BANKRUPTCY BASICS: WHAT EVERY ATTORNEY SHOULD KNOW ABOUT BANKRUPTCY

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Michael F. Thomson
Dorsey & Whitney LLP
111 South Main Street, 21st Floor
Salt Lake City, Utah 84111
Tel. 801.933.8929
Fax 801.933.7373
thomson.michael@dorsey.com

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I. Policies and Maxims of Bankruptcy Laws

A. Initially for the Benefit of Creditors. The first insolvency laws and the court decisions interpreting and extending them were intended primarily for the benefit of creditors. Over the years, as commercial relationships and transactions evolved and as consumer rights and issues became more important, insolvency laws have become more balanced, with scholars and legislators attempting to find a happy medium between creditors' rights and debtor protection. The most recent major amendments to the Bankruptcy Code in 2005 ("BAPCPA") swung the pendulum in the consumer bankruptcy area back toward creditors. The positions of debtor and creditor play out based on the relative leverage held by each. Ultimately, the law of debtors and creditors is based even more than other areas of the law on relative leverage. The laws alter this relative leverage as do, of course, the facts of each situation involving a debtor unable to pay all of its debts and a creditor wishing to ensure full and prompt payment of debts owed to it.

B. Bankruptcy Policies in Consumer and Business Cases. The underlying policies of bankruptcy differ slightly as between consumer and commercial cases.

1. Consumer Cases. In a consumer bankruptcy case, the principal policy is for a debtor to obtain a "fresh start." The debtor's fresh start is obtained through a "discharge" of the debtor's obligations. With the abolition of debtor's prisons, this type of policy only makes sense, although consumer bankruptcy is, in many respects, a middle class phenomenon and impoverished people with few or no assets and inability to incur much debt receive little benefit from bankruptcy.

2. Business Cases. In business cases, the policies are more balanced between the interests of debtors and creditors. An underlying assumption of business bankruptcy is that creditors as a whole will do better in a collective proceeding rather than in a piecemeal picking at the bones of an insolvent business where the law of the jungle rules. A maxim of all bankruptcy law, though more acutely focused in business bankruptcy, is that creditors in similar positions should have equality of distribution. This is based on a priority scheme developed in statutes over the years, more fully discussed below. A debtor, particularly in a Chapter 11

[1]Portions of this outline were written by Kenneth L. Cannon II of Durham Jones & Pinegar in Salt Lake City, Utah, and are used with his permission.

reorganization or a Chapter 12 family farm restructuring, is given a "breathing spell" after filing a bankruptcy case to take stock of its position and to focus on rehabilitating its business for the benefit of debtor and creditor alike. Discharge and fresh start are important concepts in many business bankruptcies, although, because legal entities that are not natural persons can be terminated without violation of law, corporations do not receive a discharge in Chapter 7.

II. Critical Concepts and Procedural Protections. Bankruptcy law implements a number of key concepts and procedural protections.

A. The Estate and Property of the Estate. When a bankruptcy petition is filed, at least a voluntary petition, an estate is created. Section 541 of the Bankruptcy Code defines of what property this estate consists. Generally, with a few limited exceptions, it consists of all legal and equitable interests of the debtor in property. The estate includes exempt property, even though an unsecured creditor or some involuntary secured creditors may not be able to participate in the value of exempt property.

B. The Automatic Stay. The automatic stay created by section 362(a) of the Bankruptcy Code is a procedural protection implemented to preserve the estate. It is very broad, it is automatic, and it generally stays, with certain restricted but important exceptions, all actions against the debtor to recover on its financial obligations and against property of the estate to recover on those obligations. Violation of the automatic stay is a pitfall many parties fall into, some innocently, and is something you want to avoid and have your clients avoid. The law in the Tenth Circuit, as in many circuits, is that an action taken in violation of the automatic stay is void. Ellis v. Consolidated Diesel, 894 F.2d 371 (10th Cir. 1990). Where the action is declared void, the relief is to return the parties to their respective positions prior to the stay violation occurred. Jubber v. Bank of Utah (In re C.W. Mining Co.), 749 F.3d 895, 899 (10th Cir. 2014). Under section 362(k), damages (including costs and attorneys' fees) and punitive damages are available to an individual injured by a willful violation of the automatic stay.

