

NORTON BANKRUPTCY LAW ADVISER

Monthly Analysis of Important Issues and Recent Developments in Bankruptcy Law

Managing Editor: Hon. Keith M. Lundin, United States Bankruptcy Judge (1982-2016), Nashville, TN

Board of Contributing Editors: Hon. John T. Gregg, United States Bankruptcy Judge, Western District of Michigan; Scott B. Cohen, Engelman Berger, PC, Phoenix, Arizona; Andrew J. Currie, Venable LLP, Washington, D.C.; Eugene J. Geekie Jr., Saul Ewing Arnstein & Lehr LLP, Chicago, Illinois; Paul R. Hage, Jaffe Raitt Heuer & Weiss, Southfield, Michigan

Editor-in-Chief: William L. Norton III, Bradley Arant Boult Cummings LLP, Nashville, Tennessee

February 2021

Issue 2

***CITY OF CHICAGO v. FULTON*—A REJECTION OF THE MAJORITY RULE**

*By Kenneth N. Klee and Sasha M. Gurvitz**

In a decision authored by Justice Alito,¹ the Supreme Court holds in *City of Chicago v. Fulton* that a non-debtor's mere retention of property of the estate after the filing of a bankruptcy petition does not constitute an act to exercise control over property of the estate in violation of the Bankruptcy Code's automatic stay.² The decision resolves a circuit split between the Courts of Appeals for the Second, Seventh, Eighth, and Ninth Circuits, on the one hand, and the Third and Tenth Circuits, on the other hand.³ Those familiar with the Court's jurisprudence over the last decade will not be surprised that the predominantly textualist Supreme Court adopted the plain-meaning minority rule in *Fulton*, as the majority rule applied by the Seventh Circuit below has been criticized as "driven more by 'practi-

IN THIS ISSUE:

City of Chicago v. Fulton—A
Rejection of the Majority Rule 1
*By Kenneth N. Klee and Sasha M.
Gurvitz*

**Recent Decisions From The
Appellate Courts 6**

Erin Malone-Smolla
Bethany Davenport
Elizabeth Brusa
Shundra Manning
Hirshel Hall

*Kenneth N. Klee and Sasha M. Gurvitz are partners of KTBS Law LLP, a premier nationwide boutique law firm focusing on business and municipal bankruptcy and restructuring, corporate finance, and mergers and acquisitions. Professor Klee is a nationally recognized expert on bankruptcy law and was one of the principal drafters of the 1978 Bankruptcy Code. He became a Professor of Law Emeritus at the UCLA School of Law in 2014 and is a founding partner of KTBS Law LLP. Professor Klee is the author or co-author of six books and numerous law review articles on bankruptcy law. Professor Klee served as co-counsel for Bettina Whyte as COFINA agent in the Puerto Rico PROMESA restructuring cases and served as the appointed Examiner in the Tribune Chapter 11 cases. He also represented Jefferson County, Alabama, in its successful Chapter 9 case from 2011 to 2014. Professor Klee continues to serve clients as an expert witness, mediator, arbitrator, attorney, and consultant in his Chapter 11 business reorganization practice. Ms. Gurvitz also specializes in corporate reorganization and has represented clients in both out of court restructurings and in court proceedings in Delaware, New York, California, and Nevada. Ms. Gurvitz has represented Chapter 11 debtors, purchasers, contract counterparties, landlords, trustees, a governmental regulator, secured lenders, and other creditor constituencies in cases across industries, including in Chapter 11 cases such as Woodbridge Group of Companies (real estate), The Weinstein Company (entertainment), Pacific Sunwear (retail), and Garden Fresh (restaurant), as well as in recent out of court workouts in the healthcare and marijuana industries.

cal considerations’ and ‘policy considerations,’ than a faithful adherence to the text” of the Bankruptcy Code.⁴ Although *Fulton* is a Chapter 13 case, its holding and analysis should apply in business bankruptcy cases, giving additional bargaining leverage to secured creditors in possession of estate property on the petition date.

