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OBTAINING A SECURITY INTEREST IN A GOVERNMENT-ISSUED LICENSE

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In July of this year, a state court in California ruled that a court-appointed receiver for a business with a cannabis license could sell the assets of the business – including the license – and remit the proceeds to a creditor that had a security interest in the license.[1] Two weeks later, a federal court in Michigan ruled that a licensed cannabis testing facility had no property rights in its license so as to trigger Due Process protections.[2]

These rulings provide a useful backdrop for reviewing the law relating to whether a lender's security interest can attach to a government-issued license, and whether the lender ultimately can realize upon the value of the license. The issue arises not merely with respect to cannabis licenses, but also with respect to liquor licenses, gaming licenses, broadcast licenses, and many other government-issued licenses and permits.[3] Because the results vary, secured lenders relying on a license as collateral need to do careful due diligence.

BACKGROUND

Article 9 of the Uniform Commercial Code applies to security interests in personal property and fixtures. Consequently, for an asset to be collateral subject to an Article 9 security interest, the asset must be personal property[4] and the debtor must have rights in the property or the power to transfer rights in the property.[5] Nothing in Article 9 determines whether the debtor has a property interest; that issue is left to other law.[6]

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Article 9 does, however, contain several provisions that override a restriction on the transfer of property. One of these, § 9-408(c), provides that a rule of law, statute, or regulation that prohibits, restricts, or requires the consent of a government or governmental body or official to the creation of a security interest in a general intangible, including a license, is ineffective to the extent it would impair the creation of a security interest.[7] Of course, as a provision of state law, § 9-408 cannot override federal laws restricting the assignment of property rights.[8] So, to the extent that federal law prevents the creation of a security interest in a government license, § 9-408 is irrelevant.

Even with respect to state-issued licenses, there are two reasons why § 9-408(c) *might not* override a statute that would otherwise prevent a security interest from encumbering such a license.

First, while § 9-408(c) undoubtedly prevails over *a common-law rule*, whether it prevails over another state *statute* is uncertain.[9] This is illustrated by two cases analyzing whether a similar provision, § 9-406(f), overrides a statutory restriction on the assignment of lottery winnings. In 2010, the Texas Court of Appeals ruled that § 9-406(f) takes precedence over a Texas statute prohibiting assignment of state lottery winnings, even though the lottery statute was more recent and more specific, because § 9-406(f) makes clear that it controls over other law.[10] A few weeks later, a California Court of Appeal ruled that a California statute that restricts the assignment of lottery winnings trumped § 9-406(f) because the specific rules in the Lottery Act controlled over the more general rules in Article 9, even though Article 9 was enacted more recently.[11] Thus, when § 9-406(f) or § 9-408(c) conflicts with another state statute, it is often impossible to know for sure which will control.

That said, the official text of § 9-408(e) provides a potential mechanism to determine whether § 9-408 prevails over another statute. It states that "[t]his section prevails over any inconsistent provisions of the following statutes, rules, and regulations" and then invites states to list the statutes over which § 9-408 is to control. Only one state – Kentucky – has listed a licensing statute in its version of § 9-408.[12] Almost half the states did something different. Nine enacted a nonuniform version of § 9-408(e) stating that the section prevails over any inconsistent statute (with some noting exceptions).[13] Thirteen others and one territory enacted nonuniform language stating that the section prevails over any inconsistent statute unless that other statute expressly refers to the state's enacted version of § 9-408 and states that the other statute prevails.[14] Presumably, all of these nonuniform versions of § 9-408 would indeed

override a licensing statute of that state that purports to prohibit or require the issuer's consent to the creation of a security interest in a license.[15]

The second reason why § 9-408 might not override a restriction on the assignment of a government-issued license is that § 9-408(c) does not purport to convert non-property into property, a point the official comments confirm.[16] Instead, Section 9-408(c) applies to a rule of law, statute, or regulation relating to a general intangible. The term "general intangible" is defined to be a type of "personal property."[17] Consequently, for § 9-408(c) to apply to an asset, that asset must, in the first instance, be personal property.

Traditionally, many government-issued licenses were declared by statute to be privileges, not property, of the licensee.[18] This was likely intended to facilitate the ability of the issuer to suspend or terminate a license, possibly without triggering Due Process protections. The United States Supreme Court long ago frustrated this objective when it ruled that the Due Process clause applies to the suspension of a driver's license regardless of whether the license was characterized as a property right or a privilege.[19] Nevertheless, it remains unclear whether a statute declaring a particular type of government license not to be property was intended to prevent a security interest from attaching to the license, and similarly unclear whether § 9-408(c) is relevant to the issue.[20] What is clear is that if a government-issued license is not property of the licensee, a security interest cannot attach to the licensee's interest in the license.

Given this background, it is not surprising that the law regarding security interests in government-issued licenses is not uniform. The remainder of this article explores the treatment of specific types of licenses.

LIQUOR LICENSES

Most states do not limit to the number of liquor licenses that the state or its subdivisions may issue in a geographic area. In such states, a liquor license has little or no value because another license can readily be obtained for a nominal fee. However, seventeen states limit the number of liquor licenses that may be issued for a geographic area, thereby creating value and a secondary market for liquor licenses. In such a state, a lender extending credit to an operator of a restaurant, bar, night club, or similar establishment might want a security interest in all of the debtor's property so as to be able to sell the business as a going concern in the event of a default.[21]

The following chart categorizes how those seventeen states treat a security interest in a liquor license. If a statute purports to prohibit the transfer or encumbrance of a license or require issuer approval for any such transfer or encumbrance, it is possible that § 9-408(c) would override that statute. If a statute declared the license not to be property, it is less likely that § 9-408(c) would be relevant but a court might conclude that the declaration was not intended to prevent a security interest from attaching. In any state that allows a security interest to be created in a liquor license, it is likely that the approval of the issuer would be needed for any transfer of the license pursuant to an Article 9 disposition.

	States Limiting the Number of Liquor Licenses			
	Security Interest Permitted	**Security Interest Not Permitted**	**License Declared Not to be Property**	**Statute Purports to Prohibit or Restrict Assignment of a License**
Alaska	√[22]			
Arizona	√[23]			
California		√[24]		
Florida	√[25]			
Idaho			√[26]	
Kentucky				√[27]
Massachusetts	√ (with issuer's approval)[28]			
Michigan	√[29]			
Minnesota		√[30]		
Montana	apparently[31]			
New Jersey		√[32]		
New Mexico	√[33]			

	States Limiting the Number of Liquor Licenses			
	Security Interest Permitted	Security Interest Not Permitted	License Declared Not to be Property	Statute Purports to Prohibit or Restrict Assignment of a License
Ohio		√[34]		
Pennsylvania	√[35]			
South Dakota	√[36]			
Utah	possibly[37]			
Washington			√[38]	

Even among the states that do not limit the number of liquor licenses that may be issued, whether a security interest may attach to such a license varies. The following chart illustrates this variation with respect to the states for which information is available.