C. Claims. Claims in bankruptcy are construed very broadly both by the statute (section 101(5) of the Bankruptcy Code) and the case law. A claim is a right to payment, whether or not that right is liquidated, matured, contingent, disputed, legal, equitable, secured, unsecured, or a right to an equitable remedy for breach of performance if that breach gives rise to a right to payment.

D. Priorities. Unsecured debt and equity interests are paid from a bankruptcy estate in accordance with a priority scheme developed over centuries and currently governed by sections 507 and, in Chapter 7 cases, 726. Secured debt is governed by relative priority of security interest in accordance with applicable law, with an exceedingly important caveat: section 506(a) of the Bankruptcy Code divides a "secured" claim in two if the collateral securing the collateral is insufficient to

cover the full amount of the claim; a claim is secured for bankruptcy purposes to the extent of the value of the collateral and is unsecured for the remaining amounts owing. The unsecured portion fits within the section 507/726 priority scheme like other unsecured debt.

E. Exemptions. Individuals, who are only living, breathing natural persons as opposed to legally invented persons such as partnerships, corporations, and limited liability entities, are entitled to exempt certain of their property from distribution to creditors.

F. Preferences, Fraudulent Transfers, and Strong-Arm Actions. Bankruptcy trustees ("Trustees"), including debtors in possession ("DIP's") in Chapter 11, are endowed with the power to avoid certain transfers and transactions. These all further the fundamental bankruptcy policy favoring equal treatment of similarly situated creditors.

G. Best Interests of Creditors. The gauge of whether a creditor is treated sufficiently is applied against liquidation. Unless creditors agree to something less, they are theoretically entitled under Chapter 11 or 13 to receive at least as they would receive in Chapter 7. This is called the "best interests of creditors" test.

H. Cramdown. This is a happy, non-statutory term to describe what can happen to dissenting creditors under a plan in Chapter 11. If certain criteria under section 1129(b) of the Bankruptcy Code are met under a plan of reorganization with respect to a class of dissenting creditors or equity security holders, the plan proponent can cram the proposed plan treatment down the creditors' throats.

I. Discharge. The ultimate goal in bankruptcy – when a debtor legally is excused of paying his, her, or its debts as they existed prior to bankruptcy.

III. The Bankruptcy Code and Its Chapters. The Bankruptcy Code is broken down into chapters, subchapters, and sections with subsections.

A. Cases under the Chapters. Chapter 7, Chapter 9, Chapter 11, Chapter 12, and Chapter 13 encompass different types of bankruptcy cases. As discussed more fully below, Chapter 7 governs general liquidation for individuals or business entities. Chapter 9 governs a highly specialized type of case for governmental entities, such as the City of Detroit and Orange County cases. Chapter 11 governs business reorganization cases. Chapter 12 governs another specialized type of reorganization case that only qualifying family farmers are eligible for. Finally, Chapter 13 governs individual debt restructuring. Chapters 9 and 12 are sufficiently specialized that they will not be discussed further in this discussion.

B. Administration Chapters. In addition, the Bankruptcy Code has Chapters 1, 3, and 5. In theory, at least, provisions in these three chapters have general applicability to bankruptcy cases under Chapters 7, 9, 11, 12, and 13. In fact,

some of the provisions in Chapters 1, 3, and 5 have only limited applicability in some types of cases and some provisions are modified by specialized provisions in Chapters 7, 9, 11, 12, and 13. What about even-numbered chapters? Other than Chapter 12, there are no even-numbered chapters.

