

Representing Bankruptcy Post-Confirmation Liquidation and Litigation Trusts

Structuring the Entity Agreement, Managing the Trust,
and Representing the Trust as General or Special Litigation Counsel

TUESDAY, AUGUST 11, 2015

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

Amanda Demby, Director, **Province**, Las Vegas

Steven T. Gubner, Partner, **Ezra Brutzkus Gubner**, Woodland Hills, Calif.

Peter Kravitz, Principal, **Province**, Las Vegas

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REPRESENTING BANKRUPTCY POST- CONFIRMATION LIQUIDATION AND LITIGATION TRUSTS

**STRUCTURING THE ENTITY AGREEMENT,
MANAGING THE TRUST, AND REPRESENTING
THE TRUST AS GENERAL OR SPECIAL
LITIGATION COUNSEL**



Steven T. Gubner, Esq.



PROVINCE

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**Peter Kravitz, Esq.
Amanda Demby**

WHO WE ARE

Peter Kravitz, Esq. (Principal, Province, Las Vegas and New York):

The focus of Mr. Kravitz' national practice is dedicated to serving as a Chief Restructuring Officer; Chapter 11/Liquidating Trustee/Plan Administrator; Disbursing Agent; member of bankruptcy oversight and creditor committees; and member of Boards of Directors where his legal and business backgrounds are well served. These efforts were recognized during both the 11th and 12th Annual M&A Advisor Awards where the Firm was a repeat Finalist for Restructuring Deal of the Year.

Amanda Demby (Director, Province, Los Angeles and New York):

Ms. Demby's primary focus concerns claim pool analysis, reconciliation and the orderly administration of an estate from start to finish. Ms. Demby has provided services as the Financial Advisor, Plan Administrator/Liquidating Trustee for various Chapter 11 liquidations. She manages claim reconciliation and provides analysis and support in the objection process, and oversees wind-down tasks and has experience in employee benefit plan terminations, asset liquidations, and document retention and destruction.

Steven T. Gubner, Esq. (Managing Partner, Ezra Brutzkus Gubner LLP, Los Angeles and Las Vegas):

Mr. Gubner regularly represents liquidating trustees in the disposition of assets, and the prosecution and resolution of large claims resulting in significant distributions to beneficiaries. He was recently counsel to Al Siegel, trustee in the mega-chapter 11 Circuit City filing, obtaining significant, multi-million dollar recoveries from insurance companies, and prosecuting numerous class action claims on behalf of the trust; to Peter Kravitz, trustee of the Fleetwood Liquidating Trust as the successor to Fleetwood Enterprises Inc. and its related entities; and Howard Grobstein, trustee in New Meatco Provisions, LLC.

WHAT IS A POST-CONFIRMATION LITIGATION/LIQUIDATION TRUST ?

- Trusts are separate and distinct legal entities and are created for the benefit of a Debtor's creditors to prosecute certain causes of action and/or liquidate assets that are transferred to the Trust, usually as a result of a Debtor's confirmed plan.
- The creation of Trusts are authorized under section 1123(b)(3)(B) of the Bankruptcy Code, which provides that “.. a plan may provide for the retention and enforcement by the debtor, by the trustee, or by a representative of the estate appointed for such purpose, of any such claim or interest...”
- The ultimate goal is to make pro-rata distributions to the Trust beneficiaries (holders of claims against the pre-confirmation Debtor)

WHAT IS A POST-CONFIRMATION LITIGATION/LIQUIDATION TRUST ?

- See, e.g. *In re Acequia, Inc.*, 34 F.3d 800, 807-08 (9th Cir. 1994): “[The] aim [of section 1123(b)(3)(B)] was to make possible the formulation and consummation of a plan before completion of the investigation and prosecution of causes of action such as those for previous insider misconduct and mismanagement of the debtor. Thus, the statute was in furtherance of the purpose of preserving all assets of the estate while facilitating confirmation of a plan.”

WHY ARE POST-CONFIRMATION TRUSTS CREATED?

- Trusts allow a bankruptcy estate to end its existence, and as a result, the Debtor loses its status as a debtor-in-possession. However, the bankruptcy case remains open until a final decree is entered, which provides for continuing Bankruptcy Court jurisdiction.
- Trusts provide a mechanism by which the Debtor's creditors can maximize their recovery by liquidating Debtor's assets and causes of action, and minimize costs associated with Bankruptcy Court oversight approval of that process.

