have been within the scope of her authority; (2) the interested parties must have had notice of the proposed acts; (3) she must have candidly disclosed the proposed acts to the bankruptcy court; and (4) the bankruptcy court must have approved the acts.

Judge Nguyen made a point of saying, "Notice to interested parties is still not enough." The disclosure must be candid, truthful and complete and must apprise "the bankruptcy court of all material facts that would bear on the court's decision, including facts that weigh against the proposed action." Of course, the trustee must obtain court approval for derivative immunity to apply.

Applying the Law to the Facts

Judge Nguyen said that the trustee's "failings" were "relatively modest in scope" because the trustee allegedly had allowed two real properties to deteriorate and had not demanded that tenants pay rent to the trustee and had not demanded that the debtor turn over rental income he had received. These functions, she said, "call upon the trustee to act as a property manager."

Therefore, Judge Nguyen held that quasi-judicial immunity did not apply. Similarly, she held that the trustee was not entitled to derivative immunity because there were "no orders in the bankruptcy docket authorizing [the trustee's] inaction in that regard."

A Trustee's Other Defenses

Judge Nguyen said she had "two responses" to the concern expressed in the *amicus* brief of the NABT that liability for negligence could discourage people from serving as bankruptcy trustees.

Although negligence is enough to confer liability, Judge Nguyen doubted, as "a practical matter," that "subjecting trustees to liability for negligence will dissuade potential trustees from serving in that role," because the trustee "can invoke the business judgment rule" as a defense to liability.

Judge Nguyen said that a trustee "can further limit her liability by filing regular reports of the estate's management, thereby placing on creditors 'the burden of raising their objections.'"

If the "trustee 'account[s] at prompt intervals'" and the creditor "fails to timely object to the trustee's actions, then the creditor may be estopped from mounting a collateral attack," Judge Nguyen said.

"And when a creditor brings factually or legally baseless claims against the trustee for her administration of the estate," Judge Nguyen said that "the trustee can always seek sanctions, including 'all or part of the reasonable attorney's fees and other expenses.' Fed. R. Bankr. P. 9011(c)(4)(A)(iii); *see Law v. Siegel*, 571 U.S. 415, 427 (2014)."

Reversed and Remanded

Judge Nguyen reversed and remanded where the trustee would be "free to raise derived immunity as a defense if she believes she can make the necessary showing." She denied the creditors' request for the case to be assigned to a different bankruptcy judge on remand.

Observations

The opinion is required reading for trustees and anyone involved with trustee liability. The Ninth Circuit opinion is or may become law in other circuits.

To the Ninth Circuit's credit, the opinion disentangles the often-conflated issues of quasi-judicial and derivative immunity.

To fend off liability when a trustee and a creditor disagree about the proper course of action, the trustee could respond by offering to retain counsel on a contingency. If counsel are unwilling to undertake a matter on a contingency, the inability to engage counsel is good if not compelling evidence that an action is unnecessary.

Or, a trustee could offer to allow the creditor to buy a claim from the estate or pursue a matter for the benefit of the estate, with compensation limited to a portion of recoveries for the estate.

The more narrow scope of immunity may prompt trustees to examine the sufficiency of insurance coverage. For sure, the opinion will prompt more frequent and more detailed court filings, thus increasing the trustee's labor, but without a commensurate increase in compensation. The nature of the additional work may allow compensation for trustees' counsel, at the expense, however, of a lower return to creditors. In no-asset cases, the trustee and counsel will bear the additional expense.

The opinion is *Phillips v. Goldman (In re Gilman)*, 24-2249 (9th Cir. May 7, 2026).

Transferring ownership of the debt to the creditor after the filing of the claim didn't establish ownership of the claim on the claim-filing date and led to disallowance of the claim.

A Creditor Must Own the Claim When Filing the Proof of Claim, Eleventh Circuit Says

The Eleventh Circuit made a strict rule based on state foreclosure law: A secured claim will be disallowed if the entity that files the proof of claim didn't acquire ownership of the underlying note and mortgage until after filing the proof of claim.

The corporate debtor in chapter 7 owned real properties. The bankruptcy court approved the sale of the properties "free and clear," with liens and claims attaching to the proceeds. The bankruptcy court ordered that claims to the proceeds must be filed within 30 days.

An entity that we shall call the purported owner filed proofs of claim for three of the properties, attaching the mortgages. Although Circuit Judge Gerald B. Tjoflat didn't say so explicitly in his July 24 opinion, it appears as though the mortgagees appearing on the mortgages were not the purported owner who filed the proofs of claim.

The purchaser of the properties objected to all three claims, saying that the claims did not attach the notes or other evidence that the debt was owing to the purported owner. As it turned out, the notes were not payable to the purported owner but were payable to the entity shown as the mortgagee.

Although not contesting the existence of the debt, the buyer moved for summary judgment, asserting that the purported owner did not have standing to file the claims.

It turned out that the mortgagees had transferred and assigned the mortgages and the notes to the purported owner after the filing of the proofs of claim. Although not said in Judge Tjoflat's opinion, the claimant evidently did not move to amend the proofs of claim as filed.

Bankruptcy Judge Catherine Peek McEwen granted summary judgment in favor of the buyer, disallowing all three claims. As Judge Tjoflat put it, Judge McEwen decided that the purported owner "did not have an interest in the promissory notes and mortgages at the time it filed the claims."

Affirmance in the district court brought the appeal to the Eleventh Circuit.

Claimant Must Have the Power of Enforcement

Reviewing the grant of summary judgment *de novo*, Judge Tjoflat said that state law governs the validity of claims in bankruptcy. In Florida, he said that "a party must be the owner or holder of a note to foreclose on the property attached to it." He therefore concluded that "a party must also be the owner or holder of a note to file a claim based on it in bankruptcy" and that "a party has no claim before it owns the note."

It was therefore "obvious" to Judge Tjoflat that "a proof of claim must show the debt is owed to the claimant at the time it files the claim." Because "the true owners of the mortgages and notes failed to file claims by the deadline is what makes them unenforceable now," he said.

Since there was "no evidence" that the purported owner had owned the notes and mortgages "on the date it filed its claims," Judge Tjoflat affirmed the order of the district court upholding disallowance of the claims.

In a footnote, Judge Tjoflat rejected the purported owner's "appeals to equity." He explained,

> Though bankruptcy courts are courts of equity, they "are not authorized in the name of equity to make wholesale substitution of underlying law controlling the validity of creditors' entitlements." The underlying law here is that a party must own a note before it is entitled to enforce it. We cannot look past that. [Citations omitted.]

The opinion is *Bay United Holdings LLC v. INXS 7 LLC (In re Aegis Asset Management LLC)*, 25-10331 (11th Cir. July 24, 2026).

Alleging that the lender failed to credit payments under a chapter 13 plan states a claim for violation of the discharge injunction, Ninth Circuit says unanimously.

Ninth Circuit Majority Says Emotional Distress Damages Survived *Taggart*

In a split decision, the Ninth Circuit majority affirmed the Bankruptcy Appellate Panel by holding that a claim for intentional infliction of emotional distress from a violation of the discharge injunction survived the Supreme Court's *Taggart* decision.

The Ninth Circuit's nonprecedential, *per curiam* decision on April 20 was unanimous on the more mundane point that a debtor asserts a claim for violation of the discharge injunction by alleging that the lender failed to credit payments under a chapter 13 plan.

Notably, the circuit panel used the word "agree" eight times in concurring with the BAP.

Arrears Paid in Full

In 2014, a couple confirmed a chapter 13 plan in one month. The debtors filed a claim when the home mortgage lender didn't. The claim filed by the debtors asserted that the arrears on their home mortgage were about $19,000. The lender never filed an amended claim.

The plan called for curing the $19,000 in arrears during the life of the chapter 11 plan and paying the mortgage currently. At the end of the 60-month plan, the debtors had paid some $166,000, more than the $165,500 called for under the plan.

The chapter 13 trustee filed a notice of final cure payment. The lender responded with a statement saying that the debtors had paid the arrears in full and that the debtors were current on postpetition payments.

The trustee filed a final report, and the debtors received their discharges.

After discharge, the lender began rejecting the debtor's monthly mortgage payments and claimed that the mortgage was delinquent by more than $10,000. The debtors filed an adversary proceeding in bankruptcy court.

The debtors' complaint alleged that the lender had violated the discharge injunction under Section 524(a)(2) by failing to credit the mortgage payments they made after discharge. The complaint sought damages for intentional infliction of emotional distress.

The lender responded with a motion to dismiss, which the bankruptcy court granted. *Valdellon v. Wells Fargo Bank N.A. (In re Valdellon)*, 659 B.R. 377 (Bankr. E.D. Cal. April 30, 2024). To read ABI's report, click here.

The bankruptcy court reasoned that the failure to credit post-discharge payments could not be in violation of Section 524(i), which deals with payments under a plan. The bankruptcy court also believed that *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), obviated the possibility of having emotional distress damages for a discharge violation. To read ABI's report on *Taggart*, click here.

The BAP reversed in an opinion by Bankruptcy Judge Scott H. Gan. *Valdellon v. PHH Mortgage Corp. (In re Valdellon)*, 665 B.R. 420 (B.A.P. 9th Cir. Dec. 20, 2024). To read ABI's report, click here.