IV. Different Types of Bankruptcy Cases

A. Liquidation

1. Chapter 7. Chapter 7 encompasses the traditional concept of bankruptcy—a Trustee is appointed and the debtor's assets are collected, determined, and sold or abandoned, with net proceeds distributed to creditors according to the priority schemes of the Bankruptcy Code. The Chapter 7 bankruptcy estate is fixed at the time of the bankruptcy petition and income received by an individual debtor after the bankruptcy petition, with certain narrow exceptions, are not part of the bankruptcy estate. Debtors other than individuals do not receive a discharge in Chapter 7. See 11 U.S.C. § 727(a)(1). Some debtors, particularly individuals with substantial future income potential, may not be eligible for Chapter 7. See 11 U.S.C. § 707(b).

2. Chapter 11. Chapter 11 typically contemplates reorganization of a business. However, Congress expressly provided for the possibility that an orderly liquidation of a business could be accomplished in Chapter 11. See 11 U.S.C. § 1123(b)(4). In such a liquidating Chapter 11 case, no discharge is granted. See 11 U.S.C. § 1141(d)(3).

B. Reorganization/Restructuring

1. Chapter 11 "Ordinary" Case . Chapter 11 governs what has become the classic, some would say infamous, reorganization of a business. An "ordinary" Chapter 11 case is simply one that is not a "small business case." The DIP (or some other party) proposes a plan of reorganization which restructures the company's debts and provides to pay creditors from the future operations of the reorganized business. The same priorities apply in Chapter 7, but creditors may, as a class under a plan of reorganization, agree to permit a class of creditors to receive some distribution under the plan even if prior claims are not paid in full.

2. Chapter 11 "Small Business" Case. In 1994, Congress imposed slightly different rules under Chapter 11 on "small businesses," which are currently defined to be certain businesses with secured and unsecured debt of less than $2,566,050. The 2005 amendments, which became generally effective to new cases filed after October 17, 2005, further defined small business cases. Generally, there is a shorter exclusive period for small business debtors in possession, the disclosure process is expedited and

somewhat simplified, and the duties of a small business debtor are slightly different.

3. Chapter 11 "Individual" Case. Chapter 11 is also available to individuals and, because of debt limitations for debtors eligible to file under Chapter 13, Chapter 11 may be the only available bankruptcy chapter for some individuals. Similar to a business Chapter 11 case, an individual Chapter 11 DIP (or some other party) proposes a plan of reorganization which restructures the individual's debts and provides to pay creditors from the future income (or the sale of assets) of the debtor. As in Chapter 13, property of the estate includes the traditional property, as of the petition date, as set forth in § 541, but also all property acquired post-petition and all earnings from services performed by the debtor post-petition, but before the case is closed, dismissed, or converted.

4. Chapter 12. Chapter 12 provides for restructuring of the business or debts of family farmers or family fishermen. It is, in certain respects, an amalgamation of Chapter 11 and Chapter 13 with important differences applicable to farmers and farming businesses.

5. Chapter 13. Chapter 13 is an income-based debt restructuring for individuals. Only individuals with regular income and less than statutorily fixed maximum levels of noncontingent, liquidated, secured debt (generally, $1,184,200) and unsecured debt (generally, $394,725). Generally, an individual consumer debtor can discharge his or her debts by devoting all of his or her disposable income for a period from three to five years to payment of these debts under a plan.

V. Exemptions

Individuals are entitled to claim certain items of property as being exempt from distribution to creditors. Generally speaking, exemptions derive from the law of the state in which the debtor has lived for 730 days (2 years) prior to bankruptcy. If the debtor moved during that 730-day period, then exemptions apply for the state in which the debtor lived the majority of the 180 days *before* the 730-day period (§ 522(b)(3)(A)). If the foregoing residency requirement somehow renders the debtor ineligible for any exemption, then the debtor can choose federal exemptions. (§ 522(b)(3)).

At times a debtor will engage in certain pre-bankruptcy "planning" which, in the eyes of his or her creditors, unfairly manipulates the exemption laws in the debtor's favor. This issue often arises when the debtor, on the eve of filing bankruptcy, transforms substantial non-exempt property into exempt property.

Depending on the circumstances, such conduct could result in the debtor losing his exemption rights[2] or being denied a discharge.