HOW CAN THESE TRUSTS BE CREATED?

- Trusts are created by contract
- Created by an agreement between creditors and other parties-in-interest, usually through a confirmed Chapter 11 Plan
- However, a confirmed plan is not the only way a Trust can be created:
 - Structured Dismissals
 - Settlement Agreements

WHAT ARE SOME KEY PROVISIONS THAT NEED TO BE CONSIDERED WHEN CREATING A TRUST?

- Most Trusts (almost all) are considered Grantor Trusts (Treasury Regulation § 301.7701-4(d) and Revenue Procedure 94-45).
 - Debtor/Estate Assets → Creditors → Trust
 - Assets are transferred first to Creditors, then into the Trust
 - Creditors become owners/beneficiaries of the Trust
 - As a result, the Trust does not generate its own tax liabilities and the Trust is enabled to make pro-rata distributions to its Beneficiaries (the former Debtor's Creditors)

WHAT ARE SOME KEY PROVISIONS THAT NEED TO BE CONSIDERED WHEN CREATING A TRUST?

- The Trust should have the authority to retain Debtor's former-key employees as consultants (independent contractors) and to hire all professionals necessary to accomplish the Trust's goals
 - Professionals add value to the Trust because of their knowledge of bankruptcy laws/rules/statutes and other applicable governing provisions/statutes
 - Independent Contractors have the historical background and knowledge

WHAT ARE SOME KEY PROVISIONS THAT NEED TO BE CONSIDERED WHEN CREATING A TRUST?

- Another important provision to consider is whether or not an Oversight Committee should be established. Most Trusts either provide that the Trustee has a high degree of discretion in the management of the Trust, or that the Trustee will be required to seek the approval of an Oversight Committee for transactions rising above a pre-determined threshold
 - What are some of the pros/cons of Oversight Committees?

WHAT ARE SOME KEY PROVISIONS THAT NEED TO BE CONSIDERED WHEN CREATING A TRUST?

- In creating a Trust, one should consider the Trustee's responsibility and liability when something goes wrong
 - Trustee acts a fiduciary to the Trust's beneficiaries
- See, e.g. *In re Fruehauf Trailer Corp.*, 369 B.R. 817, 831 (Bankr. D. Del. 2007): “[a] trust is defined as a fiduciary relationship with respect to property, subjecting the person with legal title to equitable duties to deal with the property for the benefit of another person, ‘which arises as a result of a manifestation of an *intention* to create it.’ ”

WHAT ARE SOME KEY PROVISIONS THAT NEED TO BE CONSIDERED WHEN CREATING A TRUST?

- The Trust agreement may (and usually does) include indemnity provisions which limit the Trustee's liability (subject to certain limitations), and which may have the effect of potentially deterring nuisance lawsuits against the Trustee

DURATION OF THE TRUST

- **Some Trusts may endure for a long time, during which there may be little to no activity, while the Trust is waiting on the results of a litigation matter or the liquidation of a certain asset**
 - Smart budgeting is very important during these lulls so that the Trust is able to pay all necessary fees to remain open (U.S. Trustee, etc...)

TRUST DISTRIBUTIONS TO BENEFICIARIES

- **To receive a distribution, a Trust creditor/beneficiary must have an allowed claim in the former Debtor's estate.**
- **Usually in a Chapter 11 case, the Court will enter a Claims Bar Date Order which will set a deadline to file proofs of claim.**
 - But what happens if a claim is filed late?

TRUST DISTRIBUTIONS TO BENEFICIARIES

- **Should the Trust make interim distributions or just one distribution when it has liquidated all assets assigned to it?**
 - Can distributions be made while reserving funds for disputed claims?
- **What should be done with unclaimed property/distributions?**
 - Can effective drafting of a Trust agreement help resolve these issues before they arise?

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Scheduled vs. Filed Claims**
 - Reconciliation of claims is based mainly on Debtor's books and records. The Trust's employment of Debtor's former employees as independent contractors is extremely helpful during this process.