	States with an Unlimited Number of Liquor Licenses			
	Security Interest Permitted	Security Interest Not Permitted	License Declared Not to be Property	Statute Purports to Prohibit or Restrict Assignment of License
Alabama			√[39]	
Colorado				√[40]
Connecticut			√[41]	
Georgia			√[42]	
Illinois			√[43]	
Indiana		√[44]		
Iowa			√[45]	
Kansas		√[46]		
Mississippi		apparently[47]		
Missouri				√[48]
Nebraska		√[49]		
New York		apparently[50]		
North Carolina				√[51]
Oklahoma			√[52]	
Rhode Island	√[53]			
South Carolina			√[54]	
Tennessee				√[55]
Texas			√[56]	
Virginia				√[57]
West Virginia	√[58]			
Wisconsin	apparently[59]			
Wyoming	√[60]			

The New York statute on liquor licenses has some particularly troubling language. It provides that "[n]o license shall be pledged or deposited as collateral security for any loan or upon any other condition; and any such pledge or deposit, and any contract providing therefor, shall be void." Notice, the last phrase does not state that "a term in a contract" providing for a pledge or deposit of the license is void, it states that "the contract" is void.[61] Thus, the language purports to invalidate an entire agreement that attempts to encumber a New York liquor license. The statute therefore would seem to invalidate an entire security agreement if a New York liquor license was included in the described collateral.[62] It is difficult to believe that statute is intended to have that effect. Moreover, § 9-408(c) should override the provision.[63] Nevertheless, given the limited value of New York liquor licenses and the potentially catastrophic consequences of invalidating an entire security agreement, it might be prudent for those drafting security agreements to: (i) exclude New York liquor licenses from the grant of the security interest; (ii) include a savings clause that provides that the grant does not apply to a New York liquor license if the law prevents the attachment of a security interest in such property and Article 9 does not override that rule; (iii) have one security agreement for all other collateral and a separate security agreement for New York liquor licenses; or (iv) structure the transaction so that all liquor licenses are held in one or more special purpose entities, the equity in which is pledged to the lender.

GAMING LICENSES

A few courts have dealt with issues relating to a security interest in gaming equipment or gaming revenue[64] but very few cases have addressed whether it is possible to obtain a security interest in a gaming license. This is not surprising. The states that have legalized gaming tend to exercise significant control over who can obtain a gaming license so as to help ensure that organized crime does not infiltrate the gaming industry. The states are therefore highly unlikely to permit anyone other than the licensee to acquire any rights associated with a license.

This certainly appears to be the rule in New Jersey and Pennsylvania, which have statutes declaring a gaming license not to be property.[65] Statutes in Colorado, Delaware, Louisiana, New Mexico, and West Virginia provide similarly.[66] Massachusetts, in contrast, appears to treat a gaming license as property and requires the issuer's consent to a transfer of the license (unless § 9-408 overrides that rule).[67]

But even without a statute expressly declaring a gaming license not to be property, that result seems likely. For example, Nevada requires approval of the State Gaming Control Board to enforce a security interest in the equity of a licensee.[68] Although Nevada has no statute expressly addressing a security interest in a gaming license, that silence is telling. It would make no sense to extensively regulate the equity of a licensee while permitting the license itself to be transferrable. Presumably, therefore, a Nevada gaming license is not property and cannot be collateral.

CANNABIS LICENSES

Twenty-three states, along with the District of Columbia and three U.S. Territories have legalized the recreational use of cannabis.[69] Sixteen additional states and territories have legalized cannabis for medical purposes.[70] Almost all of these jurisdictions have legalized commercial distribution of cannabis but require a license to cultivate or distribute it.

There is little case law on whether a creditor can obtain a security interest in a cannabis license. Other than the cases mentioned at the beginning of this article, the only other known case is a 2021 decision in which the court ruled that the seller of a membership interest in a limited liability company, who represented and warranted that the buyers were acquiring the membership interest free of all liens, violated that provision because the LLC had a license to sell cannabis, state law provides that the members of such an LLC are the true parties in interest in such a license, and the state had a lien on the license to secure unpaid taxes.[71]

Even if it is possible to acquire a security interest in a cannabis license, lenders need to be cautious. Courts almost uniformly agree that an entity that derives a substantial portion of its income from cultivating or selling cannabis pursuant to a state license cannot be a debtor in a bankruptcy proceeding because the income-producing assets could not be administered without involving the court, the trustee, and the debtors in an ongoing violation of federal criminal law.[72] Courts have even barred from bankruptcy relief debtors that acquire a substantial portion of their income from cannabis indirectly, such as by contracting with a licensee.[73] It therefore seems likely that even if a security interest could attach to a cannabis license under state law, no federal court would enforce that security interest. Accordingly, a lender to a cannabis licensee should include in the loan or security agreement a clause either selecting state courts as the exclusive forum for all litigation or providing for arbitration (with a back-up selection of state courts as the exclusive forum, just in case the parties waive arbitration or it is necessary to get a judicial order compelling arbitration).

FCC BROADCAST LICENSES

Federal law prohibits the holder of a broadcast license from assigning the license without the FCC's prior consent,[74] and the FCC has long interpreted this rule as prohibiting the creation of a security interest in an FCC license. Courts have upheld this interpretation.[75] However, the FCC has indicated that a creditor may take a security interest in the proceeds of a broadcast license.[76] Relying on this ruling, some lenders have taken a security interest in the future proceeds of the borrower's FCC licenses, rather than in the licenses themselves.

One potential problem with this approach is that § 552 of the Bankruptcy Code prevents a security interest from attaching to collateral acquired post-petition unless the post-petition property is proceeds of pre-petition collateral. Consequently, because the license itself is not and cannot be collateral, any receivable generated by a post-petition contract to sell cannot be proceeds of pre-petition collateral. It is at best after-acquired property, to which no pre-petition security interest can attach.[77]

Nevertheless, a few courts have ruled that a security interest can, if properly drafted, attach pre-petition to the "economic value" of a license and that any post-petition sale of the license will then generate proceeds of that economic value, which the security interest will encumber.[78] This might seem a bit like judicial slight-of-hand but it seems analogous to how some states treat a member's interest in a limited liability company, distinguishing among a member's economic rights, control rights, and membership status and presumptively permitting members to assign their economic rights while presumptively prohibiting members from assigning their control rights or membership status.[79] Thus, even though a secured party cannot in most cases obtain a security interest in all of a member's rights or in the member's status as a member, a secured party can generally obtain a security interest in economic rights.

CONCLUSIONS

A transactional lawyer representing a secured lender that is relying on a security interest in a government-issued license should carefully review the law relating to the type of license involved. If a statute declares the license not to be property of the licensee, it is doubtful that a security interest can attach to the license. If a statute lacks such a statement but indicates that the license is not assignable or prohibits assignment without the issuer's consent, it is possible that § 9-408 will override that restriction and permit the security interest to attach, but that conclusion is uncertain. Even if § 9-408 does override that restriction, the issuer's consent would likely be needed to any disposition of the license.[80]

To deal with such situations, the lawyer should consider suggesting structural devices – such as a pledge of the equity in the licensee – to help ensure that the economic value of the license is at least indirect collateral for the secured lender.

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Notes:

1. Cutter Mill Credit LA LLC v. Aeon Botanika Los Angeles, Inc., Case No. 22SMCV01841 (Super. Ct. L.A. Cty. July 17, 2023).

2. Viridis Labs., LLC v. Klutyman, 2023 WL 4861698 (W.D. Mich. 2023). *Cf.* Brinkman v. Washington State Liquor and Cannabis Board, 2023 WL 1798173, at *11 (W.D. Wash. 2023) (because "citizens do not have a legal interest in participating in a federally illegal market," states could not run afoul of the dormant Commerce Clause by preferring their own residents in the granting of cannabis licenses).