Reversing, the BAP held that the debtors' complaint had stated a claim for relief under § 524(i), which provides:

> The willful failure of a creditor to credit payments received under a plan confirmed under this title . . . shall constitute a violation of an injunction under subsection (a)(2) if the act of the creditor to collect and failure to credit payments in the manner required by the plan caused material injury to the debtor.

The BAP went on to hold that *Taggart* did not preclude compensatory damages for emotional distress caused by willful violations of the discharge injunction.

The lender appealed to the circuit.

Appellate Jurisdiction

Because the BAP reversed and remanded for further proceedings, the circuit panel first addressed appellate jurisdiction. Facially, the BAP opinion was not final because the bankruptcy court was directed to conduct the adversary proceeding from the beginning.

The panel said that a BAP order "is considered final 'where it 1) resolves and seriously affects substantive rights and 2) finally determines the discrete issue to which it is addressed.'" When a BAP has remanded, the panel listed four factors to consider.

The panel decided there was appellate jurisdiction because "our resolution of the legal questions raised on appeal would avoid piecemeal litigation and prevent the parties from later climbing back up the appellate ladder on the same issues."

A Willful Stay Violation

On the merits, the circuit panel unanimously "agree[d] with BAP that the Bankruptcy Court erred in concluding that Debtors failed to state a claim under § 524(i) for contempt sanctions. Creditors may not willfully fail to credit payments received under a bankruptcy plan unless the plan is in default." More particularly, the panel said that the debtors' complaint "sufficiently alleged that they had cured arrears with total payments of [$19,000]."

Regarding a willful violation of the discharge injunction, the circuit panel unanimously agreed that the "alleged misapplication of . . . payments to pre-petition arrears rather than to the monthly mortgage payment is sufficient to allege a willful misapplication of payments under the plan under § 524(i)."

Taggart

Turning to *Taggart*, the panel analyzed whether the lender had "an objectively reasonable basis" for believing that the loan was in default. Again, the panel unanimously "agree[d] with BAP that [the lender] lacked an objectively reasonable basis to declare Debtors in default following the bankruptcy discharge. Creditors' own alleged miscrediting undermines any fair ground of doubt."

Next, the panel majority addressed the question of whether *Taggart* precluded an award for emotional distress damages by requiring bankruptcy court to "consider the 'old soil' of traditional civil contempt principles when evaluating their authority in bankruptcy contempt proceedings."

The panel majority read *Taggart* narrowly by saying that the Supreme Court "did not directly address what remedies, or measures of damages, are proper when a party is held in civil contempt by a bankruptcy court." The majority added, "*Taggart* provides no specific limitations on courts determining which civil contempt remedies prove appropriate in the bankruptcy discharge context."

The majority recounted how the BAP read Ninth Circuit authority as allowing bankruptcy courts to "award compensatory damages for emotional distress and that *Taggart* did not alter a bankruptcy court's authority to do so." *See Ocwen Loan Servicing, LLC v. Marino (In re Marino)*, 577 B.R. 772, 788-88 (B.A.P. 9th Cir. 2017), *aff'd in part & appeal dismissed in part*, 949 F.3d 483 (9th Cir. 2020).

The panel majority held that "*Taggart* did not effectively abrogate the holding in *In re Marino*, which we find persuasive."

The majority buttressed its conclusion by referring to *Leman v. Krentler-Arnold Hinge Last Co.*, 284 U.S. 448 (1932), and saying that the "Supreme Court concluded that an award for lost profits was an available contempt remedy in a patent-infringement case despite the fact that lost profits clearly could be distinguished from pecuniary damages." The majority elaborated,

> The same reasoning dictates that full and equitable relief in the bankruptcy discharge context allows potential damages for emotional distress and that civil contempt law permits such an award of nonpecuniary damages. We base this conclusion partially on *Leman's* guidance that civil contempt aims to compensate a party fully for their damages, and partially on the fresh start purpose behind bankruptcy discharge.

The majority offered yet another rationale for allowing emotional distress damages by "conclud[ing], in the alternative, that nonpecuniary damages are available based on traditional civil contempt principles."

The majority affirmed the BAP "in full" by "declining to conclude that emotional distress damages are categorically unavailable."

The Dissent

Circuit Judge Ryan D. Nelson "respectfully" dissented in part. He agreed "that the Bankruptcy Court erred by dismissing the claim for sanctions under § 524(i) and that Creditors lacked an objective reasonable basis for asserting default."

Judge Nelson did not agree "that the Bankruptcy Court can award compensatory damages for emotional distress." He saw *Taggart* as having abrogated *Marino*.

The majority on the panel were Circuit Judge Milan D. Smith, Jr., and Chief District Judge Brian M. Morris, sitting by designation.

The opinion is *PHH Mortgage Corp. v. Valdellon*, 25-538 (9th Cir. April 20, 2026).

Bankruptcy Judge Timothy Barnes explained why surrendering property alone does not divest a debtor of title, or of future liability.

Surrendering Property in Chapter 13 Doesn't Insulate a Debtor from Future Liability

Bankruptcy Judge Timothy A. Barnes of Chicago explained why surrendering property alone does not insulate a debtor from claims that may arise later in connection with the property. His April 10 opinion shows how the Bankruptcy Code has a gaping hole that can deprive someone of comprehensive debt relief, but only for claims arising in the future.

A couple filed a chapter 13 petition in 2010 and confirmed a plan that surrendered their home. Specifically, the plan "surrendered their interest in the property . . . to" the secured lender and the City of Chicago. Adopting Section 1325(a)(5)(C), the plan said that the lender and the City "shall look solely to said collateral in payment of their secured claim."

Neither the lender nor the City objected to the plan or to confirmation. The debtors received a discharge.

Fifteen years later, the couple filed another chapter 13 petition. In their schedules, the debtors said that they remained in title because the lender had not foreclosed. They declared that they had only bare legal title and claimed no interest in the property in view of the surrender in 2010. Their plan did not deal with the surrendered property in any fashion.

The City filed three claims in the new case relating to health and safety violations on the previously surrendered property. The City also objected to the plan. As Judge Barnes said, "the City argue[d] that the Debtors purport to shift the burdens of property ownership onto the local government."

The debtors responded to the City's plan objection by asserting that the City was precluded from asserting new claims against them because they had surrendered the property in the 2010 plan and the City had not objected to the prior plan or to confirmation of it.

Surrender Isn't a Transfer

Addressing the City's objection to the plan, Judge Barnes stated the issue as "whether the Debtors' surrender of the Property in the 2010 Plan, combined with their discharge from the 2010

Bankruptcy Case, changed their ownership status and released them from any liabilities associated with owning the Property."

Judge Barnes said that "surrender is not defined in the Bankruptcy Code, [and] the use of the term in section 1325 has given rise to much understandable confusion." He drew upon his own opinion in *In re Ware*, 533 B.R. 701, 706 (Bankr. N.D. Ill. 2015), where he had "defined 'surrender' as the relinquishment of all the rights the debtor has in the collateral, thereby allowing the creditor to take possession of the property, but not requiring delivery of the collateral to the creditor."

In the bankruptcy context, Judge Barnes said that "surrender is properly seen as a claims mechanism, not a transfer one." For surrender to result in a transfer, he said that "the creditor in question must accept it as such."

Because *Butner* holds that state law governs interests in property, Judge Barnes alluded to Illinois law, where "the courts have made clear that surrender requires voluntary acceptance." He found "[n]othing in the Bankruptcy Code [to suggest] that a debtor has the right to forcibly vest title of surrendered property in the secured creditor."

Judge Barnes turned to Section 1325(a)(5)(C), which the debtor was using to support the idea that the City had no claim in the new case. While Section 1325(a)(5)(C) allowed the debtor to treat the secured creditor's claims in the prior case as having been satisfied, he said that "surrender is a claims mechanism, [and that] any additional effect such as a transfer should only occur with the creditor's consent."

Furthermore, Judge Barnes said that the "creditor is free not to accept the surrender, in which case the collateral remains the debtor's."

Applying the law to the case at hand, Judge Barnes said that the debtors had only surrendered the property in 2010 and that the City had not accepted the surrender. He went on to cite caselaw for the notion that continued ownership could mean the debtor's continued liability for real estate taxes, insurance premiums and postpetition association fees.

Distinguishing between *in personam* and *in rem* claims, Judge Barnes said that the City's "*in personam* claims against the Debtors arising out of their continued ownership of the Property" are "potentially valid claims," assuming "such claims arose after the Debtors received their discharge in 2010."

Judge Barnes held "that the Debtors may remain liable for whichever claims by the City that might have arisen since the 2010 Bankruptcy Case." He sustained the City's objection to the plan and added that the debtors "are potentially responsible for all its accruing liabilities, including any validly asserted claims by the City arising out of their continued ownership of the Property."

Question

Because the debtors are still in title, do they need to surrender the home a second time, or is once enough?

The opinion is *In re Jones*, 25-10807 (Bankr. N.D. Ill. April 10, 2026).

ROCHELLE'S DAILY WIRE

The Tenth Circuit BAP holds that dismissal is not automatic and immediate when a chapter 13 debtor moves to dismiss voluntarily under Section 1307(b).