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Objecting to Claims**
 - Non-Substantive Objections
 - Duplicate(s), Amended/Superceded, Late-filed
 - Substantive
 - Books and Records, Litigation

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Objecting to Claims**
 - Omnibus Claims Objections
 - What are the benefits?
 - Amending Schedules vs. Objecting to Scheduled Claims
 - The procedure depends on the pertinent Local Rules

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Contingent/ Unliquidated/ Disputed Claims**
 - Some claims of beneficiaries may be contingent (depends on some event that hasn't yet occurred, and may not ever occur), unliquidated (amount of claim is undetermined) or disputed (the Trustee does not agree with the amount claimed by a certain creditor)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Contingent/ Unliquidated/ Disputed Claims**
 - For example, a secured creditor whose claim is secured by a real property may be permitted to collect post-petition interest, the Bankruptcy Code does not specify the timing regarding the determination of a claimant's secured status and the value of the collateral
 - Most courts seem to support a flexible approach. See, e.g., *In re Sroka*, 2014 WL 2808101, at *4 (Bankr. M.D. Fla. 2014): “In Chapter 11 cases, the valuation date appears fluid, with courts generally opting for one of four dates: the petition date, valuation hearing date, confirmation date, or plan's effective date.”
 - But what about attorneys' fees?

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Contingent/ Unliquidated/ Disputed Claims**
 - Unliquidated claims and estimation motions
 - Claims must be liquidated so that the Trust has a definitive claims pool. With respect to unresolved claims, this usually occurs through estimation motions
 - Section 502(c) of the Bankruptcy Code provides:
“There shall be estimated for purpose of allowance under this section— (1) any contingent or unliquidated claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case; or (2) any right to payment arising from a right to an equitable remedy for breach of performance.”

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Contingent/ Unliquidated/ Disputed Claims**

- Unliquidated claims and estimation motions
 - The court may estimate contingent or unliquidated using whatever method is best suited to the particular contingencies at issue. The principal consideration must be an accommodation to the underlying purposes of the Code. In accomplishing this task, the estimating court is bound by the legal rules which may govern the ultimate value of the claim. For example, when the claim is based on an alleged breach of contract, the court must estimate its worth in accordance with accepted contract law.

In re Fed.-Mogul Global, Inc., 330 B.R. 133, 155 (D. Del. 2005)

- Section 502(c)(1) is designed to avoid the need to await the resolution of outside lawsuits to determine issues of liability or amount owed by means of anticipating and estimating the likely outcome of these actions. By so doing, the trustee can more rapidly determine the payout to each creditor who, in the meantime, receives no interest on its claim. Second, Section 502(c)(1) is designed to promote a fair distribution to creditors through a realistic assessment of uncertain claims.

In re Ford, 967 F.2d 1047,1053 (5th Cir.1992)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Contingent/ Unliquidated/ Disputed Claims**
 - Disputed Claims Process
 - Upon the creation of a Trust, there may be claims objections pending, or the Trust itself may want to object to certain claims. The Trustee will need to establish sufficient reserves to pay those claims at face value, if objections are not sustained
 - What are some considerations that you should take into account when establishing a claims reserve?

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - Trustee should be vested with the discretion to investigate and pursue all potential causes of action without the need for further approval from the Bankruptcy Court
 - Reduction of claims as a form of affirmative recovery
 - How do you value the amount of reduction?

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Post-confirmation Bankruptcy Court Jurisdiction**
 - The jurisdiction of the non-Article III bankruptcy courts is limited after confirmation of a plan. But where there is a **close nexus** to the bankruptcy plan or proceeding, as when a matter affects the interpretation, implementation, consummation, execution, or administration of a confirmed plan or incorporated litigation trust agreement, retention of post-confirmation bankruptcy court jurisdiction is normally appropriate.
 - Whether a matter has a close nexus to a bankruptcy plan or proceeding is particularly relevant to situations involving continuing trusts, like litigation trusts, where the plan has been confirmed, but former creditors are relegated to the trust res for payment on account of their claims. To a certain extent, litigation trusts by their nature maintain a connection to the bankruptcy even after the plan has been confirmed. The question is how close a connection warrants post-confirmation bankruptcy jurisdiction. Matters that affect the interpretation, implementation, consummation, execution, or administration of the confirmed plan will typically have the requisite close nexus. Under those circumstances, bankruptcy court jurisdiction would not raise the specter of “unending jurisdiction” over continuing trusts.
 - *In re Resorts Int'l, Inc.*, 372 F.3d 154 (3d Cir. 2004)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Post-confirmation Bankruptcy Court Jurisdiction**
 - The implementation of the payment of unsecured creditors through claims prosecuted by the Litigation Trustee ...falls squarely in the realm of limited jurisdiction that a bankruptcy court may hear. In addition, this type of proceeding, avoidance of a fraudulent transfer, is deemed a core-proceeding under the Bankruptcy Code.