In the homestead exemption context, Congress addressed fraudulent conduct by enacting Section 522(o). Under that section, if the debtor converted non-exempt real or personal property into exempt homestead property, with the intent to hinder, delay, or defraud creditors, within ten years prior to the petition date, then the debtor's homestead exemption is reduced by the amount of non-exempt property so converted.

The general rule for exemption planning is that the conversion of nonexempt assets to exempt assets, *standing alone*, is not necessarily fraudulent conduct. See In re Warren, 512 F.3d 1241 (10th Cir. 2008) (declining to find that conversion of nonexempt assets to exempt assets within one month of bankruptcy filing was fraudulent *per se*, but affirming denial of discharge based on additional factors showing fraudulent intent); In re Beverly, 374 B.R. 221, 245 (9th Cir. BAP 2007) (denying discharge where $1 million of debtor's nonexempt assets were exchanged for lesser amount of exempt assets in marital settlement agreement and substantial evidence of intent to avoid paying one substantial creditor).

Thus, there typically must be more than the act of transforming nonexempt property to exempt property to result in the disallowance of an exemption or the denial of the debtor's discharge, such as nondisclosure of assets, other evidence of an intent to keep a specific creditor from being paid, or irregular property transactions (such as selling property for substantially less than its value without justification). See In re Warren, 512 F.3d 1241 (10th Cir. 2008). When in doubt, remember bankruptcy courts are courts of equity and will usually recognize the principle of "too much," or, in agrarian terms: "when a pig becomes a hog it is slaughtered." In re Beverly, 374 B.R. at 245.

VI. Discharge and Denial of Discharge

A. General Overview of the Bankruptcy Discharge. Under 11 U.S.C. §§ 727, 1141(d), 1228, and 1328, the bankruptcy court must grant a discharge to an individual debtor unless one or more of the specific grounds for the denial of discharge is proven by a creditor or a trustee. Generally speaking, the discharge relieves the debtor from all debts that arose before the petition date. A discharge declares void any personal liability on a judgment pertaining to a discharged debt and operates as an injunction against any act to collect a discharged debt. The purpose of the discharge is to relieve the debtor of all legal responsibility for

[2] A debtor may also have his or her exemptions disallowed where there is evidence of bad faith in the debtor's failure to disclose the otherwise-exempt property. See Gillman v. Ford (In re Ford), 492 F.3d 1148 (10th Cir. 2007). However, the Supreme Court has ruled that exempt assets cannot be equitably surcharged as a sanction for a debtor's bad conduct, even where the debtor had fraudulently recorded (and defended) a second lien against his primary residence. See Law v. Siegel, 134 S. Ct. 1188, 1193-95 (2014) (holding that equitable surcharge contravened specific statutory provisions in 11 U.S.C. § 522(k)).

discharged debt, and to assist in generating a “fresh start” for the debtor. The discharge is subject to two separate kinds of challenges, the first is a denial of discharge, and the second is nondischargeability of particular debts.

B. Denial of Chapter 7 Discharge. Creditors and/or the trustee may file a complaint objecting to discharge and asking that the debtor’s request for a discharge be denied. The statutory grounds for objecting to a discharge are found in 11 U.S.C. § 727. The most common of these grounds is for transfers of assets with actual intent to hinder, delay, or defraud creditors, fraudulent concealment of assets, failure to keep or preserve books and records, the making of a false oath in connection with the case, and failure to cooperate with the court and prosecution of the case. See Rupp v. Biorge (In re Biorge), 536 B.R. 24 (Bankr. D. Utah 2015) (evidence of intent to hinder or delay creditors from reaching assets is sufficient to deny discharge under 727(a)(2)(A), and reckless disregard for truth satisfies “knowingly and fraudulently” prong of 727(a)(4)(A)). A discharge will also be denied if the debtor has obtained a prior discharge in a chapter 7 or chapter 11 bankruptcy case commenced within the eight years preceding the petition.

