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BANKRUPTCY

Bankruptcy Update

By: Keith Langley

The Automatic Stay

The automatic stay is perhaps the most fundamental protection for a debtor in bankruptcy. As many of us have experienced, the automatic stay is a pause button at the time of a bankruptcy filing that precludes a creditor from making demands, filing liens, or proceeding with lawsuits. The stay, however, is not an infinite bar. Rather, there are many caveats and conditions that warrant a bankruptcy court providing relief to a creditor to move forward with claims. This often takes the form of allowing a lawsuit to continue or foreclosure of collateral. Last month, the US Supreme Court –- in an opinion authored by Justice Ginsburg –- clarified that a creditor does have immediate appellate rights when a Bankruptcy Court denies relief from the automatic stay, and more importantly, that an appeal is waived if not instituted quickly.

Generally speaking, a party does not have a right to appeal every adverse decision that occurs in litigation. In most cases, a party has to wait for a final order or judgment before exercising its appellate rights. In the bankruptcy context, there has been confusion on what constitutes an appealable order. In the automatic stay context, there was some thought that denial of relief from the stay was not appealable because the creditor still had avenues for recovery in the bankruptcy court itself. Most notably, the creditor had the right to assert a claim, which would then be adjudicated (if disputed by the debtor) under the relevant bankruptcy rules.

The Supreme Court was confronted with a situation where a creditor was denied stay relief and then elected to go through the claim process, believing that the denial order was not appealable since it was not "final." In that case, the creditor moved forward through the claim process, but ultimately had its claim denied by the bankruptcy court following a contested adversary proceeding. It was at that point that the creditor sought to appeal the denial of stay relief. The bankruptcy court noted that the creditor missed its opportunity to appeal and should have done so sooner; this was ultimately affirmed by the District Court and the Sixth Circuit. In somewhat of a surprise move, the US Supreme Court decided to weigh in on the issue (most likely because of the confusion among the various courts about what is and is not appealable). The Court sided with the Bankruptcy Court and Sixth Circuit, holding that the creditor missed its opportunity. While it recognized that finality is a condition precedent to any appeal, it found that an order denying stay relief was appealable because it finally resolves a discrete issue within a bankruptcy case. The Court reasoned that adjudicating the merits on a stay relief motion is a distinct procedural unit, which carries with it notice, a hearing, and a legal determination of a creditor's rights under the Bankruptcy Code. Further, because the automatic stay bars any efforts to address or control the debtor's assets, the bankruptcy court is the only place that a motion for stay relief could be brought. Thus, when relief is denied, that is the end of the story on that particular issue.

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The only caveat that the Supreme Court included (by way of a footnote) is that it was not necessarily deciding the finality of an order that allowed for a creditor to seek the same relief based on a change in circumstances in the case. Indeed, as part of getting stay relief, a creditor typically argues that there is not a realistic chance that a bankruptcy plan could be confirmed. This changes sometimes as a bankruptcy unfolds. Thus, the practice point is to ensure that you have a savings language in any proposed order to the Court. Or, when in doubt, make sure that you preserve any appellate rights by immediately challenging an adverse order.

The Supreme Court's opinion is *Ritzen Group, Inc. v. Jackson Masonry, LLC*, 18-938, 2020 WL 201023 (U.S. Jan. 14, 2020).

Involuntary Bankruptcy

A creditor does not have standing under Section 303(b)(1) of the Bankruptcy Code to file an involuntary bankruptcy petition against a debtor because a portion of the creditor's claim was subject to a bona fide dispute. *Montana Department of Revenue v. Blixseth*, 942 F.3d 1179 (Ninth Circuit 2019). In the Blixseth case, the alleged debtor had more than 12 creditors as of the petition date and so three petitioning creditors needed qualifying claims for the involuntary bankruptcy to proceed. The Bankruptcy Court determined that Bankruptcy Code, Section 303(b)(1) disqualifies a claim based on any bona fide dispute as to amount, even if some portion of the claim is undisputed. The Bankruptcy Court stated that Montana had not showed that it was authorized to create a separate liability for an undisputed issue or if authorized that it took the proper steps to create the separate liability. Accordingly, there was one claim for one tax year, and the entire claim amount was disputed. The Appellate Court had to determine whether Montana's claim for the 2004 tax year was subject to a bona fide dispute as to amount notwithstanding Blixseth's concession that the deduction challenged in one issue was improper (which rendered a $200,000 amount). After the BAPCPA Amendment in 2005, and based upon the language of the code itself, in following the First and Fifth Circuits, the Court found that the plain meaning of the statute meant that a claim subject to a bona fide dispute means that creditor lacks standing. The Court found that the Montana creditor sought to influence Blixseth on the total tax year of 2004. This it found was prohibited.

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