In re Railworks Corp., 325 B.R. 709, 723 (Bankr. D. Md. 2005)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- Investigation and pursuit of claims and causes of action
 - Post-confirmation Bankruptcy Court Jurisdiction

For example:

- *In re BWI Liquidating Corp.*, 437 B.R. 160 (Bankr. D. Del. 2010) – Bankruptcy Court could not exercise post-confirmation, “related to” jurisdiction over breach of contract claims (arising from pre-petition conduct) filed by liquidating trust established under debtors' confirmed plan, even though successful prosecution of claims had potential to increase the assets of trust available for distribution to creditors.
 - Plaintiff asserted that its claims arose from pre-petition conduct, so claims could have been brought pre-confirmation, and therefore, there was a “close nexus”
 - Court held that timing of the conduct alleged in the complaint is not a factor to be considered in determining whether there is a “close nexus.”
 - Court ultimately concluded that Plaintiff could not establish a “close nexus” sufficient for it to properly assert subject matter jurisdiction over the claims.

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - Post-confirmation Bankruptcy Court Jurisdiction

For example:

- *In re The Fairchild Corp.*, 452 B.R. 525, 532 (Bankr. D. Del. 2011) – Trust filed complaints post-confirmation even though the agreements were created prepetition and the breach arguably occurred before confirmation of the plan. Trust asserted that the funds recovered from the adversary proceedings would enhance the estate and allow for a greater distribution for creditors. However, the potential to increase recovery for trust beneficiaries cannot be sufficient, in and of itself, to establish a close nexus because it would create a broader jurisdiction than Congress intended. Moreover, Debtors' plan only included a broad general retention of jurisdiction provision and failed to mention the properties or breach of contract claim. Such a general retention of jurisdiction is insufficient for this Court to retain “related to” jurisdiction.
 - So “benefit to creditors/beneficiaries” is not a likely basis, in and of itself, for a Bankruptcy Court to conclude that it may properly assert “related to” jurisdiction over a post-confirmation claim.

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Post-confirmation Bankruptcy Court Jurisdiction**
 - **Specific assignment of claims to the Trustee and reservation of jurisdiction:**
 - *In re Consol. Meridian Funds*, 511 B.R. 140, 146 (W.D. Wash. 2014): Where a claim is specified in the Plan and reserved for prosecution by the trustee on behalf of the creditors, such facts support “related to” jurisdiction...Unlike a claim that arose post-confirmation, a claim that was considered by the bankruptcy court when confirming the Plan is not the independent initiative of the trustee, but rather a claim that formed part of the calculus of the parties when negotiating the Plan and the pursuit of which is part of the Plan execution and/or implementation. By specifically identifying and reserving a claim as a potential asset of the estate to be pursued for the benefit of the estate's creditors, the parties make clear that the claim is “related to” the bankruptcy Plan or proceeding.
 - Important for the Plan to specifically assign known causes of action to a Trust to avoid any potential jurisdiction issues!

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - Post-confirmation Bankruptcy Court Jurisdiction
 - But the Bankruptcy Court cannot create jurisdiction.
 - “...if a court lacks jurisdiction over a dispute, it cannot create that jurisdiction by simply stating it has jurisdiction in a confirmation or other order.”
 - “If there is no jurisdiction under 28 U.S.C. § 1334 or 28 U.S.C. § 157, retention of jurisdiction provisions in a plan of reorganization or trust agreement are fundamentally irrelevant. But if there is jurisdiction, we will give effect to retention of jurisdiction provisions.”
 - *In re Resorts Int'l, Inc.*, 372 F.3d 154 (3d Cir. 2004)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- Investigation and pursuit of claims and causes of action
 - Unique Claims and Issues that May Arise
 - The Worker Adjustment and Retraining Notification Act (WARN) protects workers, their families, and communities by requiring most employers with 100 or more employees to provide notification 60 calendar days in advance of plant closings and mass layoffs. Are these employees entitled to administrative claims? Courts say no.
 - Pre-petition employees not entitled to administrative expense priority status based upon claimed WARN Act damages. In terms of priority, a claim for severance pay will only have administrative priority to the extent that it is based on post-petition services.” Because the [employee] was terminated pre-petition, his WARN Act damages vested pre-petition, and therefore were not administrative expense claims.
 - Pre-petition WARN damages are not necessary to maintain the debtor as a going concern, nor are they necessary to preserve the bankruptcy estate during the liquidation process. *In re First Magnus Fin. Corp.*, 403 B.R. 659, 665-66 (D. Ariz. 2009)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- Investigation and pursuit of claims and causes of action
 - Unique Claims and Issues that May Arise
 - But secured creditors **may be liable** for WARN act damages:
 - “For the purpose of determining when a defendant becomes an employer under WARN, we see no reason for drawing a distinction between a “fiduciary” in bankruptcy who takes control of a debtor's assets and a creditor who exercises control over collateral securing a delinquent loan. ...WARN's obligations indeed can apply to a secured creditor, but only where the creditor operates the debtor's asset as a “business enterprise” in the “normal commercial sense.” On the other hand, where the creditor does no more than exercise that degree of control over the debtor's collateral necessary to protect the security interest, and acts only to preserve the business asset for liquidation or sale, the notice requirement of WARN will not apply” *Chauffeurs, Sales Drivers, Warehousemen & Helpers Union Local 572, Int'l Bhd. of Teamsters, AFL-CIO v. Weslock Corp.*, 66 F.3d 241, 244 (9th Cir. 1995)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Unique Claims and Issues that May Arise**
 - What about Debtors that work closely with lender's pre-petition and terminate employees in a such a manner as to avoid any secured claim against the Debtor and/or lender?
 - Is it wise to terminate the employees pre-petition?
 - Settle these claims early in the case?