The burden of proof for showing a denial of discharge is squarely on the objecting party, i.e. the creditor or the trustee, because courts generally construe the provisions granting discharge liberally. Generally speaking, the denial of discharge is disfavored and courts will construe such provisions strictly against the creditor or trustee.

C. Nondischargeability of Particular Debts. Certain types of debts are nondischargeable even though a debtor would have the right to receive a discharge of debts generally. Under 11 U.S.C. § 523, there are 19 categories of debts that are excepted from discharge. Such categories include debts for taxes, debts obtained by fraud, false pretenses, false representation, debts for “domestic support obligations”, and debts for willful and malicious injury to another entity or an entity’s property.

An action to determine whether a particular debt is excepted from a debtor’s discharge, which means a non-dischargeable debt, may be instigated by a creditor. Such an action is an adversary proceeding and must be initiated by filing a complaint in bankruptcy court within 60 days of the date first set for the meeting of creditors. The creditor seeking to have its debt excepted from discharge bears the burden of proof. To prevail in the action the creditor must only prove its case by a preponderance of the evidence. See Grogan v. Garner, 498 U.S. 279, 111 S. Ct. 654, 112 L. Ed.2d 755 (1991).

Note that fraudulent intent may be inferred from the totality of the circumstances. For an example of a bad check case, see Groetken v. Davis (In re Davis), 246 B.R. 646 (10th Cir. BAP 2000), in which the BAP discusses the kind of evidence that needs to be presented. The court held that fraudulent intent of a debtor may be inferred from the totality of the circumstances based upon the timing of the

presentation of a bad check, and not upon representations in the check or that the debtor made at the time of presentation of the check. See also Zions First Nat'l Bank v. Taylor (In re Taylor), 528 B.R. 826 (Bankr. D. Utah 2015) (court excepts debt from discharge under 523(a)(2)(A), rejects debtor's "pure heart, empty head" defense and holds that "willful blindness will not allow a debtor to avoid liability for his actions").

For domestic support obligations, §523(a)(15) no longer has a balancing test for dischargeability, resulting in property settlements and hold harmless provisions (which are in favor of a spouse, former spouse, or child of the debtor) arising from a divorce or separation being nondischargeable in Chapter 7. In addition, §523(c)(1) makes the nondischargeability of such debts (in Chapter 7) self-executing with no adversary proceeding required.

D. Chapter 13's Not-So-"Super" Discharge. BAPCPA all but eliminated the super discharge in a Chapter 13 by expanding the list of debts excepted from a Chapter 13 discharge under §1328(a). While the Bankruptcy Code, prior to BAPCPA, excepted from the Chapter 13 discharge only certain tax claims, support obligations, student loans, alcohol related injury claims, and restitution or criminal fines, BAPCPA greatly expanded the list in §1328(a)(2) and §1328(a)(4) to specifically include previously dischargeable tax claims, fraud claims, unlisted claims, fraud by a fiduciary claims, and restitution or damages claims in a civil action arising from willful or malicious acts by the debtor. In addition, the debtor's discharge is conditioned, by §1328(a), upon the debtor's certification that all domestic support obligations, both post-petition and those included in the Plan, have been paid.

Under §1328(a)(2), the discharge for taxes in Chapter 7 and 13 is now very similar. Chapter 13 is no longer available as a partial payment remedy, if the tax obligation arose from nonfiled returns or returns late-filed within two years of the petition date, and taxes with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat the tax.

E. Chapter 11 Individual Discharge. An individual debtor under Chapter 11 does not receive a discharge of debts upon confirmation of the debtor's plan. See 1141(d)(5). Instead, the individual Chapter 11 debtor must wait to receive the discharge until "all payments under the plan" have been "complet[ed]." Id.