LEGAL BACKGROUND

Section 541(a)(1) of the Bankruptcy Code provides that the filing of a bankruptcy petition creates a bankruptcy estate, generally comprised of “all legal or equitable interests of the debtor in property as of the commencement of the case.”⁵ Under § 362(a)(3) of the Code, the filing of a bankruptcy petition also operates as an automatic stay, applicable to all entities, of acts to enforce or collect prepetition debts, including “any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate.”⁶ Finally, § 542(a) of the Code provides

that, with certain exceptions, a non-debtor entity, other than a custodian, that is in possession, custody, or control, during the case, of property of the bankruptcy estate shall turn over to the estate and account for such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.⁷

Prior to the Supreme Court’s decision in *Fulton*, these provisions were the subject of two conflicting strains of case law. The majority position, applied by the Second, Seventh, Eighth, and Ninth Circuits, held that a creditor exercised control over estate property, in violation of § 362(a)(3), by refusing to return estate property that was in the possession of the creditor as of the petition date.⁸ The minority position, applied by the Third and Tenth Circuits, held that under the plain meaning of the statutory text, § 362(a)(3) only prohibits affirmative acts to alter the status quo, and thus mere retention of estate property already in the creditor’s possession on the petition date does not violate the automatic stay.⁹

...

(continued)

Managing Editor:

Hon. Keith M. Lundin, United States Bankruptcy Judge (1982-2016), Nashville, Tennessee

©2021 Thomson Reuters. All rights reserved.

Norton Bankruptcy Law Adviser (USPS 013-530), is published Monthly, 12 times per year by Thomson Reuters, 610 Opperman Drive, P.O. Box 64526, St. Paul, MN 55164-0526. Periodicals Postage is paid at Twin Cities, MN.

POSTMASTER: send address correspondence to Norton Bankruptcy Law Adviser, 610 Opperman Drive, P.O. Box 64526, St. Paul, MN 55164-0526.

For authorization to photocopy, please contact the **Copyright Clearance Center** at 222 Rosewood Drive, Danvers, MA 01923, USA (978) 750-8400, <http://www.copyright.com> or **West’s Copyright Services** at 610 Opperman Drive, Eagan, MN 55123, copyright.west@thomsonreuters.com. Please outline the specific material involved, the number of copies you wish to distribute and the purpose or format of the use.

This publication was created to provide you with accurate and authoritative information concerning the subject matter covered; however, this publication was not necessarily prepared by persons licensed to practice law in a particular jurisdiction. The publisher is not engaged in rendering legal or other professional advice and this publication is not a substitute for the advice of an attorney. If you require legal or other expert advice, you should seek the services of a competent attorney or other professional.

This article appears in full in Norton Bankruptcy Law Adviser, February 2021 issue. To subscribe to the Adviser, visit :

<https://store.legal.thomsonreuters.com/law-products/Newsletter/Norton-Bankruptcy-Law-Adviser/p/100027749>

This article is also available on Westlaw:

Klee and Gurvitz, *City of Chicago v. Fulton* — A Rejection of the Majority Rule, 2021 WL 601864, 2021 No. 2 Norton Bankr. L. Adviser NL 1 (February 2021).

ENDNOTES:

¹Justice Barrett took no part in the consideration or decision of the case, because it was argued approximately two weeks before she was sworn in as Justice. Justice Sotomayor filed a concurring opinion.

²*City of Chicago v. Fulton*, 141 S. Ct. 585, 589 (2021).

³*Compare In re Fulton*, 926 F.3d 916 (7th Cir. 2019); *Weber v. SEFCU (In re Weber)*, 719 F.3d 72

(2d Cir. 2013); *Cal. Empl. Dev. Dep't v. Taxel (In re Del Mission, Ltd.)*, 98 F.3d 1147 (9th Cir. 1996); *Knaus v. Concordia Lumber Co. (In re Knaus)*, 889 F.2d 773 (8th Cir. 1989) (concluding retention of estate property after the filing of the petition violated the automatic stay), *with In re Denby-Peterson*, 941 F.3d 115 (3d Cir. 2019); *WD Equip., LLC v. Cowen (In re Cowen)*, 849 F.3d 943 (10th Cir. 2017) (concluding retention of estate property after the filing of the petition did not violate the automatic stay), *accord United States v. Inslaw, Inc.*, 932 F.2d 1467 (D.C. Cir. 1991).

⁴*In re Cowen*, 849 F.3d at 948-49 (internal citations omitted).

⁵11 U.S.C.A. § 541(a)(1).

⁶11 U.S.C.A. § 362(a)(3).

⁷11 U.S.C.A. § 542(a).

⁸*See, e.g., In re Fulton*, 926 F.3d at 925.

⁹*In re Denby-Peterson*, 941 F.3d at 124-26; *In re Cowen*, 849 F.3d at 949; *accord Inslaw, Inc.*, 932 F.2d at 1474.