Two BAPs Now Uphold Sanctions Alongside Voluntary Dismissals Under Section 1307(b)

The Tenth Circuit Bankruptcy Appellate Panel joined the Ninth Circuit BAP in becoming the only appellate courts to hold that a chapter 13 debtor isn't entitled to immediate dismissal under Section 1307(b) to avoid the imposition of sanctions or conditions on dismissal.

In her nonprecedential opinion for the Tenth Circuit BAP on February 3, Bankruptcy Judge Sarah A. Hall said she was addressing "the all-too-frequently used, but rarely successful, scheme to preserve property interests on the eve of [foreclosure by] using a repeated pattern of transfers and bankruptcy filings."

To halt foreclosure of a home, the owner twice filed chapter 13 petitions. Both were dismissed. After the second dismissal, the owner transferred the home to another individual whom we shall refer to as the debtor.

Facing foreclosure, the debtor filed a chapter 13 petition. The day after filing, the lender filed a motion to modify the automatic stay. The day before the hearing on the stay-relief motion, the debtor filed a motion for voluntary dismissal under Section 1307(b).

At the hearing on the stay motion, the debtor argued that the bankruptcy court had no jurisdiction to modify the stay in view of his voluntary dismissal. Bankruptcy Judge Joel T. Marker (ret.) went ahead with the hearing and ruled that the case would be dismissed after entry of the stay modification order. The dismissal order also provided that the debtor would be barred from filing another petition for 180 days in view of Section 109(g)(2).

The debtor appealed.

Dismissal Isn't Automatic

Judge Hall stated the issue on appeal as being whether the bankruptcy court had jurisdiction to grant the stay motion before dismissing the case.

The outcome turned in large part on Section 1307(b), which reads:

> On request of the debtor at any time, if the case has not been converted under section 706, 1112, or 1208 of this title, the court shall dismiss a case under this chapter. Any waiver of the right to dismiss under this subsection is unenforceable.

Judge Hall said that Section 1307(b) is "generally regarded to confer upon a chapter 13 debtor an absolute right to dismiss." In the opinion of the "majority" of courts, she said that the "absolute right to dismiss is not subject to an implied condition of good faith and cannot be denied because of a pending motion to dismiss or convert for cause under § 1307(c)."

But there's more. Citing Bankruptcy Rule 1017(f)(2), Judge Hall said there are "specific procedures" for voluntary dismissal that include the filing and service of a motion. "While nothing in the Rules or Code requires a hearing when a debtor seeks to voluntarily dismiss a case under § 1307(b)," she saw nothing to suggest that "holding a hearing on such a motion or other matter prior to dismissal is prohibited." "Similarly," she said, "there is nothing in the Rules or Code … making § 1307(b) motions self-executing."

Judge Hall found a "consensus" of decisions by bankruptcy courts around the country finding that "dismissal is not required to be immediate or unconditional," although "a right to dismiss under § 1307(b) is absolute." Among the authorities she cited was *In re Duran*, 630 B.R. 797 (B.A.P. 9th Cir. 2021), where the Ninth Circuit BAP upheld dismissal with prejudice when the debtor had sought voluntary dismissal under Section 1307(b). In other words, moving under Section 1307(b) did not bar the bankruptcy court from attaching a sanction to dismissal. To read ABI's report on *Duran*, click here.

Judge Hall found "nothing in the Code or binding authority [that] prohibits a court from setting and conducting a hearing." Therefore, she held that the bankruptcy court "did not err in delaying entry of the Dismissal Order to consider and rule on the Stay Relief Motion." More specifically, she held that "a debtor's absolute right to dismiss under § 1307(b) is not required to be immediate or unconditional."

Judge Hall went on to find no error "in imposing filing restrictions in the Dismissal Order," because "§ 109(g)(2) would have operated to bar [the debtor] from filing another bankruptcy case for 180 days." She affirmed Bankruptcy Judge Marker.

The opinion is *Lopez v. Jenkins (In re Lopez)*, 25-2 (B.A.P. 10th Cir. Feb. 3, 2026).

A district court in New York affirmed Bankruptcy Judge Paek by holding that collection of a sanction for a stay violation doesn't require a writ of execution under Federal Rule 69(a).

Collecting a Sanction May Be Enforced by Contempt Rather than Writ of Execution

Affirming the bankruptcy court, a district judge in New York held that a monetary sanction for violation of the automatic stay may be collected by use of a contempt motion rather than through use of a writ of execution.

Last year, Bankruptcy Judge Kyu Y. Paek of Poughkeepsie, N.Y., held a creditor in contempt for ignoring the automatic stay and attempting to collect a $335 unsecured debt. The creditor had actual notice of the chapter 7 filing but did not appear to oppose the contempt motion. Judge Paek awarded the debtor punitive damages of $3,000 and about $2,500 in attorneys' fees. The contempt order required payment within 20 days.

When the creditor did not pay the $5,500 after having been served with the contempt order, the debtor filed a second contempt motion. The creditor appeared the second time but argued that the first contempt order was a money judgment that could only be enforced by writ of execution issued under Rule 69(a)(1), not by contempt. By time of the hearing, though, the creditor had paid the $5,500 but never appealed the first contempt order.

Judge Paek entered a second contempt order, directing the creditor to pay an additional $4,000 in compensation for the debtor's attorneys' fees incurred in prosecuting the second contempt motion.

Judge Paek held that a monetary sanction for contempt could be collected by a contempt motion, not only by use of a writ of execution. *In re Alexander*, 24-35982, 2025 BL 89241, 2025 Bankr. Lexis 651 (Bankr. S.D.N.Y. March 18, 2025). To read ABI's report, click here.

The creditor appealed, primarily contending that sanctions for stay violations must be enforced by a writ of execution. District Judge Cathy Seibel of White Plains, N.Y., affirmed in an opinion on January 9.

Rule 69(a)(1) Isn't for Contempt

Judge Seibel first alluded to F.R.C.P. 69(a)(1), made applicable by Bankruptcy Rule 7069. The rule says that a "money judgment is enforced by a writ of execution, unless the court directs otherwise." Citing the Ninth Circuit, she said that the "purpose of the rule is to 'restrict remedies on money judgments to legal process' and to avoid the use of the contempt power or other methods beyond those prescribed by state law 'except in cases where established principles so warrant.'"

Among several courts relied upon by Judge Paek, Judge Seibel quoted the Seventh Circuit for saying "that '[u]se of the contempt power is an appropriate way to enforce a sanction for misconduct, which is not an ordinary money judgment.'" She went on to say that Judge Paek "correctly" followed the Ninth Circuit Bankruptcy Appellate Panel for holding that "'willful failure to comply with an order constitutes misconduct [that] may be remedied via contempt sanctions.'"

Judge Seibel concluded that the case on appeal was

> analogous to the cases . . . where courts allowed parties to seek enforcement through contempt proceedings of fees imposed as sanctions for misconduct, and distinguishable from cases where courts found that fee awards imposed for other purposes must be enforced by writ of execution.

Like Judge Paek, Judge Seibel cited "some courts [that] have held that a sanctions order under § 362(k) is a money judgment that must be enforced by writ of execution." Picking the opinions apart one by one, Judge Seibel said she was "likewise unpersuaded by those cases," "largely for the reasons set forth by Judge Paek."

Judge Seibel affirmed Judge Paek, "holding that orders awarding fees as a sanction for misconduct are not money judgments and therefore can be enforced through contempt proceedings."

The opinion is *ProScript Pharmacy v. Alexander (In re Alexander)*, 25-3296 (S.D.N.Y. Jan. 9, 2026).

Student Loans

An Internal Revenue Code definition means that the bankruptcy court cannot make part of a private student loan dischargeable and another part nondischargeable.

Private Student Loans Are Discharged Entirely or Not at All, BAP Says

Unless all of a private student loan was used for "qualified higher education expenses," none of the loan is nondischargeable under Section 523(a)(8)(B).

The Ninth Circuit Bankruptcy Appellate Panel gave the following example in its February 27 *per curiam* opinion: The private lender made a $500,000 loan where $495,000 was for educational purposes and $5,000 went to purchase a car. Although none of the loan would be nondischargeable, the BAP said,

> The result may seem harsh, but the language of the statute is clear, and exceptions to discharge "are to be construed narrowly so that they are confined to their plainly-expressed terms."

Stiffing the In-Laws

A young man borrowed $331,500 from his in-laws to finance his medical school education. After graduating with a medical degree, he divorced his wife and refused to pay back his former in-laws, claiming it was a gift, not a loan. The in-laws sued and won a $331,500 judgment in state court.

After the newly minted doctor filed a chapter 7 petition, the in-laws filed a complaint seeking a declaration that the $331,500 loan was nondischargeable under Section 523(a)(8)(B). After trial, the bankruptcy court determined that some $267,000 was for educational purposes and was nondischargeable. The remainder was dischargeable.

The in-laws appealed and won in the BAP before a panel composed of Bankruptcy Judges Scott H. Gan, Frederick P. Corbit and Jennifer E. Niemann.

The Key Word Is 'Solely'

If the debt does not "impose an undue hardship," Section 523(a)(8)(B) provides that a debtor does not receive a discharge for "any other [private] educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual."

Drilling down, "qualified education loan" is defined in Section 221(d)(1) of the Internal Revenue Code as, among other qualifications, "any indebtedness incurred by the taxpayer *solely* to pay qualified higher education expenses . . . ." [Emphasis added.]

