

## BE WARY OF BANKRUPTCY COURT ASSIGNMENTS



*Terry Bates*

In the last 20 years, bankruptcy filings have increase by about 16 percent. If you have a matter that turns on a contract that was assigned in the Bankruptcy Court, you should examine the assignment early in the litigation.

For plaintiffs, it may reveal problems in what you thought was a strong claim. For defendants, it may reveal the winning defense.

The Bankruptcy Code requires that a party in bankruptcy list all its debts, as well as its assets. This allows creditors to file claims in bankruptcy proceedings and secure a portion of all their debt, depending on priority.

For example, in a state court case in Alhambra, Plaintiff plead a single breach of contract claim based on a Power Purchase Contract for a cogeneration facility. Plaintiff claimed to be an assignee of rights under the agreement based on bankruptcy proceedings it which it was a creditor. But surprisingly, the Plaintiff had not perfected the assignment in the Bankruptcy Court.

We were retained by in-house counsel about two years after the litigation had commenced and it went to trial shortly thereafter. We moved for nonsuit after Plaintiff's opening statement, and we prevailed. The case boiled down to a single concept: whether the assignment from the Bankruptcy Court had been approved. Further, that concept depended on a single authority—*Neptune Society Corp. v. Longanecker* (1987) 194

Cal.App.3d 1233—as well as its predecessors and progeny. (Neptune Society lost its claim and the cross-defendant prevailed on its cross-complaint—receiving its attorneys' fees to boot.)

There are several considerations when assessing whether a plaintiff can assert rights based on a purported assignment that occurred in Bankruptcy Court. They include the following: (1) whether the bankruptcy trustee assigned the contract to the proper party; (2) whether the Bankruptcy Court itself should decide if there was a proper assignment; (3) whether there are contractual limitations on assignability; and (4) whether the assignor's knowledge or action raise statute of limitations issues.

So let us look at the issues, not necessarily in chronological order.

### **1. Whether the Bankruptcy Trustee Assigned the Contract to the Proper Party.**

The bankruptcy trustee is an administrator appointed by the court to oversee the debtor's estate in a bankruptcy proceeding. Whether the trustee assigned the contract to the proper party is critical. In our situation, the Trustee did not. Plaintiff argued it held the Power Purchase Agreement through an assignment in the Bankruptcy Court from an entity that had submitted Chapter 11 proceedings. But the Trustee neither assigned the contract specifically, nor recognized the assignment in the existing bankruptcy as it was not pled in the proceedings. Requesting that the opposing party produce the assignment does not take much effort. However, you need to see the assignment to evaluate it in the context of the Bankruptcy Court's rules to determine whether a purportedly assigned contract was actually assigned.

## **2. Whether the Bankruptcy Court, itself, should decide the contract was properly assigned.**

During Plaintiff's argument in our case, he claimed that the assignment was valid because the Bankruptcy Court itself completed the assignment, even if the Trustee did not. After evidence was heard before the trial court made its decision, Plaintiff noticed a hearing before the Bankruptcy Court so that it could decide whether an assignment took place before the state court entered its judgment. The California court then rendered judgment in our favor before the Bankruptcy Court hearing but stayed the matter until the Bankruptcy Court hearing took place. Fortunately for our side, the Bankruptcy Court ultimately agreed that the assignment had been improper.

You might not have a comparable situation, but it is important to consider whether to seek a hearing in the Bankruptcy Court, as that could clear up ambiguity and help you to evaluate your options. In our situation, the Bankruptcy Court held the hearing after the trial court made its decision. If you are going to seek the Bankruptcy Court's guidance, earlier is better.

## **3. Whether there are contractual imitations on assignability.**

The contract at issue might have language in it that restricts a party's ability to assign it. You should carefully review the contract to determine if there are any limitations on assignability, as that might influence how you craft your claims or defenses.

## **4. Whether the statute of limitations issues is presented by the assignor's knowledge or actions.**

Assessing the limitations period and whether suit was brought within that period is another important consideration. In our situation, the Plaintiff filed the action more than five years after the statute of limitations expired, making it time bared under the four-year statute of limitations for contract actions. Importantly, a former officer of the bankruptcy party admitted that he had spoken to senior management about a potential claim five years before the lawsuit was filed.

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