Generally speaking, the foregoing rule (combined with Section 1129(a)(15)) requires a Chapter 11 individual debtor to pay 5 years of projected disposable income[3] to receive a discharge. However, the Court may grant a Chapter 11

[3] While it may be argued that a Chapter 11 individual debtor is subject to the same "projected disposable income" requirements as a Chapter 13 debtor (such as means test-based expenses as opposed to judicially-determined expense standards), at least one bankruptcy court in the 10th Circuit has rejected that argument. See In re Roedemeier, 374 B.R. 264 (Bankr. D. Kan. 2007) (criticized on other grounds by In re Stephens, 704 F.3d 1279 (10th Cir. 2013) (holding that absolute priority rule applies to individual

discharge on the effective date of the plan where "all payments under the plan" have been completed on the effective date (such as where all estate assets are transferred to a liquidating trustee and no further payments will be made by the debtor), or where "cause" has been shown for the entry of a discharge prior to completion of all payments under the plan. See In re Sheridan, 391 B.R. 287 (Bankr. E.D.N.C. 2008).

Also, the Court can provide for an early discharge to an individual debtor who has not completed payments under a confirmed plan if (1) the value of what creditors have received under the plan is at least as much as they would have received in a Chapter 7 liquidation (with the measuring date for value being the effective date of the plan), and (2) modification of the plan is not practicable.

VII. The Automatic Stay

A. Broad and Automatic. As noted above, section 362(a) of the Bankruptcy Code imposes a broad-ranging stay of proceedings and actions against a debtor and its property. The stay is automatically imposed upon the filing of a bankruptcy petition.

B. Exceptions. Section 362(b) provides for certain exceptions to the stay. These include criminal actions against the debtor, certain regulatory proceedings by government agencies, collection of alimony, and netting out of certain commodities contracts.

C. Relief from the Stay. A creditor must obtain relief from the stay before it can proceed against property or the debtor. Generally, relief from the stay may be obtained if (1) the property is not necessary to an effective reorganization (which is, of course, not difficult to do if the case is a liquidation under Chapter 7) and the debtor has no equity in the property or (2) for "cause," including lack of "adequate protection." Stay motions are heard on an accelerated basis by the bankruptcy court and by statute are to be heard no later than thirty days after a request is made for relief from the stay, although it is not uncommon for the court to hold a preliminary hearing on the motion within thirty days and then complete the hearing at a later date.

VIII. Claims

A. Proofs of Claim. The submission of claims through filing of proofs of claim is something virtually every attorney will be asked to do. It is through the claims process that the Trustee knows who to pay from the proceeds of liquidated assets or under a plan. In all but under Chapter 11, creditors must file claims to participate in the proceeds of the estate. In Chapter 11, a creditor need not file a claim if the debtor schedules the claim in an amount the creditor agrees with and

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Chapter 11 debtors, and thus no property held by debtor on petition date may be retained where dissenting class of creditors has not been paid in full)).

if the claim is not listed as "disputed," "unliquidated," or "contingent." Note that, in individual debtor cases, Rule 3001(c) has strict requirements concerning the supporting information that needs to be filed with a proof of claim, and the failure to include required information may preclude the creditor from later presenting the omitted information.

B. Secured Claim Issues. Secured claims are treated differently than unsecured claims, at least to the extent that they are secured.

1. Division into Secured and Unsecured Portions. Division of a secured claim into secured and unsecured portions. Under section 506(a), a claim is secured only to the extent that the collateral securing it fully covers the amount of the debt. If a claim is not fully secured, the portion in excess of the value of the collateral is treated as an unsecured debt. This is important because, generally, only fully secured claims are entitled to accrue interest and attorneys' fees.

2. Cash Collateral. In a typical Chapter 11 case (if there is such a thing), the DIP's accounts receivables and proceeds therefrom are encumbered by its lender. "Cash collateral" is cash and cash equivalents that the DIP and its lender have an interest in. In order for the DIP to use cash collateral, it must either obtain the lender's consent and/or it must obtain an order of the court authorizing the use of the cash collateral. In order to use cash, the DIP must show that the creditor's interest in the cash collateral is "adequately protected."