Synthesizing the statutes, the BAP panel said that "the loan is nondischargeable if it is a qualified educational loan, and a qualified educational loan must be incurred *solely* for the purpose of paying qualified higher education expenses." [Emphasis added.]

"The bankruptcy court's uncontested findings of fact demonstrate the loan was incurred for both qualified and unqualified education expenses," the panel said. The BAP therefore held that "it cannot be a qualified education loan."

The IRC Definition Controls the Outcome

Reaching a contrary conclusion, the bankruptcy court had read "any indebtedness" in Section 221(d)(1) to mean that the court could separately consider the portion of the loan used for qualified higher education expenses. The BAP disagreed for two reasons.

First, the BAP said,

> § 523(a)(8)(B) excepts from discharge "an educational loan that *is* a qualified education loan." (emphasis added). The statute leaves no room for a court to partition an educational loan and hold a portion nondischargeable. Either the educational loan is a qualified education loan, or it is not.

"Second," the BAP said, "the bankruptcy court's interpretation of IRC § 221(d) gives no effect to the term 'solely.'"

The panel therefore held that a "loan incurred for multiple purposes — and not solely to pay qualified higher education expenses — is not a qualified education loan."

The panel reversed and held that the loan was discharged "in its entirety," because the "Bankruptcy Code does not permit the court to hold a portion of a loan nondischargeable where the loan does not meet the statutory criteria."

The opinion is *Pearson v. Nichols (In re Pearson)*, 25-1086 (B.A.P. 9th Cir. Feb. 27, 2026).

Cross-Border Insolvency

The drafters of chapter 15 disagree with the Second Circuit's holding that Section 109 requires a chapter 15 debtor to have property in the U.S.

On a Split, Rhode Island Judge Says Property in the U.S. Isn't Required for Chapter 15

Sitting in the First Circuit, Chief Bankruptcy Judge John A. Dorsey, Jr., of Providence, R.I., was able to differ with the Second Circuit and followed the *Collier* treatise in concluding that Section 109 does not apply to chapter 15 debtors who need not have property in the U.S.

Judge Dorsey therefore held in his March 2 opinion "that Chapter 15 debtors do not have to meet § 109's eligibility requirements."

Foreign liquidators for five related companies filed chapter 15 petitions in Judge Dorsey's court seeking foreign main recognition under Section 1517. Three were in liquidation in Mauritius, and two were in liquidation in the British Virgin Islands.

The liquidators told Judge Dorsey that they were primarily seeking chapter 15 recognition to stay actions against them and to take control of accounts at a bank in Rhode Island. However, he said that "the Debtors were unable to clearly demonstrate whether or which Debtors have an interest in the Bank Accounts."

Although the petitions were evidently unopposed, Judge Dorsey analyzed whether venue was proper, whether the debtors were eligible for chapter 15 relief and whether other requisites for foreign main recognition were satisfied.

Venue

Section 1410(1) of Title 28 provides that a "case under chapter 15 of title 11 may be commenced in the district court of the United States for the district — (1) in which the debtor has its principal place of business or principal assets in the United States."

The debtors asserted that their principal assets were the bank accounts and a retainer on deposit with the liquidators' counsel in Rhode Island.

There being no binding First Circuit authority, Judge Dorsey said he was "persuaded by several Second Circuit cases which have found that retainer accounts provide a sufficient basis to fulfill Section 1410(1)'s requirements."

Although the debtors were unable "clearly" to demonstrate ownership of the bank accounts, Judge Dorsey held that venue was proper because "retainer accounts can independently satisfy Section 1410(1)."

Eligibility to Be a Chapter 15 Debtor

Section 109(a) provides that "only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title." Of significance, Section 109 is part of chapter 1 of Title 11, and Section 103(a) provides that "this chapter [1], sections 307, 362(o), 555 through 557, and 559 through 562 apply in a case under chapter 15."

In other words, Section 109(a) applies in chapter 15 cases, and Section 109(a) requires "a domicile, a place of business, or property in the United States." However, Judge Dorsey said, "Courts are split on whether [Section 109] should apply to Chapter 15 debtors." There are "two approaches," he said.

From the Second Circuit, one approach is seen in *Drawbridge Special Opportunities Fund LP v. Barnet (In re Barnet)*, 737 F.3d 238 (2d Cir. 2013). Judge Dorsey read *Barnet* for having found "nothing in Chapter 15 overriding § 103(a)'s explicit instruction that Chapter 1 should apply to Chapter 15."

Citing the *Collier* treatise and *In re Al Zawawi*, 637 B.R. 663, 667 (Bankr. M.D. Fla. 2022), *aff'd*, 97 F.4th 1244 (11th Cir. 2024), Judge Dorsey said, "Courts following the alternative approach find that the Second Circuit misconstrued Chapter 15's requirements." He quoted *Al Zawawi* for saying "there are 'just three conditions for recognition, none of which involve an assessment of the foreign debtor's contacts with the United States.'" *Id*.

Alluding to Section 1528 and Section 1410(2) and (3) of Title 28, Judge Dorsey noted how the "*Al Zawawi* court also looked at other sections of the Code indicating the inapplicability of § 109." He quoted *Collier* for "explicitly stating that '[w]hile Chapter 1 of the Bankruptcy Code applies in Chapter 15 cases by § 103, the § 109(a) criteria should apply only to cases under Chapters 7, 11, 12 and 13.'"

"Though it might appear that the plain language of § 103 requires the application of § 109," Judge Dorsey concluded that "such a reading would render § 1517, § 1528 and Section 1410 meaningless." Therefore, he was "persuaded by the reasoning in *Al Zawawi* and *Collier*" and his belief that "the alternative approach is more consistent with Congress' intentions."

Judge Dorsey held "that Chapter 15 debtors do not have to meet § 109's eligibility requirements." In a footnote, he added that "the Debtors would meet the eligibility requirements of § 109 through ownership of the retainer accounts" if he were to follow the Second Circuit.

After analyzing the other requirements from Section 1517, Judge Dorsey granted foreign main recognition.

Scholarly Commentary

Prof. Jay L. Westbrook, the Benno C. Schmidt Chair of Business Law at the University of Texas School of Law, and Daniel M. Glosband are the foremost authorities on chapter 15. Mr. Glosband provided ABI with the following commentary:

> Subsequent to the 2013 Second Circuit decision in *Barnet*, the National Bankruptcy Conference approved several proposed revisions to chapter 15, including one that states specifically that section 109(a) of the Bankruptcy Code does not apply to chapter 15. After surveying organizations interested in cross-border insolvency, the NBC proposed its unopposed revisions to Congress and on two occasions received draft legislation embodying the revisions, but it has not been successful in getting Congress to follow through.
>
> As one of the draftsmen of both the UNCITRAL Model Law on Cross-Border Insolvency and its U.S. adaptation as chapter 15, I know that the only requirements for recognition of a foreign proceeding were those set forth in section 1517.
>
> There is no reference to section 109(a) in section 1517. The primary reason that section 109(a) does not apply to chapter 15 is that the foreign proceeding — not the debtor — is the subject of the Model Law and chapter 15.
>
> Section 109(a) refers to "who may be a debtor under this title [title 11, the Bankruptcy Code]"; the debtor in a foreign proceeding is just that, a debtor in the foreign proceeding, but it never becomes a debtor under title 11. UNCITRAL confirmed in its *Guide to Enactment and Interpretation of the Model Law* that the attributes of the debtor were not relevant to recognition of a foreign proceeding:
>
>> In principle, the Model Law was formulated to apply to any proceeding that meets the requirements of article 2, subparagraph *(a)* [the definition of "foreign proceeding" and the same as the "foreign proceeding" definition in section 101(23) of the Bankruptcy Code], **independently of the nature of the debtor or its particular status under national law**." (Emphasis added.) *UNCITRAL Model Law on Cross-Border Insolvency, Guide to Enactment and Interpretation*, ¶ 55.

In this context, the March 2 decision of the U.S. Bankruptcy Court for the District of Rhode Island in *In re Venus Capital Management Company* is refreshingly straightforward and correct in its analysis by rejecting the application of section 109(a) to a petition for recognition under chapter 15.

In contrast, the February 10, 2026, decision of the Bankruptcy Court for the Southern District of Texas in *In re Siu-Fung Ceramics Holdings Limited* follows the erroneous analysis of the Second Circuit in *Barnet* and rules that section 109(a) must be satisfied in respect of a debtor when the foreign representative of the debtor's foreign proceeding seeks recognition of that foreign proceeding.

Since the requirements to satisfy section 109(a) are minimal, whether or not it applies is not often a real-world problem, but the issue invites tactical litigation that may delay the granting of a wholly appropriate petition for recognition and increase the costs. Note that the Eleventh Circuit ruled that section 109(a) does not apply to chapter 15, but did so based on pre-chapter 15 precedent and not on a straightforward analysis of chapter 15.

Mr. Glosband is of counsel in the Boston office of Goodwin Procter LLP. He and Prof. Westbrook were the primary draftsmen assisting the Department of State in drafting chapter 15.

The opinion is *In re Venus Capital Management Co.*, 25-10709 (Bankr. D.R.I. March 2, 2026).

When a foreign company operates from one country but has an inactive liquidation in another, the inactive liquidation doesn't establish 'center of main interests' for foreign main recognition in chapter 15, district judge says in affirming.