3. Such other licenses and permits include taxicab medallions, fishing licenses, and slotting rights at airports. With respect to the last of these, the Fifth Circuit held that exclusive access to airport gates was not property of the airline to which the gates had been assigned. In re Braniff Airways, Inc., 700 F.2d 935 (5th Cir. 1983). Three years later, the FAA amended its regulations to allow airlines to sell such rights. As a result, courts have held that such rights are now property. In re Gull Air, Inc., 890 F.2d 1255, 1260 (1st Cir. 1989); In re McClain Airlines, Inc., 80 B.R. 175, 178 (Bankr. D. Ariz.1987).

4. *See* § 1-201(b)(35) (defining "security interest" to mean "an interest in *personal property* or fixtures") (emphasis added).

5. § 9-203(b)(2) & cmt. 6.

6. *See* § 9-408 cmt. 3.

7. *See also* §§ 9-406(d)-(f), 9-407(a) 9-408(a), 9-409(a) (each overriding other restrictions on assignment that would otherwise impair the creation of a security interest).

8. *See* § 9-408 cmt. 9. *See also* § 9-109(c)(1).

9. The uniform text of § 9-408(e) does state that the section prevails over specified other statutes, and then invites states to enumerate those statutes. But if a statute restricting the creation of a security interest in a government-issued license is not among those listed, then § 9-408 does not specify which rule controls and a negative implication that the other law controls might be drawn.

10. Texas Lottery Comm'n v. First State Bank of DeQueen, 254 S.W.3d 677 (Tex. Ct. App. 2008), *aff'd*, 325 S.W.3d 628 (Tex. 2010). *See also* Fenway Fin., LLC v. Greater Columbus Realty, LLC, 995 N.E.2d 1225 (Ohio Ct. App. 2013) (§ 9-406 did not override Ohio statute that prohibits a brokerage from paying real estate commission to a creditor of a broker).

11. Stone Street Capital, LLC v. California State Lottery Comm'n, 80 Cal. Rptr. 3d 326 (Cal. Ct. App. 2008). *See also* Clark v. Missouri Lottery Comm'n, 463 S.W.3d 843 (Mo. Ct. App. 2015) (a bank obtained a security interest in a lottery winner's right to future distributions despite a state statute prohibiting the assignment of lottery proceeds because, in the

view of the court, § 9-406 provides otherwise, expressly purports to prevail in the event of conflict with other law, and thus overrides that other state statute).

12. *See* Ky. Stat. § 355.9-408(5) (this section prevails over § 243.620(2)).

13. *See, e.g.*, Fla. Stat. § 679.4081(5); Ind. Stat. § 26-1.9.1-408(e); Kan. Stat. § 84-9-408(e); Md. Code, Com. Law § 9-408(e)(1); Mo. Stat. § 400.9-408(e); Mont. Stat. § 30-9A-408(6); Neb. Rev. Stat. UCC § 9-408; N.D. Stat. § 41-09-70(5); R.I. Stat. § 6A-9-408(e).

14. *See, e.g.*, Ala. Stat. § 7-9A-408(e); Alaska Stat. § 45.29.408(e); Ariz. Stat. § 4-9-408(e), (f); Conn. Stat. § 42a-9-408(e), (f); Del. Stat. tit. 6, § 9-408(e), (f); Iowa Stat. § 554.9408(5); Mass. Gen. Laws ch. 106, § 9-408(e); Miss. Stat. § 75-9-408(e); N.J. Stat. § 12A:9-408(e), (f); N.C. Stat. § 25-9-408(e), (f); Or. Rev. Stat. § 79.0408(5), (6); 13 Pa. Cons. Stat. § 9408(e); Tenn. Code § 47-9-408(e); V.I. Code tit. 11A, § 9-408(e).

15. At least one state did not enact any version of § 9-408(e), leaving it even more unclear what law controls when another state statute conflicts with § 9-408. *See* N.Y. U.C.C. § 9-408.

16. *See* § 9-408 cmt. 3 ("Neither this section nor any other provision of this Article determines whether a debtor has a property interest.").

17. *See* § 9-102(a)(42).

18. *See, e.g.* N.H. Rev. Stat. 270:63(I) ("A mooring permit shall not be construed as ownership of any real or personal property and shall not be transferred to any other person or location").

19. *See* Bell. v. Burson, 402 U.S. 535 (1971).

20. *Compare* In re Amereco Envtl. Servs., Inc., 129 B.R. 197 (Bankr. W.D. Mo. 1991) (because a statute declared a hazardous waste operating permit was not property of the licensee, no security interest could attach to the license), *with* First Pennsylvania Bank v. Wildwood Clam Co., 535 F. Supp. 266 (E.D. Pa. 1982) (lender's security interest in general intangibles attached to the debtor's clamming license and the proceeds thereof because there was no statute prohibiting the creation of a security interest in such a license).

21. States issue different licenses for producers, distributors, and retailers of alcoholic beverages. Even if such a license is property to which a security interest can attach, and the license can be transferred in connection with the enforcement of the security interest, the transferee's permission under the license would be limited in the same manner as the debtor's was. For example, if the debtor was a licensed distributor, a transferee of the license would be permitted to sell alcoholic beverages only to other distributors or back to the manufacturers.

22. *See* Rendezvous Club, Inc. v. Padgett, 1984 WL 908392 (Alaska 1984) (no dispute that a liquor license was subject to a security interest); Queen of the North, Inc. v. Legrue, 582 P.2d 144 (Alaska 1978) (liquor license was subject to a security interest); Gibson v. Alaska Alcoholic Beverage Control Bd., 377 F. Supp. 151, 153 (D. Alaska 1974) (an Alaska liquor license can be collateral Article 9). *But cf.* C.Y., Inc. v. Brown, 574 P.2d 1274 (Alaska 1978) (because Alaska Stat. § 4.10.330 requires that all of a licensee's debts be paid before the Alcoholic Beverage Control Board may approve a transfer of the license, a creditor with a security interest in a liquor license could not foreclose on the license if debts to unsecured creditors remained; § 4.10.330 has since been repealed).

23. *See* Ariz. Stat. § 4-203(C) ("A spirituous liquor license may be transferred to a person qualified to be a licensee, if the transfer is pursuant to either judicial decree, nonjudicial foreclosure of a legal or equitable lien, including security interests held by financial institutions pursuant to § 4-205.05 . . . ."). *See also* Landon v. Baird, 709 P.2d 565 (Ariz. Ct. App. 1985) (filing a financing statement is necessary to perfect a security interest in an Arizona liquor license).

24. *See* Concorde Equity II, LLC v. Bretz, 2011 WL 5056295 (Cal. Ct. App. 2011) (but security interest did attach to proceeds of the license sold by court-appointed receiver); Bischoff v. LCG Blue, Inc., 2009 WL 148519 (Cal. Ct. App. 2009).

25. *See* Fla. Stat. § 561.65(4) (filing with the Division of Alcoholic Beverages and Tobacco within 90 days of the creation of the security interest is necessary to perfect). *See also* United States v. McGurn, 596 So. 2d 1038 (filing with Division of Alcoholic Beverages and Tobacco is necessary and sufficient to perfect a security interest in a liquor license; a UCC filing is not needed).

