

## Business Bankruptcy Case Developments - 2020

November 5 - 6, 2020  
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## **I. ADMINISTRATIVE MATTERS**

### **A. Jurisdiction, Constitutional Authority and Powers of the Court**

#### **Fifth Circuit Holds that Injunctive Relief Directed at the SBA is “Absolutely Prohibited.”**

*Hidalgo Cty. Emergency Serv. Found. v. Carranza (In re Hidalgo Cty. Emergency Serv. Found.)*, 962 F.3d 838 (5th Cir. June 2020) (Smith, J.).

This case arose from a challenge to an SBA regulation that bars debtors in bankruptcy proceedings from obtaining loans under the SBA’s Paycheck Protection Program. Hidalgo County Emergency Center, which was in Chapter 11 bankruptcy, was denied a PPP loan. So, it filed an adversary proceeding in bankruptcy court, arguing “that the SBA’s decision to preclude bankrupt parties from obtaining PPP loans (1) violates 11 U.S.C. § 525(a), which prohibits discrimination based on bankruptcy status under certain circumstances, (2) is ‘arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law,’ and (3) is ‘in excess of statutory jurisdiction, authority, or limitations, or short of statutory right.’” (citations omitted).

The bankruptcy court agreed with Hidalgo and “issued a preliminary injunction mandating that the SBA handle Hidalgo’s PPP application without consideration of its ongoing bankruptcy.” The district court stayed the injunction, certified a direct appeal, and the Fifth Circuit took the case.

The Fifth Circuit vacated the injunction under the plain language of 15 U.S.C. § 634(b)(1), which provides that “no ... injunction ... shall be issued against the Administrator or his property.” The Court also noted that binding precedent held “that all injunctive relief directed at the SBA is *absolutely prohibited*.” Bound by the rule of orderliness, the Court rejected Hidalgo’s attempt to craft a narrow exception to that “absolute prohibition.” The Court concluded:

The issue at hand is not the validity or wisdom of the PPP regulations and related statutes, but the ability of a court to enjoin the Administrator, whether in regard to the PPP or any other circumstance. Because, under well-established Fifth Circuit law, the bankruptcy court exceeded its authority when it issued an injunction against the SBA Administrator, we VACATE its preliminary injunction.

#### **New York District Court Holds that Non-Debtor Injunctions are Not Core Proceedings.**

*Dunaway v. Purdue Pharm. L.P. (In re Purdue Pharm. L.P.)*, 619 B.R. 38 (S.D.N.Y. Aug. 11, 2020) (McMahon, J.)

The Southern District of New York recently upheld a preliminary injunction issued by a bankruptcy court preventing government officials and other parties from suing the non-debtor co-chairman of Purdue Pharmaceuticals LP. In doing so, the District Court found that while the bankruptcy court had “related to” jurisdiction to make such a finding, it lacked the “arising under” jurisdiction.

Prior to Purdue’s bankruptcy filing, a group of district attorneys sued the company and its former president and co-chairman for damages under a Tennessee state law, alleging their participation in an illegal drug market in the state. Three days after the debtor filed its chapter 11 petition, it filed an adversary proceeding seeking a preliminary injunction to halt that suit, as well as over 2,600 governmental enforcement and private lawsuits in both state and federal courts against the company’s non-debtor directors and officers. The bankruptcy court granted the injunction and later extended it further, and the district attorneys appealed, arguing that the bankruptcy court lacked jurisdiction to provide the preliminary injunctions.

The District Court agreed with the bankruptcy court’s granting of the preliminary injunction based on its finding of “related to” jurisdiction under 28 U.S.C. § 1334(b). The District Court reiterated that a bankruptcy court’s jurisdiction extends to any case in which “the action’s outcome might have any conceivable effect on the bankrupt estate,” before concluding that the interrelated nature of the claims against the debtor and its co-chairman and the potential for indemnification or contribution claims against the debtor were sufficient to confer “related to” jurisdiction to the bankruptcy court.