An Inactive Liquidation Abroad Isn't Entitled to Chapter 15 Foreign Main Recognition

When a foreign liquidator has conducted "no relevant liquidation activities" abroad, a letterbox company's foreign proceedings won't be granted recognition under chapter 15, for reasons explained by District Judge Lee H. Rosenthal in an opinion affirming Bankruptcy Judge Alfredo R. Pérez of Houston.

The July 6 opinion by Judge Rosenthal follows a decision 10 years earlier by Bankruptcy Judge Robert E. Gerber of New York who, she said, cut back on "the increasing trend of courts 'readily grant[ing] recognition to proceedings emanating from letterbox jurisdictions based on the foreign representatives' material efforts to manage or liquidate their debtors' businesses before coming to the U.S.'" *In re Creative Finance Ltd.*, 543 B.R. 498, 518 (Bankr. S.D.N.Y. 2016). To read ABI's report on *Creative Finance*, click here.

The Maltese Debtor

The debtor was a corporation evidently operating from Turkey that was incorporated in Malta. Having no operations itself, the debtor owned about 50 other Maltese companies that owned and operated ships. With the debtor not paying its debts, a court in Malta ordered the company dissolved and liquidated in 2017 and appointed a liquidator.

In late 2023, the court in Malta appointed a new liquidator designated as a foreign representative and authorized to file a chapter 15 petition in the U.S. Sixteen months later, the liquidator filed a chapter 15 petition in Houston, seeking foreign main recognition. A creditor opposed, contending that the Maltese proceedings were entitled to neither foreign main nor foreign nonmain recognition.

Judge Rosenthal meticulously recounted the decision by Bankruptcy Judge Pérez, finding that the proceedings were not entitled to recognition, neither main nor nonmain. Judge Rosenthal quoted Judge Pérez for having decided that "'the relevant inquiry is whether [the Maltese liquidator] engaged in significant pre-Petition work to operate or liquidate [the debtor] in Malta.'"

Since the liquidator's appointment in Malta, Judge Pérez had found that the liquidator had not paid taxes, had not brought legal proceedings outside of the chapter 15 case nor had he "reached out" to the debtor's former officers and directors. The liquidator conceded that those "were the general responsibilities of a liquidator in a Maltese proceeding."

Following *Creative Finance*, Judge Pérez ruled that the Maltese proceedings were not entitled to foreign main proceeding nor were they eligible for foreign nonmain recognition because there was no "establishment" in Malta.

The liquidator appealed to Judge Rosenthal, to no avail.

COMI Presumption Isn't Controlling

Among other requirements, Section 1517(a) provides that a foreign proceeding shall be recognized as foreign main proceeding if there is a "foreign main proceeding." In turn, Section 1517(c) says there is foreign main recognition if the foreign proceeding "is pending in the country where the debtor has the center of its main interests," or COMI.

The liquidator principally argued that the proceedings should have been recognized given the presumption of "center of main interests" in Section 1516(c). "In the absence of evidence to the contrary," the subsection provides that "the debtor's registered office . . . is presumed to be the center of the debtor's main interests."

Without ado, Judge Rosenthal held that Judge Pérez did not err by refusing to apply the presumption. Quoting another decision by Bankruptcy Judge Gerber, she said,

> This presumption "save[s] stakeholders costs in straightforward cases, but does not tie the hands of a court to examine the facts more closely in any instances where the court regards the issues to be sufficiently material to warrant further inquiry."

Quoting a bankruptcy court in California, Judge Rosenthal said that the presumption applies "'where there is no serious controversy.'"

Turning to the merits beyond the presumption, Judge Rosenthal alluded to the finding by Judge Pérez that because the liquidator "did not make any material efforts as a liquidator, COMI in Malta was not established." Similarly, in *Creative Finance* where recognition was denied, she said that the liquidators had "taken almost no relevant liquidation activities."

Because the debtor had "presented no evidence of any other activity in or ties to Malta during the relevant period other than [the liquidator's] (minimal) work as foreign representative and liquidator," Judge Rosenthal affirmed the denial of foreign main and foreign nonmain recognition, holding that the debtor had "not met its burden of proving that its COMI is in Malta."

The opinion is *Balzan v. Advantage Award Shipping LLC (In re Geden Holdings Ltd.)*, 25-4308 (S.D. Tex. July 6, 2026).

ROCHELLE'S DAILY WIRE

New York judge says that a Chinese company's arrangement in the Cayman Islands will garner foreign main recognition if the scheme is overwhelmingly accepted by creditors.

Mainland Chinese Company's Attempted Arrangement in Caymans Didn't Pass Muster

Sometimes a property company in mainland China can reorganize successfully in the Cayman Islands, and sometimes it can't.

Bankruptcy Judge Philip Bentley of New York declined to defer to the Caymans when the progress toward approval of a scheme of arrangement was going nowhere.

Incorporated in the Cayman Islands as an exempt company, the debtor was the ultimate parent of a large property developer whose assets and management were in mainland China. Being an exempt company meant that the debtor was precluded from conducting business in the Caymans.

Beset with falling revenue, the debtor needed to restructure about $600 million in four tranches of dollar-denominated senior notes with differing maturities and interest rates. The senior notes were governed by New York law and contained a New York forum-selection clause.

In early 2025, the debtor defaulted following the maturity of one issue of $170 million in senior notes. Three months later, the holders of some $65 million of the notes filed an involuntary chapter 11 petition in Judge Bentley's court.

Within a month of the involuntary petition, the debtor commenced arrangement proceedings in the Caymans, asserting that holders of 25% of the principal amount of all the note issues were supporting the scheme. Later, the debtor filed a motion to dismiss the involuntary chapter 11 petition in New York.

By the time the motion to dismiss came on for hearing eight months after commencement of the reorganization in the Caymans, Judge Bentley noted in his March 3 opinion that noteholders in support of the scheme had risen only to 31%, while Caymans law requires 75% approval.

The debtor sought abstention under Section 305. Alternatively, the debtor asked for dismissal for "cause" under Section 1112(b) or for *forum non conveniens*.

Abstention

Judge Bentley's opinion is a survey on the law of abstention under Section 305(a). The court may "dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if — (1) the interests of creditors and the debtor would be better served by such dismissal or suspension."

Judge Bentley began by saying that abstention is "an extraordinary remedy" to be employed only when both creditors and the debtor would be better served by dismissal. On a case-by-case basis, the inquiry is a fact-intensive investigation of the totality of the circumstances. Courts invoke several factors "flexibly," including comity, but not all are given equal weight.

Applying the law to the facts of the case before him, Judge Bentley began by analyzing the benefit to creditors from dismissal. "If the Debtor's Cayman Islands restructuring case appeared to be headed toward a successful conclusion," Judge Bentley said, he "would be reluctant to allow a concurrent chapter 11 case to proceed."

From the record, though, Judge Bentley concluded that "the Debtor's Cayman proceeding appears to be on a path to failure." He cited the failure to garner 75% creditor support required by Caymans law and the possibility that Caymans law might not countenance treating all four debt issues in the same class under a scheme.

Even if a scheme were to be approved in the Caymans, Judge Bentley said that an "even more daunting" hurdle would be recognition of a foreign main proceeding in the U.S. under chapter 15 to ensure enforcement of the scheme against holders of dollar-denominated debt. Given the current record, he said that the debtor "would face a significant challenge" in finding that the Caymans was the center of main interest.

COMI in the Caymans

"The standards governing determination of a chapter 15 debtor's COMI [center of main interests] were set forth by the Second Circuit in *Morning Mist Holdings Ltd. v. Krys (In re Fairfield Sentry Ltd.)*, 714 F.3d 127 (2d Cir. 2013)," Judge Bentley said. The opinion teaches that the country of incorporation gives rise to a statutory presumption of COMI, but the courts have "broad discretion" to determine the debtor's COMI.

In the case before him, Judge Bentley said that the debtor's nerve center was in mainland China and that the debtor only had "minimal" connections with the Caymans. Citing *In re Modern Land* (*China*) *Co., Ltd.*, 641 B.R. 768 (Bankr. S.D.N.Y. 2022), he said,

> [P]recedent in this District would support a Cayman Islands COMI finding if two conditions were met—specifically, if (i) the Debtor obtained the overwhelming

support of its Scheme creditors, and (ii) no party objected to recognition. [To read ABI's report on *Modern Land*, click here.]

In *Modern Land*, Judge Bentley said that the debtor was similarly based in mainland China and had minimal connections to the Caymans. However, Judge Bentley said that creditors in *Modern Land* had "overwhelmingly" approved the scheme in the Caymans restructuring, and there were no objections to foreign main recognition in chapter 15.

If the debtor were to obtain overwhelming support for the Caymans scheme and if there were no objections, Judge Bentley said that "*Modern Land* would provide strong precedential support for recognition of the Cayman Restructuring as a foreign main proceeding." At the time, however, he said that "the Debtor is very far from obtaining overwhelming creditor support."

The debtor countered by saying it may be difficult to enforce a judgment from a chapter 11 case in China, but Judge Bentley responded by saying that "the Debtor has provided no reason to expect that this would be any more of an issue for a U.S. reorganization than for a Cayman Islands restructuring." Furthermore, he cited the debtor's counsel for saying that the debtor would honor the terms of a restructuring.

For the foregoing reasons, Judge Bentley found that "the Debtor has not met its burden of showing that abstention would benefit its creditors."