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Unique Claims and Issues that May Arise**
 - Large retailers often sell gift cards which are usually intended as gifts for third-parties unknown to the retailer/Debtor. Issues arise when these gift card holders did not receive notice of the bankruptcy case or a claims bar date, but allege that they were entitled to that notice and as such should be permitted to file late claims. Courts have held that these gift card holders are not “known creditors” that are entitled to notice because the Debtor does not actually know the identity of the gift-card holder.

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Unique Claims and Issues that May Arise**
 - It is long-held that known creditors must be afforded notice “reasonably calculated, under all the circumstances to apprise” them of the pendency of the Bar Date.
 - Several basic principles underlie the determination of whether a creditor is “known” or “unknown” to the debtor... a “known” creditor includes both a claimant whose identity is actually known to the debtor or a claimant whose identity is “reasonably ascertainable” by the debtor. An “unknown” creditor is a claimant whose identity or claim is not “reasonably ascertainable” or is merely “conceivable, conjectural or speculative.” A creditor is “reasonably ascertainable” if the debtor can uncover the identity of that creditor through “reasonably diligent efforts.” Reasonable diligence does not require “impracticable and extended searches ... in the name of due process.” A debtor does not have a “duty to search out each conceivable or possible creditor and urge that person or entity to make a claim against it.” *In re XO Commc'ns, Inc.*, 301 B.R. 782, 793 (Bankr. S.D.N.Y. 2003)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- **Investigation and pursuit of claims and causes of action**
 - **Unique Claims and Issues that May Arise**
 - “...Gift Card Holders' status as possible creditors was not known or reasonably ascertainable to the Debtors. As an initial matter, gift cards, as their name illustrates, are not intended to be used by the purchaser but are instead intended as gifts, so even if the Debtors were able to identify the purchasers of the Gift Cards, they would have no way of tracing the ultimate recipients. And, in fact, the Gift Card Holders, by their own admission, received their Gift Cards as gifts. Therefore, the Debtors had no way of tracing their identities.”
 - “...the Court finds that the Gift Card Holders were unknown creditors and only entitled to constructive notice of the General Bar Date, which they received through the Publication Notice.... The Debtors were not required to provide notice of the kind required for known creditors to unknown creditors. ... Because the Gift Card Holders were unknown creditors, and the Debtors had no reasonable method for ascertaining addresses or identifying information for them, the Debtors were required to provide only constructive notice of the General Bar Date to them.
 - *In re BGI, Inc.*, 476 B.R. 812, 821 (Bankr. S.D.N.Y. 2012)