26. *See* Id. Stat. § 23-514 (a liquor license "shall be a personal privilege, subject to be denied, revoked, or canceled for its abuse. It shall not constitute property; nor shall it be subject to attachment and execution; nor shall it be alienable or assignable.").

27. *Compare* Ky. Stat. §§ 243.630(2), (4) ("Any license issued to any person for any licensed premises shall not be transferable or assignable," and "[a]ny acquisition of interest in a license without prior authorization shall be void."), 243.660 ("No person shall pledge or grant a security interest in any license. This type of pledge or security interest and any contract providing for the pledge or security interest shall be void.") *with* Ladt v. Arnold, 583 S.W.2d 702 (Ky. Ct. App. 1979) ("It has long been the rule in this jurisdiction that a liquor license is but a temporary permit not involving a property right as between the issuing authority and the licensee, but Kentucky Courts, without condemning the practice, have recognized that such licenses are bought and sold."). *But see* Ky. Stat. § 355.9-408(5) (this section prevails over § 243.620(2)).

28. *See* Mass. Gen. Laws ch. 138, § 23 ("Any license granted under the provisions of this chapter may be pledged by the licensee for a loan, provided approval of such loan and pledge is given by the local licensing authority and the commission."); In re Jojo's 10 Rest., LLC, 455 B.R. 321 (Bankr. D. Mass. 2011).

29. *See* Brown v. Yousif, 517 N.W.2d 727 (Mich. 1994) (but the Liquor Control Commission might have to approve an assignee in connection with a disposition); In re Three Lakes Cocktail Lounge & Restaurant, Inc., 131 B.R. 70 (Bankr. W.D. Mich. 1991); In re Matto's, Inc., 9 B.R. 89 (Bankr. E.D. Mich. 1981).

30. *See* Ropas, Inc. v. City of New Hope, 1991 WL 4048, at *2 (Minn. Ct. App. 1991) ("no person has a vested property right to engage in or continue to engage on the liquor business"; concurring opinion suggests that the appellant, by retaining a security interest in the debtor's liquor licenses, did have a protectable property right).

31. *See* Montana Bank of Livingston v. Old Saloon, Inc., 766 P.2d 878 (Mont. 1988) (surety not discharged by creditor's relinquishment of security interest in liquor license for $6,000).

32. *See* In re Circle 10 Rest., LLC, 519 B.R. 95 (Bankr. D.N.J. 2014); In re S & A Rest. Corp., 2010 WL 3619779 (Bankr. E.D. Tex. 2010) (applying N.J. law).

33. *See* N.M. Stat. § 60 6A 19(A) (a licensee has no vested property right in a liquor license but the license "shall be considered property subject to . . . a secured transaction"); State ex rel. Clinton Realty Co. v. Scarborough, 429 P.2d 330 (N.M. 1967).

34. *See* Banc of Am. Strategic Solutions, Inc. v. Cooker Rest. Corp., 2006 WL 2535734 (Ohio Ct. App. 2006), *appeal denied*, 861 N.E.2d 144 (Ohio 2007); Paramount Fin. Co. v. United States, 379 F.2d 543 (6th Cir. 1967).

35. *See* In re Ciprian Ltd., 473 B.R. 669 (Bankr. W.D. Pa. 2012).

36. *See* Rushmore State Bank v. Kurylas, Inc., 424 N.W.2d 649 (S.D. 1988); In re O'Neill's Shannon Village, 750 F.2d 679 (8th Cir. 1984).

37. *See* Celebrity Club Inc. v. Utah Liquor Control Comm'n, 657 P.2d 1293 (Utah 1982) (a licensee had sufficient property rights in a license to raise a claim that revocation of the license without notice or an evidentiary hearing might have violated the licensee's due process rights).

38. *See* Arndt v. Manville, 333 P.2d 667, 669 (Wash. 1958) ("A liquor license is not property, but a personal privilege"). *But cf.* Scottsdale Ins. Co. v. International Protective Agency, Inc., 19 P.3d 1058, 1061 (Wash. Ct. App. 2001) (a liquor license is intangible property for tax purposes).

39. *See* Ott v. Everett, 420 So. 2d 258, 261 (Ala. 1982) (quoting an earlier ruling that stated, in connection with a dispute about denial of a liquor license, that "[a] license to engage in the sale of intoxicants is merely a privilege with no element of property right or vested interest of any kind").

40. *See* Colo. Stat. § 44-3-303(1)(a) ("No license granted under the provisions of this article 3 or article 4 of this title 44 shall be transferable except as provided in this subsection (1)").

41. *See* Conn. Stat. § 30-14(a) ("Each permit shall be a purely personal privilege . . . . No permit shall constitute property, be subject to attachment and execution or be alienable").

42. *See* Ga. Stat. § 3-3-1 ("The businesses of manufacturing, distributing, selling, handling, and otherwise dealing in or possession alcoholic beverages are declared to be privileges in this state and not rights").

43. *See* Ill St. ch. 255 5/6-1 ("A license shall be purely a personal privilege . . . and shall not constitute property . . . nor shall it be alienable or transferable, voluntarily or involuntarily, or subject to being encumbered or hypothecated."

44. *See* Ind. Code § 7.1-3-1-2 ("A permittee shall have no property right in a . . . permit of any type."); Cole v. Loman & Gray, Inc., 713 N.E.2d 901, 905 n.3 (Ind. Ct. App. 1999); Vanek v. Indiana State Bank, 540 N.E.2d 81, 84 (Ind. Ct. App. 1989); In re Eagles Nest, Inc., 57 B.R. 337 (Bankr. N.D. Ind. 1986). *But cf.* In re Barnes, 276 F.3d 927 (7th Cir. 2002) (an Indiana liquor license is subject to an involuntary lien).

45. *See* Michael v. Town of Logan, 73 N.W.2d 714, 716 (Iowa 1955) ("A license or permit . . . to sell beer in Iowa is a privilege granted by the state and in no sense is a property right" and thus may be revoked without a hearing).

46. *See* Kan. Stat. § 41-326; In re Disc Heat, LLC, 2013 WL 6080183 (Bankr. D. Kan. 2013).

47. *See* Miss. Stat. § 67-7-67 ("No permit shall be transferred by the permittee to any other person . . . except with the written consent of the commission").

48. *See* Mo. Stat. § 311.250 ("No license issued under this chapter shall be transferrable or assignable except as herein provided."). *But see* Mo. Stat. § 400.9-408(e) ("This section prevails over any inconsistent provisions of any statutes, rules, and regulations.").

49. *See* Neb. Stat. § 53-149 ("[a] license shall be purely a personal privilege . . . shall not constitute property . . . nor shall it be alienable or transferable, voluntarily or involuntarily, or subject to being encumbered or hypothecated."); In re Midland Services, Inc., 10 U.C.C. Rep. Serv. 499 (Bankr. D. Neb. 1971).

50. *See* N.Y. Alco. Bev. Cont. Law § 114 ("No license shall be pledged or deposited as collateral security for any loan or upon any other condition; and any such pledge or deposit, and any

contract providing therefor, shall be void."); Oxford Distrib. Co. v. Famous Robert's Inc., 173 N.Y.S.2d 468 (Sup. Ct. App. Div. 1958) (indicating that a liquor license is not property but that a lien can attach to the refund that arises at the time the license is surrendered); City of New York v. Bedford Bar & Grill, Inc., 141 N.E.2d 575 (N.Y. 1957) (similar).

