

## Legal Updates

### New Ruling Reinforces Limits on Automatic Stay Waivers

April 8, 2025

A recent decision by Bankruptcy Judge Laura Grandy in *In re DJK Enterprises LLC*, 24-60126 (Bankr. S.D. Ill. Feb. 13, 2025) further limits the enforceability of prepetition waivers of the automatic stay, reinforcing the trend that courts will scrutinize such waivers under bankruptcy law principles and public policy considerations. The enforcement of a prepetition waiver of the automatic stay is not automatic and requires approval from the bankruptcy court.<sup>[1]</sup> Even if deemed valid, the waiver alone does not allow the secured creditor to enforce its lien without first obtaining relief from the stay through the court.<sup>[2]</sup> This decision builds upon prior case law and highlights for lenders the risk they face when relying on pre-bankruptcy agreements to bypass the automatic stay.

#### **Background and Key Events in *In re DJK Enterprises LLC***

DJK Enterprises LLC (“DJK”) is the owner and operator of a hotel and restaurant encumbered by a \$10.5 million mortgage, with Effingham Asset Funding (the “Lender”) holding liens and mortgages on all of DJK’s real and personal property.<sup>[3]</sup> In addition to the liens granted in favor of the Lender, DJK is indebted to (a) the Small Business Administration (SBA) in the amount of approximately \$500,000, which loan is secured with a lien against DJK’s personal property,<sup>[4]</sup> (b) Effingham County for property taxes in the amount of \$243,494 secured by DJK’s real property<sup>[5]</sup> and (c) Royal Banks of Missouri (“Royal Banks”) in the amount of \$13,486,879.80 secured by a lien on all DJK’s assets.<sup>[6]</sup> Although DJK did not repay the Lender in full upon maturity, it continued making payments.<sup>[7]</sup>

Prior to the bankruptcy, DJK and the Lender executed the forbearance agreement, granting DJK 75 days to pay off the mortgage.<sup>[8]</sup> As part of the forbearance agreement, DJK executed a deed in lieu of foreclosure, which was to be held in escrow.<sup>[9]</sup> If DJK failed to repay the mortgage before the termination of the forbearance period, the Lender had the right to record the deed.<sup>[10]</sup> Additionally, the agreement prohibited DJK from filing for bankruptcy before the termination of the forbearance period or within 91 days after the deed’s recording.<sup>[11]</sup> In the

event DJK did file for bankruptcy and the property was deemed part of the estate, the forbearance agreement included a waiver by DJK of the protections of the automatic stay and further required DJK to consent to a modification of the automatic stay.[12]

Before the termination of the forbearance period, DJK filed for Chapter 11 bankruptcy.[13] In response, the Lender moved to enforce the forbearance agreement and sought relief from the automatic stay, arguing that DJK's prepetition waiver should be upheld.[14]

## **Summary of the Court's Decision in *In re DJK Enterprises LLC***

### **1. Waivers of the Automatic Stay Remain Unreliable**

Judge Grandy ruled that the provisions of the forbearance agreement containing a waiver of the automatic stay were per se unenforceable, emphasizing that this approach "best protects the rights and interests of the debtor-in-possession and *all* creditors under the Bankruptcy Code—not just those of the creditor asserting the waiver." [15]

### **2. Public Policy Continues to Favor the Bankruptcy Process**

While some courts have enforced stay waivers in bad-faith filings or single-asset real estate cases,[16] Judge Grandy recognized that the "trending position" among courts is to "treat the waiver as just one of several factors to be considered in determining whether 'cause' exists to lift the automatic stay." [17] She rejected the Lender's attempt to enforce the waiver solely for its own benefit, ruling that courts must consider the broader bankruptcy framework, public policy and interests of all creditors.[18]

### **3. No Cause to Lift the Stay**

The court emphasized that lifting the stay must be based on statutory grounds, such as the debtor lacking equity in the property and the property not being necessary for an effective reorganization (§ 362(d)(2)), or for "cause," including the creditor lacking adequate protection (§ 362(d)(1)).[19] In this case, the Lender failed to demonstrate that DJK's financial condition, asset values or restructuring prospects warranted stay relief.[20] Ultimately, the court found no other independent grounds to modify the automatic stay and denied the Lender's motion.[21]

## **How This Decision Builds on Prior Precedent**

Courts generally approach prepetition waivers of the automatic stay in three ways: Uphold the stay waiver in broad terms, reject the stay waiver as against public policy, and, the more modern approach which is to make a determination on a case-by-case basis.[22] The *In re DJK Enterprises* ruling adds further weight to the anti-waiver position, suggesting that lenders should not expect automatic enforcement of such provisions, and that the automatic stay is an indispensable feature of bankruptcy law.