THE PROCESS OF RECONCILING AND RESOLVING CLAIMS

- Investigation and pursuit of claims and causes of action
 - Unique Claims and Issues that May Arise
 - If the Debtor knows the amount of outstanding gift cards, should there be amounts reserved or set aside for people who may make late claims?
 - Are gift card claims entitled to priority status under 11 U.S.C. § 507(a)(7)?
 - “In the case of *In re WW Warehouse, Inc.*, 313 B.R. 588 (Bankr. D. Del.2004) the court held that claims based on gift certificates to purchase merchandise from retailer that had not been redeemed when the bankruptcy petition was filed were entitled to 507(a)(7) priority status despite the fact that they were not based on down payments or partial payments. In order to reach its decision the *WW Warehouse* court examined the legislative history of the statute and concluded that the same was passed to give priority to consumers who found themselves in the same position as gift certificate purchasers, that is, those who paid money on lay away plans or made deposits on merchandise assuming their deposit was tantamount to a trust fund and because of their ignorance and inability to bargain with a retail merchant, are unable to do a credit investigation or obtain special terms from the merchant, as a true creditor may do. 313 B.R. at 594.” *In re Palmas del Mar Country Club, Inc.*, 443 B.R. 569, 573-74 (Bankr. D. P.R. 2010)
 - See *also*, *Borders and Sharper Image Bankruptcies*

LIQUIDATING ASSETS

- Trust Assets.
 - Real/Tangible Assets:
 - Cash, Real Estate, Inventory, Furniture, Fixtures, Equipment, etc...
 - Intangible Assets: Causes of Action
- Trust's Standing to Pursue Causes of Action
 - Generally, a Trust only has standing to pursue the claims transferred to it. However, a Trust's standing to pursue claims cannot be any greater than the Debtor's standing to pursue those same claims. As discussed, if the Debtor lacked standing, a Trust agreement cannot confer standing upon the Trust simply because the Agreement was approved by a Bankruptcy Court.

LIQUIDATING ASSETS

- Trust's Standing to Pursue Causes of Action
 - A Trust does not have standing to pursue the direct claims of creditors, only claims that belonged to Debtor.
 - *Trenwick Am. Litig. Trust v. Ernst & Young, L.L.P.*, 906 A.2d 168, 191 (Del. Ch. 2006):
 - ...even if the Litigation Trust Agreement or plan of reorganization did expressly assign the direct claims of [Debtor's] creditors to the Litigation Trust, federal bankruptcy law is clear that litigation trusts do not have standing to pursue the direct claims of creditors ... the U.S. Supreme Court established that bankruptcy trustees and litigation trusts formed as part of reorganization plans do not have standing to bring direct claims belonging to creditors under the federal bankruptcy statute.
 - The U.S. Supreme Court explained that the bankruptcy statute authorized bankruptcy trustees or litigation trusts to bring only those claims belonging to the debtor at the time of the debtor's bankruptcy filing, but that it did not vest with trustees or litigation trusts standing to pursue separate claims belonging to others, such as the direct claims of individual creditors.

LIQUIDATING ASSETS

- Common Actions
 - Avoidance Actions, Fraudulent Transfers and Preference Claims
 - Usually, some of the most valuable assets transferred to a Trust are the rights to bring avoidance claims (preference and fraudulent transfer actions) to recover funds for the benefit of a Trust's beneficiaries. The transfer of these rights usually allow for an easier plan confirmation because unsecured creditors may not object to a plan if they feel as if they will receive a distribution from a Trust that may be created thereby.

LIQUIDATING ASSETS

- Breach of Fiduciary Duty Claims
 - Usually only brought when there is a sizeable D&O Policy that can be accessed
 - Unique Issues and Defenses
 - *Defendants wholly owned the pre-petition debtor. Do sole shareholders owe duties to company? See, e.g., GSM Wireless, Inc. v. Honarkar, 2013 WL 4017123 (Bankr. C.D. Cal. Apr. 5, 2013), where the court rejected a bankruptcy trustee's fiduciary duty claims on precisely these grounds. The trustee in that case had leveled fiduciary duty claims against the debtor's CEO and President, who were also its sole shareholders. In finding for the defendants, the court explained that, "if the shareholders unanimously consent to an action, even if the action is detrimental to the company, the action does not provide legal recourse to the corporation as a separate legal entity."*

LIQUIDATING ASSETS

- Breach of Fiduciary Duty Claims
 - Unique Issues and Defenses
 - *Insolvency.* When a corporation becomes insolvent, the fiduciary duties of its officers and directors inure to the benefit of its creditors. However, determining insolvency may present significant issues.
 - Must a solvency analysis be prepared in accordance with GAAP?
 - How should ongoing lease liabilities be treated?