51. *See* N.C. Stat. § 18B-903(e) ("An ABC permit may not be transferred from one person to another"). *But see* N.C. Stat. § 25-9-408(e) ("this section prevails over any inconsistent provision of an existing or future statute, rule, or regulation of this State unless the provision is contained in a statute of this State, refers expressly to this section, and states that the provision prevails over this section")

52. *See* Okla. Stat. tit. 37a, § 2-153 ("Any license issued pursuant to the provisions of the Oklahoma Alcoholic Beverage Control Act shall be a purely personal privilege. It shall not constitute property . . . or be alienable or transferable, either voluntarily or involuntarily").

53. *See* In re Camelot Court, Inc., 21 B.R. 596 (Bankr. D.R.I. 1982).

54. *See* S.C. Stat. § 61-6-4280 ("Licenses and permits are the property of the department [and] are not transferable").

55. *See* Tenn. Code § 57-3-212(a) ("The holder of a license may not sell, assign or transfer such license to any other person"). *But see* Tenn. Code § 47-9-408(e) ("This section prevails over any inconsistent provisions of an existing or future statute, rule or regulation of this state unless the provision is contained in a statute of this state, refers expressly to this section and states that the provision prevails over this section.").

56. *See* Tex. Alco. Bev. Code § 61.02(a) ("A license issued under this code is a purely personal privilege and is subject to revocation as provided in this code. It is not property, is not subject to execution, does not pass by descent or distribution, and ceases on the death of the holder."); § 11.03 (stating the same with respect to permits).

57. *See* Va. Stat. § 4-1-216(B)(3)(c) (a wholesale licensee may grant a security interest in any of its assets other than the wholesale license itself).

58. *See* Lowndes Bank v. MLM Corp., 395 S.E.2d 762, 766 (W. Va. 1990) (citing approvingly dicta in Hudson Cty. Bd. of Chosen Freeholders v. Morales, 581 F.2d 379, 384 (3d Cir. 1978), stating that a liquor license is personal property).

59. *See* Wis. Stat. § 125.04(14)(b)(1) ("Licenses to sell alcohol beverages may be transferred to persons other than the licensee if the licensee . . . dies, becomes bankrupt or makes an assignment for the benefit of creditors during the license year").

60. *See* Bogus v. America Nat'l Bank of Cheyenne, 401 F.2d 458 (10th Cir. 1968).

61. N.Y. Alco. Bev. Cont. Law § 114.62

62. Nothing in the New York statute states that the offending language must expressly refer to a liquor license. Because language purporting to encumber "all general intangibles" would normally include any liquor licenses owned by the debtor, the statute seemingly invalidates a security agreement that purports to encumber all general intangibles if the debtor owns a New York Liquor license.

Similarly, nothing in the New York statute limits its scope to security agreements. Accordingly, the statute would seem to invalidate an entire purchase and sale agreement for a business with a New York liquor license if one of the terms of the agreement purported to grant the seller a security interest in the license to secure the unpaid portion of the purchase price.

63. New York did not enact § 9-408(e), and therefore its version of the UCC provides no guidance on which statute controls when another statute conflicts with § 9-408(c). *See supra* note 15.

64. *See, e.g.*, Potts v. Maryland Games, Inc., 2019 WL 4750339 (D. Md. 2019) (a buyer that purchased gaming equipment subject to a perfected security interest was liable in conversion to the secured party for the value of the collateral as of the date of the purchase but was not also liable for the revenues that the buyer generated after that date by using the collateral); Potts v. Maryland Games, LLC, 2019 WL 1543233 (D. Md. 2019) (a secured party with a perfected security interest in the debtor's video lottery gaming machines was entitled to a preliminary injunction requiring the buyer of the machines to deposit with the buyer's counsel all monies generated by the machines; there was no discussion of whether such funds are proceeds of the machines but the security agreement did encumber "fees, payments, revenues, income . . . [and] all contracts and contract rights."); Outsource Servs. Mgmt. LLC v. Nooksack Bus. Corp., 2017 WL 1315490 (Wash. Ct. App. 2017) (a corporation that operated a casino on tribal land could and did grant a security interest in revenue of the facility to a lender that financed construction of and improvements to the facility without approval of the Secretary of the Interior).

65. *See* N.J. Stat. § 5:12-1 (" participation in casino operations as a licensee or registrant under this act shall be deemed a revocable privilege . . . . Consistent with this policy, it is the intent of this act to preclude the creation of any property right in any license . . . or the transfer of any license"); 4 Pa. Cons. Stat. § 1327 (a gaming license does not create "an entitlement" and no licensee may sell, transfer, assign, or grant a security interest in a license). *See also* In re Philadelphia Entm't and Dev. Partners LP, 860 F. App'x 25 (3d Cir. 2021) (because the debtor's slot machine license was not property under Pennsylvania law, the debtor's fraudulent transfer action against a state agency for its prepetition revocation of the license did not fall under the bankruptcy court's in rem jurisdiction and was

barred by sovereign immunity). *But cf.* Wilmington Trust Co. v. Tropicana Entm't, LLC, 2008 WL 555914 (Del. Ch. Ct. 2008) (the loss of New Jersey gaming license by subsidiary and appointment under state law of conservator to manage casino assets was a prohibited "transfer or other disposition" of assets under the indenture agreement, and thus qualified as an event of default even though loss or non-renewal of the gaming license was not expressly listed as an event of default.

66. *See* Colo. Stat. § 44-30-503 ("No licensee acquires any vested interest or property right in a license."); Del. Stat. tit. 29, § 4830(e) ("it is the intent of this chapter to preclude the creation of any property right in any license permitted by this chapter"); La. Rev. Stat. tit. 27, § 2 ("Any [casino operating license or contract] issued pursuant to the provisions of this Title . . . is expressly declared by the legislature to be a pure and absolute revocable privilege and not a right, property or otherwise"); § 42 ("Any [riverboat gaming license] issued pursuant to the provisions of this Chapter is expressly declared by the legislature to be a pure and absolute revocable privilege and not a right, property or otherwise"); N.M. Stat. § 60-2E-2(B) ("the holder of any license issued by the state in connection with the regulation of gaming activities has a revocable privilege only and has no property right or vested interest in the license."); W. Va. Stat. § 29-25-9(j) ("A license to operate a gaming facility is not transferable or assignable and cannot be sold or pledged as collateral."). *See also* El Chico Restaurants of La., Inc. v. Louisiana Gaming Control Bd., 837 So. 2d 641, 645-46 (La. Ct. App. 2002) (The plain language of the Louisiana Gaming Control Law provides that video gaming licenses are personal and non-transferable, and therefore when a licensee merged into another, surviving entity, the license was not transferred to the survivor).

67. *See* Mass. Gen. Laws, ch. 23, § 21(b).

68. *See* Nev. Rev. Stat. § 463.344(1); Admin. Code §§ 8A.020(1), 8A.030(a). Indeed, a creditor of a licensee can be required to obtain its own gaming license merely to acquire such a security interest in the equity of a licensee. *See* Nev. Rev. Stat. § 463.165 (indicating that a lender to or creditor of a licensee might be required to apply for a license if, in the opinion of the Commission, the lender or creditor has the power to exercise a significant influence over the licensee's operation of a gaming establishment).