C. Priorities. Unsecured claims are paid according to their statutorily-determined priority. These priorities are set forth in sections 507(a) and 726. Generally, claims that arise during the bankruptcy case have the highest priority and are called "administrative expense" claims or simply "administrative" claims. Postpetition fees and expenses of the lawyers representing the Trustee or DIP are administrative claims, as are the typical operating expenses of a Chapter 11 DIP. Next in priority are pre-petition wages of the DIP's employees (up to a statutory amount), then fringe benefits of such employees (again to a statutorily-determined amount), then miscellaneous types of claims, and, finally, most unpaid prepetition taxes.

IX. Using, Selling, or Leasing Property and Postpetition Financing

A. Use, Sale, and Lease of Property. Section 363 governs using, selling, and leasing property. Cash collateral, discussed above, is an important part of this. A DIP can use property of the estate in the ordinary course of business without court approval in Chapter 11 or 13, while there is generally no ordinary course of business in Chapter 7. Sales free and clear of liens and encumbrances are authorized by section 363 in certain situations.

B. Postpetition Financing. Section 364 governs postpetition financing. A Chapter 11 DIP can incur unsecured debt in the ordinary course of business (such as open account financing) without court approval. Court approval is required for all other financing, whether secured or unsecured. If a DIP can obtain financing in no other way, it can even give a prior lien to a new creditor if certain showings can be made. The profitable "DIP lending" is conducted under the auspices of section 364 of the Bankruptcy Code.

X. Avoiding Powers Or, Nasty Things that Can Happen to the Uninitiated and Unwary, and for that Matter, the Initiated and Wary Or, How Can They Do that to Me?

A. Avoiding Powers, Generally. The Bankruptcy Code provides an arsenal of avoiding powers to the Trustee or DIP. These include avoidance of "preferences," "fraudulent transfers," and "unauthorized postpetition transfers," and the undoing of "executory" contracts and unexpired leases. Under the so-called strong-arm provisions, the Trustee is endowed with the powers and leverage of an ideal, hypothetical intervening lien creditor, a judgment creditor, a bona fide purchaser of real property, and virtually any avoiding power under state law. Why? Because equally placed creditors are to be treated equally and, if a creditor receives a beneficial position within a certain period before bankruptcy, this policy of equal treatment is violated.

B. Preferences. Under section 547(b) an avoidable preference is a transfer of property of the debtor, to or for the benefit of a creditor, on account of antecedent debt, made while the debtor was insolvent (insolvency is rebuttably presumed for the ninety days prior to bankruptcy), made within ninety days (or, if the preference recipient is an insider, within one year), that enables the creditor to receive more than it would have received in Chapter 7. Each element of a preference must be found. The lack of any element makes a transfer unavoidable. Transfers of property amounting to avoidable preferences can include the perfection of a security interest, obtaining a judgment, or obtaining a security interest.

C. Defenses to Preferences. Because of the significant imposition preference liability can be for an entity doing business with a financially distressed company, and to encourage companies to continue to do business with such distressed companies, there are a number of effective defenses to a preference action under section 547(c). Included most prominently among these are the following.

1. Ordinary course. If a transfer was incurred and paid in the ordinary course of business of the parties, or in line with terms utilized in the industry, the transfer may not be avoidable.

2. Contemporaneous exchange. If the parties contemplated that they would make a substantially contemporaneous exchange and if, in fact, the

transaction involved a substantially contemporaneous exchange, the transfer cannot be avoided as a preference.

3. New value. If, after receiving a transfer that would be a preference, the creditor advances new value to the debtor, its preference liability is reduced to the extent of the new value.

D. "Fraudulent" Transfers. The term "fraudulent transfer" sounds ominous. Under section 548 and section 544(b), which essentially incorporates state law, fraudulent transfers can be set aside by a bankruptcy court to the theoretical benefit of creditors who were harmed by the transfer. There are two types of fraudulent transfer: one involving actual fraudulent intent and the other involving "constructive" fraud.