Dismissal Under Section 1112(b) and *Forum Non Conveniens*

The debtor justified dismissal on the grounds that the noteholders filed the involuntary chapter 11 petition for an improper purpose, namely, to gain an unfair advantage in restructuring negotiations. Judge Bentley said that the debtor had not shown that the involuntary filing was "in any way improper."

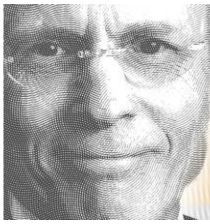
Section 1112(b) permits dismissal for "cause," but the debtor's "cause" arguments were based on improper purpose. Because the allegations about improper purpose were "unfounded," Judge Bentley saw no basis for dismissal under Section 1112(b).

The debtor also sought to dismiss for *forum non conveniens*, which, Judge Bentley said, imposes a "heavy burden" on the moving party.

Judge Bentley found "no basis whatsoever" for dismissal based on *forum non conveniens*, given how the notes had a New York forum-selection clause "that expressly waives any objection to suit being brought in any federal or state court in New York."

Judge Bentley denied the motion to dismiss without prejudice.

The opinion is *In re Xinyuan Real Estate Company Ltd.*, 25-10745 (Bankr. S.D.N.Y. March 3, 2026).



Prudential standing deprived foreign liquidators of standing, even though the liquidators were suing under a foreign law that explicitly granted standing to the liquidators.

Wagoner Deprived Liquidators of Standing Granted Them by Foreign Law

Although law in the Cayman Islands gives its liquidators the right to sue someone who knowingly participated in carrying on the debtor's business to defraud creditors, District Judge Dale E. Ho of New York held that the liquidators lacked prudential standing under the Second Circuit's *Wagoner* rule, even though the liquidators had constitutional standing.

Judge Ho's September 30 opinion explains the relationship between the *Wagoner* rule and the doctrine of *in pari delicto*. *See Shearson Lehman Hutton, Inc. v. Wagoner*, 944 F.2d 114 (2d Cir. 1991).

The debtor was an investment fund in liquidation in the Cayman Islands. The debtor's Caymans liquidators sued a bank in federal district court in New York. The liquidators brought claims for fraudulent trading under Section 147 of the Cayman Islands Companies Act.

Asserting that the debtor had conducted a Ponzi scheme, the liquidators alleged in their complaint that the bank was willfully blind to the debtor's fraud, causing the debtors to lose more than $200 million by providing services to the debtor. Judge Ho paraphrased Section 147 of the Cayman's Companies Act as permitting "liquidators to seek a contribution to a debtor's assets from any person or entity that knowingly participated in the carrying on of the debtor's business with the purpose of defrauding its creditors."

The bank filed a motion for summary judgment, which Judge Ho granted.

Injury in Fact

First, the bank argued that the liquidators lacked constitutional standing under Article III, where the plaintiff must have (1) suffered "concrete and particularized injury" that is (2) "fairly traceable to the challenged conduct" and is (3) "likely to be redressed by a favorable judicial decision." *Hollingsworth v. Perry*, 570 U.S. 693, 704 (2013).

The bank admitted that the third element was satisfied. Regarding injury, however, the bank argued that the liquidators had no constitutional standing because the purpose of the suit was to address injury to the debtors' creditors.

Judge Ho found no precedent regarding liquidators' standing under Section 147. As a remedy, he noted that Caymans law permits the court to order the defendant to make "contributions" to the debtor's assets. He therefore read Section 147 as allowing liquidators to recover losses from the company's assets but not for damages to particular creditors.

Because the "Section 147 claim [was] not brought to compensate particular creditors who were victims of the fraud," Judge Ho rejected the bank's contention that the claim was brought on behalf of creditors.

Causal Connection

Regarding a "causal connection," the bank took the position that the debtor was the direct cause of the injury, but Judge Ho said that a "direct relationship is not a requirement" and that the relationship "need not be the very last step in the chain of causation."

In the case before him, Judge Ho said that the bank "provided banking services to [the debtor], which were in turn directly used in furtherance of a Ponzi scheme." Even "if [the bank's] role in the underlying fraud could be properly characterized as only indirect," Judge Ho held that "an indirect causal connection may suffice for purposes of Article III standing."

Finding that the liquidators "met the relatively low threshold for establishing a causal connection," Judge Ho ruled that the liquidators had constitutional standing.

Prudential Standing

Citing Supreme Court authority, Judge Ho described how "'the federal judiciary has also adhered to a set of prudential principles that bear on the question of standing' and are meant to '[]impose[] limits on the exercise of federal jurisdiction.'"

In *Wagoner*, Judge Ho said that "the Second Circuit held that 'when a bankrupt corporation has joined with a third party in defrauding its creditors, the trustee cannot recover against the third party for the damage to creditors.'" *Wagoner*, *supra*, 944 F.2d at 118. The Second Circuit reasoned that the actions of corporate managers are imputed to the company and that a trustee stands in the shoes of the corporation.

Therefore, Judge Ho described *Wagoner* as holding that "a trustee is barred 'from suing to recover for a wrong that he himself essentially took part in.'" *Id.* at 87. He summarized *Wagoner* as standing "for the proposition that a bankruptcy trustee cannot assert claims on behalf of the bankrupt corporation against a third party for fraud when the corporation itself participated in the fraud."

Resisting the application of *Wagoner*, the liquidators argued that they alone can bring suit under Section 147. They also argued that *Wagoner* was New York law and that Caymans law applied to the case.

Finding no on-point authority saying whether *Wagoner* applied to Section 147 claims, Judge Ho undertook his own analysis.

Wagoner

Judge Ho identified "a resemblance between the *Wagoner* rule and the principle of *in pari delicto*, which, under New York law, prohibits one wrongdoer from recovering against another." However, he cited the New York Court of Appeals, the highest court in the New York State system, for holding "that 'the *Wagoner* rule is not part of New York law' — rather, it 'is a prudential limitation on standing under federal law.' *Kirschner v. KPMG LLP*, 938 N.E.2d 941, 946 n.3 (N.Y. 2010)."

Because the Court of Appeals is the final authority on New York law, Judge Ho said, "it follows that it is also the final authority on what is *not* an aspect of New York law." [Emphasis in original.] He went on to describe the difference between *in pari delicto* and the *Wagoner* rule.

In pari delicto, Judge Ho said, "is an *affirmative defense* under New York law on which the defendant carries the burden." [Emphasis in original.] Although "the *Wagoner* rule is related to *in pari delicto*," he said, "*Wagoner* is a distinct doctrine that 'derives in significant part from federal bankruptcy law, and is a prudential limitation on standing under federal law.'"

Judge Ho therefore found "no reason to limit the application of the *Wagoner* rule to claims brought under New York law (or to claims brought under the laws of jurisdictions that incorporate analogous legal principles)."

Resisting the idea that *Wagoner* should control, the liquidators again argued that *Wagoner* was inapplicable because Section 147 gives liquidators alone the authority to bring claims of the type. Moreover, the liquidators said that they stand in their own shoes, not in the shoes of the debtor.

Even though Section 147 may only be brought by liquidators, Judge Ho said that "it does not then follow that a liquidator stands in its 'own shoes.'" He pointed to the liquidators' complaint where they were asserting claims on behalf of the debtor and that the injury was to the debtor, not to creditors.

"All of this compels the conclusion that, for purposes of assessing prudential standing, the Joint Liquidators' Section 147 claim is brought on behalf of [the debtor]," Judge Ho said. He granted the bank's motion for summary judgment, holding that *Wagoner* bars the liquidators' claims.

Observations

The liquidators have filed a motion for reconsideration. If Judge Ho sticks by his decision, an appeal to the Second Circuit is a possibility. Given a circuit split, don't count out a petition for *certiorari*.

Arguably, there is a split of circuits. In 2016, the Sixth Circuit held that the *Wagoner* rule does not apply in federal litigation. The Cincinnati-based appeals court cited the Eighth, Eleventh and Third Circuits as also having disagreed with *Wagoner*. *Bash v. Textron Financial Corp. (In re Fair Finance Co.)*, 834 F.3d 651 (6th Cir. Aug. 23, 2016). To read ABI's report, click here.

Reconsideration and further appeals could raise several issues. Since the Supreme Court has abandoned the idea of prudential jurisdiction, is prudential standing an element of federal common law that is no more?

In *Truck Insurance Exchange v. Kaiser Gypsum Company, Inc.*, 602 U.S. 268 (June 6, 2024), the Supreme Court broadly defined parties in interest in bankruptcy cases. However, *Truck Insurance* dealt with creditors' rights to appear and be heard in bankruptcy cases, not the right of an estate representative to bring suit. Nonetheless, will *Truck Insurance* inform courts about plaintiffs' standing in bankruptcy cases? To read ABI's report on *Truck Insurance*, click here.

Reconsideration and appeals will question whether *Wagoner* or *in pari delicto* can be applied in a cross-border insolvency to deprive a foreign representative of standing when foreign law expressly grants standing. Disregard for standing granted by foreign law also raises questions about comity.

Dismissal of the liquidators' suit was based in part on the idea that the liquidators stood in the shoes of the debtor corporation that committed fraud. In that regard, *in pari delicto* and *Wagoner* are at odds with the rule that federal receivers are not subject to *in pari delicto*. It would be interesting to see a court explain why *in pari delicto* and *Wagoner* infect bankruptcy trustees and foreign liquidators, but not federal receivers.