69. The jurisdictions are Alaska, Arizona, California, Colorado, Connecticut, Delaware, District of Columbia, Guam, Illinois, Maine, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Montana, Nevada, New Jersey, New Mexico, New York, Northern Mariana Islands, Oregon, Rhode Island, U.S. Virgin Islands, Vermont, Virginia, and Washington.

70. The jurisdictions are Alabama, Arkansas, Florida, Hawaii, Kentucky, Louisiana, Mississippi, New Hampshire, North Dakota, Ohio, Oklahoma, Pennsylvania, Puerto Rico, South Dakota, Utah and West Virginia.

71. Percival-Birchard v. Caldwell, 2021 WL 235997 (Wash. Ct. App. 2021). *See also* Brinkman v. Washington State Liquor and Cannabis Bd., 2023 WL 1798173 (W.D. Wash. 2023) (because "citizens do not have a legal interest in participating in a federally illegal market," states could not run afoul of the dormant Commerce Clause by preferring their own residents in the granting of cannabis licenses).

72. *See* In re Great Lakes Cultivation, LLC, 2022 WL 3569586 (E.D. Mich. 2022) (dismissing Chapter 7 case); In re Way To Grow, Inc., 597 B.R. 111 (D. Colo. 2018); In re Arenas, 535 B.R. 845 (10th Cir. BAP 2015) (dismissing a Chapter 7 case and refusing to convert the case to Chapter 13); In re Medpoint Mgmt., LLC, 528 B.R. 178 (Bankr. D. Ariz. 2015) (dismissing an involuntary Chapter 7 petition); In re Rent-Rite Super Kegs W. Ltd., 484 B.R. 799 (Bankr. D. Colo. 2012) (dismissing the Chapter 11 case of a landlord that received approximately 25% of its revenue from leasing warehouse space to entities engaged in the business of growing cannabis).

73. *See, e.g.*, In re Mayer, 2022 WL 18715955 (Bankr. D. Ariz. 2022) (dismissing a Chapter 13 case filed by the individual who owned a business that sold equipment used to extract oil from organic materials; most of its equipment was sold to businesses engaged in cannabis-related industries and therefore most of its income was traceable to violations of the Controlled Substances Act); In re Burton, 610 B.R. 633 (9th Cir. BAP 2020 (upholding dismissal of Chapter 13 case due to the debtors' ownership of entity involved in litigation seeking to recover damages for breach of contracts related to growing and selling cannabis); *Cf.* In re Johnson, 532 B.R. 53 (Bankr. W.D. Mich. 2015) (enjoining a Chapter 13 debtor from conducting his medical marijuana business and violating the Controlled Substances Act rather than dismissing the case).

74. *See* 47 U.S.C. § 310(d).

75. *See, e.g.*, In re Tak Commc'ns, Inc., 985 F.2d 916 (7th Cir. 1993); Stephen Indus., Inc. v. McLung, 789 F.2d 386, 390-91 (6th Cir. 1986).

The Federal Communications Act provides that "[n]o . . . license, or any rights thereunder, shall be transferred, assigned, or disposed of in any manner, voluntarily or involuntarily, directly or indirectly, . . . except upon application to the Commission and upon finding by the Commission that the public interest, convenience, and necessity will be served thereby." 47 U.S.C. § 301(d). While this language might mean that no security interest can attach to a license without the FCC's consent, it could be read more narrowly: to allow a security interest to attach but leave the secured party without a right to transfer the license after a default without the FCC's approval. After all, attachment of the security interest does not,

by itself, affect the operations of the licensee or the content of any broadcast.

76. In re Cheskey, 9 FCC Rcd. 986, 987 (1994). The FCC has made one narrow exception to its prohibition of security interests in FCC licenses. To facilitate increased access to capital for commercial and private wireless, licensees in rural areas may a grant security interest in their FCC licenses to the U.S. Department of Agriculture's Rural Utilities Services). *See* Facilitating the Provision of Spectrum-Based Services to Rural Areas and Promoting Opportunities for Rural Telephone Companies to Provide Spectrum-Based Services, 69 Fed. Reg. 75,144, 75,152 (Dec. 15, 2004).

77. To deal with this, lenders often required the borrower to create a separate subsidiary to hold each FCC license and included the borrower's equity in the subsidiaries in the collateral for the loan. The licensed subsidiaries guaranteed the debt and granted a security interest in all their assets but this structure made the subsidiaries bankruptcy-remote entities (by making it unlikely they would have their own creditors) and ensured that the value of the licenses would, at least indirectly, secure the debt even if no security interest could attach to the licenses.

78. *See* In re Tracy Broad. Corp., 696 F.3d 1051 (10th Cir. 2012); In re TerreStar Networks, Inc., 457 B.R. 254 (Bankr. S.D.N.Y. 2011).

79. The Delaware Limited Liability Company Act, for example, establishes two default rules relating to assignment, which include the granting of a security interest: (i) members may assign their economic rights; and (ii) members cannot assign their control rights or membership status. Del. Code, tit. 8, § 18-702(a), (b). An operating agreement can alter either of these rules.

80. *See* § 9-408(d)(4).

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PEB Report on Choice-of-Law Issues under the 2022 UCC Amendments

On September 22, California become the eleventh state to enact the 2022 UCC Amendments. By the second week of October the amendments will be effective in seven of those states.

Enactment of 2022 UCC Amendments		
State	**Date Enacted**	**Effective Date**
Alabama	6/14/23	7/1/24
California	9/22/23	1/1/24
Colorado	5/1/23	8/6/23
Delaware	8/18/23	8/18/23
Hawaii	6/29/23	6/29/23
Indiana	5/4/23	7/1/23
Nevada	6/15/23	10/1/23
New Hampshire	8/8/23	10/7/23
New Mexico	4/5/23	1/1/24
North Dakota	3/21/23	8/1/23
Washington	5/4/23	1/1/24

Other states are expected to enact the amendments over the next few years. Until the Amendments are enacted and effective in all states, complex choice-of-law issues are likely to arise, particularly for controllable electronic records ("CERs").

For example, if litigation concerning the rights of a secured party or purchaser of a CER occurs in a jurisdiction that has enacted the Amendments, that jurisdiction will look to the law of the CER's jurisdiction, which might or might not have enacted the Amendments. If, however, the forum state has not enacted the Amendments, the forum state would treat the CER as a general intangible and look to the law of the debtor's location (which might or might not have enacted the Amendments) to deal with such matters as perfection and the effect of perfection or nonperfection. The various possibilities are almost Byzantine.

The Permanent Editorial Board for the UCC is in the process of preparing a report on these choice-of-law issues. Transactional lawyers should be on the lookout for this report, which is expected later this year. It will be available on the PEB's web site.