The District Court relied on a previous decision by the Second Circuit, which stood for the proposition that if one tortfeasor files for bankruptcy, an action against a co-tortfeasor for the same act would necessarily fall under the bankruptcy court's "related to" jurisdiction as a result of the potential for joint and several liability. *See SPV Osus Ltd. v. UBS AG*, 882 F.3d 333, 342 (2d Cir. 2018). The District Court noted that a judgment implicating the debtor's conduct "could conceivably effect" the rest of the debtor's estate because the individual case of the co-chairmen would likely "raise the issue of the corporate entity's liability, even if only indirectly." Additionally, the Court found that it was at least conceivable that an action against the co-chairman would eventually result in a contribution claim or indemnification claim by the co-chairman against the debtor. The Court upheld the preliminary injunction on the ground of the "related to" jurisdiction.

However, the Court did not end its discussion there, and ultimately ruled that the bankruptcy court erred in concluding that the state court action "arose in" the bankruptcy proceeding and was thus a core proceeding. The bankruptcy court had reasoned that the basis of the injunction was to allow sufficient time for negotiation of a settlement and plan, which would purportedly not exist outside of bankruptcy. The District Court disagreed, stating that the district attorney's claims against the co-chairman were completely independent from the bankruptcy as they were rooted in state law and filed half a year before the bankruptcy petition. The District Court accordingly ordered that the portions of the preliminary injunction that referred to "core proceedings" be vacated.

### **Court Held that Post-Petition Lawsuit Could Not Remain in Bankruptcy Court Because Removal was Untimely, and Circumstances Warranted Abstention.**

*Cedar Park Healthcare, LLC v. Harden Healthcare, LLC (In re Senior Care Ctrs., LLC)*, 611 B.R. 791 (Bankr. N.D. Tex. Dec. 2019) (Jernigan, J.).

The debtor entered into a commercial lease agreement with the plaintiff, the landlord, several years prepetition. The defendant, in turn, executed a lease guaranty in favor of the debtor. Two months after the debtor filed bankruptcy, the plaintiff filed a state court action seeking enforcement of the lease guaranty against the defendant. The defendant sought to remove the state court action to the bankruptcy court approximately six months later. The Court held that the removal was inappropriate and remanded it back to the state court for the following three reasons.

First, the Court held that the removal was untimely under Bankruptcy Rule 9027, which provides that a state court action filed after the commencement of the bankruptcy case may be removed either 30 days after receipt of service or 30 days after summons, whichever is shorter. It was undisputed that removal of the state court action was untimely. The defendant argued "excusable neglect" and requested the court to extend the timeline for removal pursuant to Bankruptcy Rule 9006. The Court looked at the *Pioneer* factors to determine whether the defendant satisfied "excusable neglect": (1) reason for the delay, including whether it was in control of the movant; (2) whether the movant acted in good faith; (3) the danger of prejudice to the debtor; and (4) the length of the delay and its potential impact on judicial proceedings. The Court held that the defendant did not satisfy those factors because: the delay was calculated and not outside of the defendant's control; the removal was not filed in good faith because the defendant aimed to delay the entry of a summary judgment ruling in favor of the plaintiff; the plaintiff would be prejudiced by the delay and the expense to relitigate the matter in bankruptcy court; and the defendant's actions were not careless because it waited until shortly before the summary judgment response deadline to file the removal.

Second, the Court held that mandatory abstention was required. The Court looked to the mandatory abstention elements established by the Fifth Circuit: (1) the claim has no independent basis for federal jurisdiction; (2) the claim is non-core; (3) an action has been commenced in state court; and (4) the action could be adjudicated timely in state court. The Court held that mandatory abstention was required because the removal action was a non-core breach of contract claim between two non-debtor parties that could be timely adjudicated in state court.

Third, having broad discretion to abstain from a hearing, the Court held that for similar reasons as stated above, it shall permissively abstain and remand the action to state court.

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First appeared as part of the conference materials for the  
39<sup>th</sup> Annual Jay L. Westbrook Bankruptcy Conference session  
"Recent Developments"