The opinion is *Trott v. Deutsche Bank A.G.*, 20-10299 (S.D.N.Y. Sept. 30, 2025).

The Federal Circuit upheld the claims court's decision that taking away bondholders' collateral wasn't an unconstitutional taking.

Puerto Rico's Debt-Adjustment Proceedings Weren't Unconstitutional 'Takings'

In May 2023, the Supreme Court held that nothing in the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*), waived the Puerto Rico Oversight Board's sovereign immunity. *Financial Oversight & Management Board for Puerto Rico v. Centro de Periodismo Investigativo Inc.*, 598 U.S. 339 (Sup. Ct. May 11, 2023). To read ABI's report, click here.

Adding another constitutional dimension to PROMESA, the U.S. Court of Appeals for the Federal Circuit held on July 31 that the haircut given to holders of so-called Cofina bonds in the PROMESA proceedings were not "takings" under the Fifth Amendment.

The Cofina Bonds

The Commonwealth of Puerto Rico and its instrumentalities were in financial straits. They were butting up against debt limits in the Puerto Rico Constitution and were unable to access bond markets. To generate borrowing power, Puerto Rico created Cofina as a public corporation, independent from the government.

Cofina was empowered to sell bonds secured by Puerto Rico's collection of sales taxes. As Circuit Judge Kara Farnandez Stoll said in her opinion for the Federal Circuit, Cofina had sole ownership and control of the fund created to hold sales taxes.

When Puerto Rico was held ineligible for a federal municipal debt adjustment under chapter 9 of the Bankruptcy Code, Congress quickly enacted PROMESA, which adopts large portions of chapter 9. Puerto Rico and many of its instrumentalities sought relief under PROMESA in 2017 in what is known as Title III debt-adjustment proceedings.

In the Title III proceedings, Puerto Rico's federally appointed Financial Oversight and Management Board in substance represented Puerto Rico and its instrumentalities. In April 2022, the First Circuit upheld confirmation of the Oversight Board's plan of adjustment for the Commonwealth of Puerto Rico. *Federacion de Maestros de Puerto Rico v. Financial Oversight and Management Board for Puerto Rico (In re Financial Oversight and Management Board for Puerto Rico)*, 32 F.4th 67 (1st Cir. April 26, 2022).To read ABI's report, click here.

Cofina was among the instrumentalities that the Oversight Board put into Title III proceedings. The ultimate outcome was a plan of adjustment giving 54% of sales tax revenues to Cofina's bondholders and 46% to Puerto Rico.

After the Cofina arrangement was confirmed, Cofina bondholders filed a class action in the U.S. Court of Federal Claims, contending that sales tax revenue taken away from bondholders violated the Takings Clause of the Fifth Amendment of the U.S. Constitution.

The claims court denied the government's motion to dismiss based on the idea that PROMESA took away the claims court's Tucker Act jurisdiction. However, the claims court went on to dismiss the complaint, holding that the PROMESA arrangement was not an unconstitutional taking.

The bondholders appealed to the Federal Circuit.

Tucker Act Jurisdiction

Judge Stoll explained that the Tucker Act, 28 U.S.C. § 1491(a)(1), "waives sovereign immunity for, and provides for Claims Court jurisdiction over, monetary claims against the United States 'founded [] upon . . . the Constitution . . . or upon any express or implied contract with the United States.'" Of course, a takings claim falls within the claims court's jurisdiction, she said.

The government nonetheless contended that PROMESA "displaced" the claims court's jurisdiction. Quoting the Supreme Court, Judge Stoll said that a "determination of displacement of jurisdiction requires 'an unambiguous [congressional] intention to withdraw the Tucker Act remedy.'" She also cited the Supreme Court for holding that the Tucker Act and another statute both remain effective when they can coexist.

As for PROMESA, Judge Stoll said that its "provision falls short of the 'specific and comprehensive scheme for administrative and judicial review' that we have found sufficient to displace the Tucker Act." As an example of a shortcoming, she pointed to "PROMESA's failure to mention or provide for recourse against the Government as reflecting Congress's belief that the general grant of jurisdiction under the Tucker Act would provide the necessary remedy for any taking that may occur."

Finding "no such expressed intention to withdraw Tucker Act jurisdiction," Judge Stoll upheld the claims court's finding that it had jurisdiction over the bondholders' constitutional claim.

No Takings Claim

Turning to the bondholders' takings claim, Judge Stoll cited 1982 and 1991 opinions where the Supreme Court found unconstitutional takings because "the Government directly took the property owner's right to exclude when it authorized the third party to enter onto private property." In both cases, she said that "the Government compelled the property owners to suffer an invasion of their property" and that it was "immaterial that the invasion was executed by a third party because it was the Government who directly took the property owner's right to exclude."

There are two tests, Judge Stoll said, in deciding whether the government's "instigation" of third-party action becomes a governmental taking. In the case on appeal, the government's action failed the second test because the government's influence over the third party was "merely coercive." The Oversight Board, she said, was not an agent of the government. Indeed, she said that the government lacked the ability to exercise "general control" over the Oversight Board.

Judge Stoll agreed with the claims court "that providing Puerto Rico with additional tools to manage its economic security, as PROMESA does, does not equate to 'the government instigat[ing] action by a third party,'" quoting Federal Circuit precedent. In fact, she said that PROMESA gives the Oversight Board power to initiate debt-adjustment proceedings, "but the Oversight Board is not required to do so." Furthermore, when the Oversight Board does act, she said it is acting on behalf of the interests of Puerto Rico, not the U.S.

Agreeing "with the Claims Court that the United States lacks the requisite amount of coercive control over the Oversight Board's actions to create liability under the Fifth Amendment," Judge Stoll affirmed dismissal of the constitutional Takings Clause claim.

The opinion is *Dinh v. U.S.*, 2023-2100 (Fed. Cir. July 31, 2025).

Brazilian foreign representative didn't show the relevant grounds for revoking a recognition order and dismissing the chapter 15 case.

New York Judge Wouldn't Dismiss a Chapter 15 Case to Circumvent Brazilian Law

Bankruptcy Judge Lisa G. Beckerman of New York didn't allow a foreign representative to dismiss a chapter 15 case as part of a strategy to obtain relief through a chapter 11 reorganization in the U.S. that wasn't available under Brazilian law.

In her October 1 opinion, Judge Beckerman seemed reluctant to create potential conflicts were the U.S. court in chapter 11 to compete with the court in Brazil over assets located in Brazil.

Brazilian Company's Second Bankruptcy Reorganization

The Brazilian debtor was one of the world's largest telecommunications services providers. All of the company's assets and 14,000 employees are in Brazil.

The debtor filed its first judicial reorganization in Brazil in 2016. The first proceeding resulted in a reorganization plan in the Brazilian court to which the bankruptcy court in New York gave full force and effect by recognition in a chapter 15 case. The first chapter 15 case was closed in early 2023.

Facing further financial difficulties, the debtor began a second judicial reorganization in Brazil later in 2023. After the debtor's foreign representative filed a second chapter 15 petition, the New York court recognized the Brazilian proceedings as the foreign main proceeding. When the Brazilian court approved a second reorganization, the U.S. bankruptcy court gave it full force and effect.

Because the second reorganization relied on optimistic projections, the debtor again faced "severe liquidity constraints" and was unable to meet its obligations as they came due, Judge Beckerman said. In response, the debtor filed a proposed amendment to its second Brazilian reorganization plan. Several creditors in Brazil objected.

A watchdog for the Brazilian court determined that the debtor could not satisfy its short-term obligations, including those in the second reorganization plan. Meanwhile, the foreign representative filed a motion asking Judge Beckerman to terminate the recognition order and dismiss the chapter 15 case.

Regarding the proposed amendment to the reorganization plan, Brazilian law put the debtor in a tight spot. Brazilian law wouldn't permit a third reorganization for five years following the prior reorganization, which had been approved only 14 months earlier.

Furthermore, Brazilian law would not permit the amendment to modify post-petition debts and other obligations like tax claims and leases.

The debtor came up with the idea of filing a chapter 11 petition in the U.S. to restructure the post-petition debts and other claims that could not be modified under Brazilian law. However, Section 1528 was a roadblock. After recognition, it provides that "a case under another chapter of this title may be commenced only if the debtor has assets in the United States [and] shall be restricted to the assets of the debtor that are within the territorial jurisdiction of the United States."

There being no assets in the U.S., Section 1528 would mean little utility for a chapter 11 case in the U.S.

To circumvent Section 1528 and permit a chapter 11 case to affect assets in Brazil, the foreign representative was asking Judge Beckerman to revoke the recognition order and dismiss the second chapter 15 case.

Section 1517(d): The Standard for Chapter 15 Dismissal

Judge Beckerman's opinion is a *tour de force* analysis of complex and contradictory provisions in chapter 15. Her opinion is a must-read for chapter 15 mavens.

On the one hand, there is Section 305(a)(2), which may or may not apply in chapter 15 cases, even though it says that a petition may be dismissed or suspended if "the purposes of chapter 15 of this title would be best served by such dismissal or suspension." Section 305(b) says that a foreign representative may seek dismissal.