1. Actual Fraud. If a debtor engages in a transaction with intent to hinder, delay, or defraud its creditors, the transaction can be avoided as a fraudulent transfer. Remember, it is not just defrauding its creditors, it also can be hindering or delaying its creditors. Case law developed a wide-ranging list of "badges" of fraud because fraudulent intent was often difficult to prove directly.

2. Constructive Fraud. Because it is often difficult to prove actual fraud, the concept of constructive fraud developed. To be avoided as a fraudulent transfer, it must be proven that the debtor received less than "a reasonably equivalent value" and was insolvent at the time of the transfer, was rendered insolvent by the transfer, or was left with "unreasonably small capital" following the transfer. The easiest example of a constructively fraudulent transfer is the transfer for no or minimal consideration by one spouse to another or by a parent to a child of a significant asset, such as a house, when the transferring spouse or parent is insolvent.

3. The Rule in Moore v. Bay. State law generally allows an unsecured creditor to avoid a fraudulent transfer to the extent that that creditor has been damaged by that transfer. Almost all states have by now enacted a fraudulent transfer law, such as the Uniform Fraudulent Transfer Act. In Utah (as of May 9, 2017), the Uniform Voidable Transactions Act is the law. Under section 544(b) a Trustee in bankruptcy (including a DIP) can assert the rights of an unsecured creditor under state fraudulent transfer law. This is sometimes critical because state fraudulent transfer laws have longer statutes of limitation than section 548's two year limit. Although an unsecured creditor can avoid a fraudulent transfer only to the extent of its damage (if it is owed $1.00 it can avoid a $1 billion fraudulent transfer only to the extent of $1.00). Under the 1931 United States Supreme Court decision in Moore v. Bay, 284 U.S. 4 (1931), however, a Trustee in bankruptcy, standing in that same creditor's place, can avoid the entire $1 billion fraudulent transfer.

4. The BFP Decision. Prior to the United States Supreme Court's decision in BFP v. Resolution Trust Corporation, 511 U.S. 531 (1994), many decisions had followed the Fifth Circuit's lead in Durrett v. Washington National Insurance Co., 621 F.2d 201 (5th Cir. 1980), by holding that a foreclosure under state law could be a fraudulent transfer if the debtor was insolvent at the time and the foreclosure resulted in less than reasonably equivalent consideration being provided. The Supreme Court ruled, however, that a foreclosure regularly conducted, and in compliance with state law, in which there is no collusion is presumptively not a fraudulent transfer.

5. Upstream and Cross-stream Transactions. Often subsidiaries and affiliates are called upon to provide guarantees of parent or sister corporations' debts. If the subsidiary is insolvent when it provides this guaranty for its parent or affiliate, it is almost certainly a fraudulent transfer because it does not receive reasonably equivalent consideration for the guarantee.

E. Section 544(a). Under section 544(a) of the Bankruptcy Code, a Trustee in bankruptcy (including a DIP in possession) is endowed with the rights and powers of a hypothetical intervening lien creditor, a judgment lien creditor, and a creditor who advances credit, all as of the bankruptcy petition date. Thus, for example, if a secured creditor fails timely to perfect a security interest under the Uniform Commercial Code, the Trustee can "avoid" the perfection of the security interest and render the secured creditor unsecured. Similarly, if a properly perfected security interest is later terminated by an erroneously filed UCC-3, the mistake cannot be corrected post-petition. See Official Committee of Unsecured Creditors v. JPMorgan Chase Bank, N.A. (In re Motors Liquidation Co.), 777 F.3d 100 (2d Cir. 2015) (holding that creditor authorized the filing of UCC-3 termination statement, even though it never intended to terminate the security interest related to the loan in question).

F. Section 544(b). Under the so-called "strong-arm" powers of the Bankruptcy Code, the Trustee in bankruptcy can stand in the shoes of an unsecured creditor at state law to avoid transactions under state law.

XI. Dismissal and Conversion. If a case is not progressing well, if there is incompetence or dishonesty in management of the company, or for various other reasons, the Court can dismiss a bankruptcy case or, if it is a case under Chapter 11 or 13, convert the case to a case under Chapter 7.