LIQUIDATING ASSETS

- Breach of Fiduciary Duty Claims
 - Unique Issues and Defenses
 - *Duties Owed to Creditors*. Presuming that insolvency has been established, the scope of the duties owed to the creditors can vary depending on jurisdiction.
 - For example, in California (unlike Delaware), a director/officer duties' during insolvency are limited to duties not to dissipate or unduly risk assets that could otherwise be used to pay creditors.
 - This means that in California and like jurisdictions, a claim for breach may only typically arise when an officer/director self-deals with funds of the insolvent corporation.

LIQUIDATING ASSETS

- Malpractice Claims
 - Unique Issues and Defenses
 - *In pari delicto*. The Trustee may want to bring a cause of action against a Debtor's former agents, accountants, attorneys, etc... But, the *in pari delicto* defense bars a trustee from asserting causes of action that the Debtor itself could not assert because the Debtor was an equal participant in the pre-petition wrong doing that gave rise to the suit.
 - *In re Estate Fin. Mortgage Fund, LLC*, 565 F. App'x 628 (9th Cir. 2014)
 - Does this make sense from a policy stand-point?
Should a Trustee be tainted by a Debtor's conduct?
 - How can you craft a complaint to avoid dismissal based upon this defense at the early stage of a case?
 - Allege that the former's agents conduct was not so obviously wrongful that that the principals of the Debtor must have known the conduct to be wrongful/unlawful

LIQUIDATING ASSETS

- Tax Carry Back Claims

- Bankruptcy court has statutory authority to assign the tax refund claim (along with other claims) to a liquidating trust, and to appoint the Liquidating Trustee to pursue the claim. See 11 U.S.C § 1123(b)(3)(B).
- But until and unless a bankruptcy trustee files a refund claim with the IRS, the bankruptcy court lacks jurisdiction to *adjudicate* that claim.
- A bankruptcy court cannot, through confirmation of a reorganization plan, expand its own jurisdiction. Thus, although a Plan may stipulate that, post-confirmation, the bankruptcy court can “hear and determine matters concerning... federal taxes in accordance with Section [] ... 505 of the Bankruptcy Code,” that Plan provision does not expand jurisdiction beyond the statutory grant. *United States v. Bond*, 762 F.3d 255, 261 (2d Cir. 2014)
 - There, The failure of (debtor-in-possession) to file its refund claim with the IRS prior to Plan confirmation had a jurisdictional consequence that could not be cured by the Liquidating Trustee or a Plan provision.

LIQUIDATING ASSETS

- Commercial Tort Litigation
 - Class Action Participation
 - Trustees make great class representatives. Why?
 - Sophisticated professionals
 - Ability to monitor case and opt-out of class if beneficial to the Trust. The Trust does not usually need the non-monetary benefits of a class.
 - For example, Visa/MC Charge-Back Litigation, Lithium-Ion and Optical Disk Drive Price-Fixing Litigation
 - Trusts do not usually have the operational vendor pressure that operating businesses have
 - Trustees usually have a higher tolerance for litigation than a traditional class member

LIQUIDATING ASSETS

- Insurance Issues
 - Change in Control
 - A change in control under a D&O policy may be triggered in many ways during the restructuring of a company (both in and out of Court)
 - In most Chapter 11 cases, this occurs upon the date of plan implementation, or the effective date.
 - Does the appointment of a Chapter 11 Trustee constitute a change in control? Change in management?
 - Is a “Structured Dismissal” a triggering event?
 - Run-Off Coverage
 - Coverage of claims against insured if noticed during policy period, but conduct need not occur during that period.
 - Benefits of Run-Off extensions
 - These issues should be addressed in advance of the restructuring

ADMINISTRATIVE DUTIES

- **Miscellaneous and Case Specific Tasks**
 - Audits: Tax, Insurance plans, etc...
 - Employee benefit plan terminations – 401(k) wind down
 - Data retention and destruction
 - TSA or other agency agreement reconciliations
- **“Day-to-Day” Administrative Duties**
 - Maintaining Claims Register
 - Disbursing Agent
 - Tax Returns and Beneficiary Notices
 - Maintaining bank accounts
 - Post confirmation quarterly reports required by office of the U.S. Trustee
 - Paying invoices, creating budgets, monitoring costs
 - Fielding creditor inquiries

MISCELLANEOUS ISSUE

There is a growing trend for Chapter 11 cases to have “fast turn arounds,” often this means that the Trust that may follow as the result of a confirmed plan has more to do, with less information.

- Pros/Cons?

QUESTIONS?

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