Judge Beckerman decided that Section 1517(d) "provides the relevant standard for modifying or terminating a recognition order." It reads as follows:

> The provisions of this subchapter do not prevent modification or termination of recognition if it is shown that the grounds for granting it were fully or partially lacking or have ceased to exist, but in considering such action the court shall give due weight to possible prejudice to parties that have relied upon the order granting recognition.

After pages of analysis, Judge Beckerman decided that "the change in the Company's liquidity position is not a justification for terminating the Recognition Order." She also determined that terminating the recognition order was "procedurally improper" under Bankruptcy Rule 5009(c), because "the purpose of a foreign representative's appearance [had not been] completed."

Judge Beckerman ruled that the foreign representative had not established that the grounds for recognition "ceased to exist." She also concluded that Section 305 permits dismissal as to "cases other than chapter 15."

Similarly, Judge Beckerman decided that Section 1521 "is only available when it is necessary to effectuate the purpose of chapter 15," but "dismissing these Chapter 15 Cases is not necessary to effectuate the purpose of chapter 15." Citing Section 1501(a)(3), she said, "it is also unclear that dismissing the Chapter 15 Cases would promote the 'fair and efficient administrations of cross-border insolvencies that protect the interests of all creditors, and other interested entities, including the debtor.'"

Judge Beckerman ended her opinion by analyzing whether the debtor's contemplated chapter 11 case in the U.S. might succeed. She said that a "chapter 11 filing might protect and maximize the value of the debtor's assets and result in a confirmed plan of reorganization which resolves treatment of" claims that could not be compromised in Brazil, "[b]ut it also might not."

Judge Beckerman explained why a chapter 11 case in the U.S. might not succeed.

> All of the assets of the Company are part of the estate under supervision of the [Brazilian court] and are located in Brazil. If a chapter 11 case were to be filed for the Company, these assets may also be part of the estate under the supervision of the United States Bankruptcy Court. If neither proceedings are ancillary proceedings, the Model Law and chapter 15 will likely not provide a basis for resolving any disputes that arise regarding any sales of assets, dueling jurisdiction over claims, the treatment of [claims that cannot be compromised under Brazilian law], debts incurred after the filing of the [second Brazilian reorganization] and executory contracts, the granting and enforcement of debtor-in-possession financing and related liens, requests to dismiss or abstain with respect to the chapter 11 case, and the recognition and enforcement of orders entered by the United States Bankruptcy Court in Brazil, to name just a few issues that might arise.

Judge Beckerman said that the court in Brazil "and the United States Bankruptcy Court might be able to work these complex issues out so that the restructuring process works and results in a successful restructuring of the Company. But, they also may not be able to do so." Consequently, she said, "the success of a chapter 11 case . . . is simply not certain."

Judge Beckerman denied the motion to revoke recognition and dismiss the chapter 15 case, finding "there is not a basis to grant dismissal of the Chapter 15 Cases."

The opinion is *In re Oi S.A.*, 23-10193 (Bankr. S.D.N.Y. Oct. 1, 2025).

Foreign reorganizations with nondebtor releases are not 'manifestly contrary' to public policy after Purdue, according to the chief district judge in Delaware.

Nondebtor Releases Are Still Permissible in Chapter 15, Delaware District Judge Says

Purdue notwithstanding, the chief district judge in Delaware upheld Bankruptcy Judge Thomas M. Horan, whose decision one year ago granted foreign main recognition and enforced a Mexican reorganization plan containing nonconsensual releases in favor of nondebtor third parties.

In his March 31 opinion, Chief District Judge Colm F. Connolly said that chapter 15 "grant[s] courts broad discretion to approve relief that protects debtor assets and creditor interests, unless explicitly excluded, and third-party releases are not among those exclusions." In the same vein, he said that the "public policy exception" in chapter 15 "provides a narrow remedy for genuine threats to core U.S. constitutional or statutory rights, as opposed to mere discrepancies between domestic and foreign law."

The Mexican Plan

The debtor was one of Mexico's largest nonbank lenders. Financial problems led to a liquidation proceeding in a Mexican court. Discussions culminated when the debtor, the Mexican liquidators and an *ad hoc* group of creditors developed a restructuring support agreement. The Mexican liquidator then commenced a proceeding in Mexico to implement the prepackaged plan.

The plan received support from almost 57% of creditors. The Mexican court overruled objections and approved the prepackaged plan.

The plan contained releases for the *ad hoc* committee members, the Mexican liquidator, the indenture trustee and related parties. The releases barred claims for actions taken during the restructuring. Like Bankruptcy Judge Horan, District Judge Connolly said that the releases were "customary in Mexican settlement agreements" and were "permitted under Mexican Bankruptcy Law."

An agency of the U.S. government, the U.S. International Development Finance Corporation, or DFC, had appealed after objecting unsuccessfully to the Mexican court's approval of the plan. The DFC's appeal remains pending in Mexico.

After approval of the plan in the Mexican court, the debtor's foreign representative commenced the chapter 15 case in Delaware, seeking foreign main recognition and enforcement of the Mexican plan and its releases in the U.S. The DFC objected to enforcement of the releases but did not object to foreign main recognition.

Bankruptcy Judge Horan overruled the objection, granted foreign main recognition under chapter 15 and enforced the nondebtor releases. *In re Crédito Real SAB de CV*, 670 B.R. 150 (Bankr. D. Del. April 1, 2025). To read ABI's report, click here.

The DFC appealed. Judge Connolly described the agency as arguing that the bankruptcy court "lacked statutory authority to approve such a release under Chapter 15 and that the release was 'manifestly contrary to the public policy' of the U.S. within the meaning of § 1506 of the Bankruptcy Code."

'Manifestly Contrary'

On granting foreign main recognition, Judge Connolly said that Section 1501 gives the bankruptcy court "broad discretion to grant enforcement of orders entered in the foreign main proceeding, consistent with the guiding principles of comity." He added,

> Section 1521(a) authorizes the court to grant "any appropriate relief" necessary to effectuate the purposes of Chapter 15, and section 1507 independently authorizes "additional assistance," subject to specifically enumerated prohibitions, which do not include third-party releases.

Judge Connolly did not fail to point out the limitation in Section 1506, which "which provides that a court may decline to grant relief that is 'manifestly contrary to the public policy of the United States.'"

Applying the statutes to the facts of the case, Judge Connolly began with Section 1506 and *Purdue*, the Supreme Court decision banning nonconsensual, nondebtor releases in chapter 11 plans. *Purdue*, he said, is "not applicable to this case as it addressed a statutory interpretation question applicable only to Chapter 11."

The DFC took the position that *Purdue* was a roadmap for the interpretation of the catchall provisions in chapter 15, but Judge Connolly responded by saying that *Purdue* addressed a "narrow question" under Section 1123(b)(6). If Congress intended "to condition Chapter 15 relief on the rules of Chapter 11, it would have so stated." He then held "that *Purdue* has no bearing on whether the Release may be recognized in a Chapter 15 case."

Nondebtor Releases Weren't Excluded from 'Additional Relief'

Next, Judge Connolly examined whether enforcement of the releases was permissible under Sections 1521(a) and 1507. The ability to grant "any appropriate relief" under Section 1521(a), he said, confers "broad judicial discretion, including the ability to enforce the terms of a foreign restructuring plan."

The DFC argued that the broad powers under Section 1521(a) were limited by Section 1521(a)(7), which allows the court to grant "any additional relief that may be available to a trustee." Because a trustee may no longer grant nonconsensual releases, the agency read Section 1521(a)(7) to mean that releases are now barred in chapter 15 cases.

Judge Connolly rejected the idea, saying that the subsection "does not impose a requirement that the relief be presently available under Chapter 11," because reference to a trustee "refers not to the identity of the actor, but to the nature of the relief available in U.S. bankruptcy proceedings."

Judge Connolly held that "sections 1521(a) and 1521(a)(7) grant courts broad discretion to approve relief that protects debtor assets and creditor interests, unless explicitly excluded, and third-party releases are not among those exclusions."

'Additional Assistance' Can Be More than Chapter 11 Permits

Judge Connolly turned to Section 1507(a), which allows the court to "provide additional assistance to a foreign representative."

The section, Judge Connolly said, allows the court to grant assistance "even when the relief exceeds what is typically available under Chapter 11, so long as basic principles of comity, fairness, and U.S. public policy are respected." He went on to say that the subsection "signals Congress's intent to accommodate the unique demands of cross-border restructurings, rather than constrain them within the narrower confines of purely domestic provisions."

Judge Connolly held "that section 1507(a) authorizes enforcement of third-party releases where the relief aligns with the principles of comity, fairness, and U.S. public policy."

Turning to public policy, Judge Connolly said that "Section 1506's public policy exception provides a narrow remedy for genuine threats to core U.S. constitutional or statutory rights, as opposed to mere discrepancies between domestic and foreign law." He held that the releases did not violate public policy, because "the relief granted in a foreign proceeding does not need to be identical to what might be available in the U.S."

Judge Connolly upheld the enforcement of the nondebtor releases, noting that the "DFC's arguments misconstrue the Supreme Court's narrow holding in *Purdue*."

The opinion is *U.S. International Development Finance Corp. v. Crédito Real SAB de CV SOFOM, ENR (In re Crédito Real SAB de CV SOFOM, ENR)*, 25-371 (D. Del. March 31, 2026).