Recent Cases

SECURED TRANSACTIONS

Priority Issues

First Financial Bank v. Fox Capital Group, Inc., 2023 WL 5979212 (S.D. Ohio 2023)

A bank with a perfected security interest in the debtor's accounts and deposit accounts stated a claim for conversion against a factor that purchased the debtor's accounts and received payment of almost $600,000 from the debtor's deposit account because the bank alleged that the factor knew of the bank's interest from the bank's filed financing statements, deliberately concealed the factoring agreements from the bank and purposefully failed to file any financing statements, and had discussions with the debtors to ensure that debtors would not inform the bank of the factoring agreements. These allegations were sufficient to claim that the factor acted in collusion with the debtor to violate the bank's rights so as to prevent the factor from taking free under § 9-332(b). The bank also stated claims that the payments were actual and constructive fraudulent transfers.

West v. West, 2023 WL 6154406 (Miss. 2023)

For a corporation's bylaws to create a lien on a stockholder's shares to secure the stockholder's debts to the corporation and for that lien to have priority over the lien of another creditor, the corporation's lien must be noted on the stock certificate and the other creditor must have either actual or constructive notice of the lien. Because it was unclear what language was on the stock certificates and what notice the stockholder's former spouse had, the issue of whether the corporation's lien had priority over the ex-spouse's equitable lien had to be remanded to the trial court.

Shinsho American Corp. v. HyQuality Alloys Co., 2023 WL 6213572 (S.D. Tex. 2023)

A bank's security interest in a debtor's existing and after-acquired inventory had priority over the rights of a supplier that entered into a consignment agreement with the debtor. That agreement did not purport to cover all future transactions between the parties and the goods that the supplier later sent to the debtor were covered by invoices that provided for title to pass on delivery, and thus were sold, not consigned. The parties' later activities – including marking the goods as belonging to the supplier, segregating the goods, not reflecting the goods as inventory on the debtor's books, and not paying property taxes on the goods – did not retroactively change the transaction to a consignment. The court did not address the bank's alternative argument that, even if the goods had been consigned, the bank would still have had priority because the supplier never perfected its interest. However, the bank had no claim against the supplier for conversion as a result of its acceptance of payment from the debtor with funds that were proceeds of inventory. The bank authorized the debtor to sell inventory and use the proceeds in the debtor's business, and the supplier therefore took free under § 9-315(a)(1).

Liability Issues

Aegis Business Credit, LLC v. Brigade Holdings, Inc., 2023 WL 5352407 (D. Md. 2023)

A debtor stated a claim against the secured party for repossessing goods consigned to the debtor. Even though the debtor did not own the goods, the debtor had the right to possess the goods and, therefore, had a sufficient interest to support a conversion claim. The debtor also stated a claim for breach of contract both for repossession of the consigned inventory and for allegedly instructing account debtors to pay amounts that the account debtors did not owe or amounts owed by a different account debtor. The debtor also stated a claim for tortious interference with advantageous business relationships arising from the same conduct.

CDM Holding Group, LLC v. NewTek Small Bus. Fin., LLC, 2023 WL 5167360 (C.D. Cal. 2023)

A senior secured party stated claims against a junior secured party for fraudulently filing a UCC-3 form, civil conspiracy, and declaratory relief – but not for intentional interference with contract – based on the junior secured party's actions in filing a termination statement purporting to terminate the senior secured party's financing statement. Although the junior secured party had the debtor's authorization, the junior secured party did not have the senior secured party's authorization and had not issued an authenticated demand requesting termination. The termination statement plausibly impaired the value of the senior secured party's security interest by creating a cloud over its priority.

T-Zone Health Inc. v. SouthStar Capital LLC, 2023 WL 5021952 (D.S.C. 2023)

Summary judgment could not be issued for either party on a supplier's claims for breach of contract, promissory estoppel, and unjust enrichment against a secured party that had allegedly, prior to delivery of goods to the debtor, confirmed that it would pay six invoices sent by the supplier. Although the secured party had paid other invoices sent by the supplier, both before and after the six at issue, there was a factual dispute about whether there was a contract between the supplier and the secured party. The claim for promissory estoppel could not be resolved until the claim for breach was resolved. With respect to the claim for unjust enrichment, the evidence was disputed as to whether the secured party had received payment from the buyer's customer for the goods to which the six invoices related.

Cleveland-Cliffs Burns Harbor LLC v. Boomerang Tube, LLC, 2023 WL 5688392 (Del. Ch. Ct. 2023)
An unsecured creditor of the debtor had no claim against the entity that owned a majority of the debtor and orchestrated a disposition of substantially all the debtor's assets to a buyer that was related to the majority owner. There was no basis for piercing the corporate veil because there was no allegation that the debtor was inadequately capitalized or that corporate formalities had not been observed, and the debtor and the majority owner had different businesses. The unsecured creditor did state a claim that the disposition was avoidable as a constructively fraudulent transfer by alleging that the debtor was insolvent and that the buyer purchased $100 million in assets for only $16.5 million. The unsecured creditor also stated a claim that the disposition was an intentionally fraudulent transfer by alleging that: (i) the transfer was made to an insider for less than fair value while the debtor was insolvent; (ii) the transfer was concealed and bids for the sale were accepted over a period from Christmas Eve to January 3, a suspiciously fast turnaround during the winter holidays; and (iii) the transfer was of substantially all of the debtor's assets. However, the potential avoidability of the transfer did not give the unsecured creditor a claim against the majority owner. The unsecured creditor also stated a claim against the buyer under the mere continuation theory of successor liability by alleging that the debtor and the buyer were owned and controlled by the same entities, the debtor effectively ceased to exist after the disposition, and after the disposition the buyer operated the same business, employed the same facilities, employees, and equipment, had a similar website, sold to the same customers, and had many of the same managers as the debtor. The unsecured creditor had no standing to challenge the commercial reasonableness of the disposition under Article 9.

In re TransCare Corp., 2023 WL 5523719 (2d Cir. 2023)
The woman who controlled and owned most of equity in the debtor, and who also controlled the collateral agent for the term loan to the debtor, violated her fiduciary duties as the controlling shareholder by orchestrating an acceptance of collateral in partial satisfaction of the term loan and then selling the foreclosed assets to newly formed entities she owned and controlled. The purpose of the fair dealing standard is to protect minority shareholders but the woman misled the largest minority shareholder throughout the process. Even if, as the woman claimed, she intended to give the other term loan lenders a proportionate interest in the new entities, that would have little bearing on the procedural fairness of the transaction, because the bargaining process was still devoid of any opportunity for the independent shareholders to advocate for themselves. The foreclosure was also avoidable as an actually fraudulent transfer because it had many of the classic badges of fraud: the woman failed to demonstrate that the price was objectively fair; she effectively sold the collateral to herself; she maintained control of the collateral at all times; she retained the most valuable parts of the business, free and clear of any liens; she executed all of the transfers after the onset of financial difficulties; she conducted the entire transaction hastily; and she kept key stakeholders in the dark.

BANKRUPTCY

Automatic Stay & Injunctions

In re Rogers, 2023 WL 5354417 (Bankr. E.D. Wis. 2023)
A secured creditor that had repossessed the debtor's vehicle prepetition did not violate the stay by refusing to return the vehicle post-petition until the debtor provided proof of insurance. Pursuant to the Supreme Court's decision in *City of Chicago v. Fulton*, retention of collateral is not an act to exercise control over property of the estate under § 362(a)(3). The creditor also did not violate § 362(a)(4) because retention of possession was not an act to enforce its lien, nor did it violate § 362(a)(6) because it made no demand for payment, merely for proof of insurance. The debtor was not entitled to damages under § 542(a) because that provision is not self-executing; turnover is required only with a court order. Even if that were not the case, § 542 does not provide a private right of action.

Discharge, Dischargeability & Dismissal

In re Daddosio, 2023 WL 5355265 (Bankr. N.D. Ill. 2023)
The debtor's obligation to a secured creditor of the business that the debtor owned was nondischargeable under § 523(a)(4) and (a)(6) because, by selling the collateral and using the proceeds to pay personal expenses and the expenses of a new business, rather than to pay the secured obligation, the debtor committed embezzlement and conversion.

Avoidance Powers

In re Sanchez Energy Corp., 2023 WL 4986394 (S.D. Tex. 2023)
The prepetition recording of correction notices for defective deeds of trust created an avoidable preference for the senior lenders whose liens were thereby perfected. Perfecting the liens would have allowed the creditors to receive more in a hypothetical Chapter 7 liquidation than they would have received if the notices not been recorded. It did not matter that, during the bankruptcy case, the senior lenders were primed by the DIP lenders (who were, in fact, also the senior lenders) and did not receive payment on account of their secured claims; the senior lenders effectively released their liens to themselves but they did benefit in connection with the DIP financing.

Moreover, without the correction notices, the debtor might have been able to obtain superior DIP financing, and thus there was injury to the estate.

In re Pacific Links U.S. Holdings, Inc.,
2023 WL 4586476 (9th Cir. BAP 2023)
A restructuring through which the debtors assumed liability for an existing $57 million debt owed by affiliates and granted security interests in their assets to secure the debt was an avoidable transaction because the debtors were insolvent and did not receive reasonably equivalent value in return. The creditor had no good faith defense for any value it might have provided because it knew or should have known that the debtors were in financial distress at the time of the restructuring and that the obligations they assumed and the transfers they made would make their financial difficulties substantially worse.

GUARANTIES & RELATED MATTERS

Pita, LLC v. Segal,
2023 WL 5843577 (W. Va. Ct. App. 2023)
The entity, owned by a guarantor, which purchased the guaranteed note had no claim for contribution against one of three original co-guarantors because the entity had not paid the note. However, the entity did have a claim against the co-guarantor on the guaranty, which claim was limited to the owner's contributive share, and that claim included contractual interest and attorney's fees that the original creditor would have been entitled to under the guaranty. Any defense based on frustration of purpose or discharge of the principal was waived in the guaranty. Among themselves, co-guarantors are generally liable equally unless they have agreed otherwise. Although the owner's guaranty was for three times the amount of the co-guarantor, that difference affected the guarantors' liability to the creditor and was not sufficient to indicate an agreement to a different allocation among the guarantors, particularly since the owner's guaranty was provided later, was not requested by the original guarantors, was not part of a joint agreement to define their contributive shares among themselves, and was something the original guarantors were not even aware of until sometime after the fact.

Armstrong v. White Winston Select Asset Funds, LLC,
2023 WL 6140186 (D. Mass. 2023)
An individual who guaranteed a loan to a pharmacy that the individual owned and who transferred all of the pharmacy's assets to the lender after default was relieved of liability pursuant to a "good guy" clause in the guaranty triggered if the guarantor "fully cooperates with the Lender in turning over to the Lender all of the Guarantor's right, title and interest in the outstanding ownership interest in the Borrower and the Target, and in causing the Borrower to turn over all of its assets." It did not matter that the lender had not accelerated the debt or sought to foreclose. By not seeking to exercise its default remedies despite the pharmacy's deteriorating finances and by ignoring the guarantor's repeated requests for direction, the lender breached the covenant of good faith and fair dealing by destroying the benefit of the good guy clause.

LENDING, CONTRACTING & COMMERCIAL LITIGATION

Magee v. Bunting,
2023 WL 4613793 (Del. Ch. Ct. 2023)
A term in a written lease of farmland prohibiting the tenant from erecting improvements without the landlord's consent and providing that all improvements "shall become" the property of the landlord at the end of the lease term did not cover an irrigation system that the tenant had installed before executing the written lease, while renting the property under an oral lease with the prior owner.

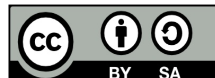
In re Furniture Factory Ultimate Holding, L.P.,
2023 WL 5662747 (Bankr. D. Del. 2023)
The trustee of a liquidation trust stated a claim for breach of fiduciary duty against the debtor's officer and directors in connection with transactions as to which the officer and directors allegedly failed to conduct due diligence and were allegedly not disinterested due to their ties to the parties on each side of the transactions. The trustee also stated a claim for recharacterizing as equity approximately $14 million in debt represented by Grid Notes and another $14 million arising under a Credit Agreement. Some of the *Autostyle* factors supporting treatment of the Grid Notes as debts were that: (i) the documents expressly evidenced a debt; and (ii) the obligations were not subordinated to all other creditors. Neutral factors included that there was a stated maturity date but no required schedule of payments. Among the factors supporting recharacterization were that: (i) the debts were unsecured and therefore repayment was contingent on the success of the business; (ii) the debtor was undercapitalized; (iii) the Grid Notes were indirectly held by the equity owners in proportion to their equity; and (iv) no other creditor was willing to provide credit on similar terms. With respect to Credit Agreement, factors supporting treatment as debt included that: (i) the documents expressly evidenced a debt; (ii) the debt was not held by equity holders in proportion to their ownership; and (iii) the debt was not subordinated. Neutral factors included a stated maturity date but no required schedule of payments. Factors supporting recharacterization included that: (i) although the debts were secured, no financing statement was filed for 16 months; (ii) the debtor was undercapitalized; (iii) no other creditor was willing to lend on similar terms; and (iv) the advances were made before the loan was documented.

Frontline Technologies Parent, LLC v. Murphy,
2023 WL 5424802 (Del. Ch. Ct. 2023)
A holding company's Equity Grant Agreements with two former employees of its operating subsidiary that included clauses barring the employees from working for a competitor of the holding company did not restrict the employees from working for a competitor of the operating subsidiary. If the holding company wanted the noncompete clauses to apply to the subsidiary's business, it could have defined the prohibited "competition" to include a business or business line that the holding company "or its affiliates" conducts.

Cummings Properties, LLC v. Hines,
2023 WL 6202474 (Mass. 2023)
A commercial lease that provided for the tenant to be liable for the present value of all future rent if the tenant breached was an enforceable liquidated damages clause even though the clause did not account for the possibility that the landlord could – and did – relet the premises and collect rent from a new tenant. The reasonableness of a liquidated damages clause is determined at the time of contracting only.

Holifield v. XRI Investment Holdings LLC,
2023 WL 5761367 (Del. 2023)
A transfer of a membership interest in a limited liability company was incurably void, and therefore could not be ratified by the company's failure to object, because the company's operating agreement prohibited specified transfers of a membership interest and stated that any attempted transfer in violation of that prohibition "shall be void, and none of the Company or any of its respective Subsidiaries shall record such purported Transfer on its books or treat any purported Transferee as the owner of such Units." It was not necessary for the agreement to state that the transfer was "void ab initio" for the transfer to be incurably void.

Navigator Business Services LLC v. Aiguang Chen,
2023 WL 5956335
The forum-selection clauses in the security agreements that two guarantors executed did not apply to an action against the guarantors on their guaranties, which lacked such a clause.



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