Some courts have upheld waivers under certain conditions, particularly when they are part of a court-approved agreement, such as a prior bankruptcy plan or stipulated order.[23] Enforcing waivers may also be justified when it aligns with public policy by promoting out-of-court settlements and loan workouts.[24] Additionally, courts are more likely to uphold a waiver if the debtor's bankruptcy filing appears to be in bad faith, suggesting an attempt to abuse the bankruptcy process.[25]

Several courts, including the Illinois Bankruptcy Court in *In re DJK Enterprises*, reject prepetition waivers, arguing that they conflict with the public policy behind the automatic stay, which is designed to protect debtors and ensure equitable treatment of creditors.[26] They also contend that such waivers violate the debtor's fiduciary duty to creditors once a bankruptcy is filed, as the debtor-in-possession must act in the best interests of all creditors, not just select lenders.[27] Additionally, courts have expressed concern that enforcing these waivers could encourage predatory lending practices by allowing creditors to bypass bankruptcy protections and gain an unfair advantage over other creditors.[28]

The final approach taken by courts, as is the modern trend acknowledged in *In re DJK Enterprises*,[29] neither automatically enforce nor reject waivers but instead weigh them alongside other factors in stay relief motions.[30] Common factors include, but are not limited to:

- the sophistication of the debtor;
- the consideration received;
- the effect on other creditors;
- the feasibility of reorganization;
- evidence of fraud, coercion or mutual mistake;
- furthering public policy; and
- whether there was compelling change in circumstances between the date of the waiver and the date of the bankruptcy filing.[31]

In *In re DJK Enterprises*, the court ruled that prepetition waivers of the automatic stay are per se unenforceable, aligning with the reasoning in *Pease*, 195 B.R. 43, and *In re Jeff Benfield Nursery, Inc.*, 565 B.R. 603 (Bankr. W.D.N.C. 2017).[32] In *Pease*, the court held that such waivers are unenforceable, citing three bases for invalidating the waiver: (1) the debtors did not have the capacity to act on behalf of the debtor-in-possession; (2) the waiver would limit the effectiveness of certain bankruptcy provisions such as §§ 363, 365 and 541; and (3) the Bankruptcy Code extinguishes the private right to freedom to contract around its essential provisions.[33] In *Jeff Benfield Nursery*, the court declined to enforce a prepetition waiver as matter of public policy, explaining that upholding these waivers deprives debtors of the "breathing spell" of the automatic stay intended by the bankruptcy code.[34]

The *In re DJK Enterprises* court emphasized that a prepetition debtor and a post-petition debtor-in-possession are distinct entities, and a debtor cannot waive rights that arise only after filing for bankruptcy.[35] Additionally, the court noted that enforcing the waiver would harm other creditors who were not parties to the agreement.[36] For example, in this case, DJK's largest creditor, Royal Banks, had agreed to settle its \$13 million claim for \$300,000—a settlement that significantly benefited not only DJK, but other creditors. Enforcing the waiver in favor of the primary Lender, EAF, would effectively end the case, leaving Royal Banks and other creditors with nothing.[37] The court reiterated that the automatic stay exists to protect both debtors and creditors, and enforcing the waiver would unfairly benefit only EAF at the expense of all other stakeholders.[38]

The ruling in *In re DJK Enterprises LLC* further solidifies the trend in bankruptcy law toward rejecting or at least limiting the enforceability of prepetition waivers of the automatic stay. It also refines the case-by-case analysis, emphasizing that waivers will not be enforced if they primarily benefit a single creditor while harming the debtor-in-possession and broader creditor pool. Overall, *In re DJK Enterprises LLC* weakens the enforceability of prepetition waivers, adding to the judicial skepticism toward automatic stay waivers and making it even more difficult for lenders to rely on them as a mechanism for bypassing the bankruptcy process.

## Implications for Lenders and Borrowers

- Lenders should not rely on prepetition waivers of the automatic stay as a guaranteed method to expedite foreclosure or debt recovery in bankruptcy. While waivers generally cannot hurt or disadvantage the lender, courts will continue to scrutinize such provisions and may refuse to enforce them altogether. To improve enforceability, waivers should be clearly drafted with explicit consideration provided, include factual stipulations about the debtor's financial status, and avoid overreach that courts may find unconscionable.
- Forbearance agreements and deeds in lieu of foreclosure should be structured carefully, taking into account applicable state law and equitable mortgage doctrines, which could preserve a debtor's rights despite contractual language.
- Lenders should seek alternative protections, such as court-approved stipulations or structuring agreements to demonstrate independent grounds for a court to grant relief from the stay.

If you have any questions about how this ruling may affect your lending practices or bankruptcy litigation strategies, please contact our office for further guidance.

[1] *In re Lopez-Granadino*, No. 08-30707-H3-13, 2008 Bankr. LEXIS 686, \*5 (Bankr. S.D. Tex. Mar. 12, 2008).

[2] *Id.*

[3] *Id.* at 2.

[4] *Id.* at 5.

[5] *Id.* at 13.

[6] *Id.*

[7] *Id.*

[8] *Id.* at 3.

[9] *Id.* at 3–4.

[10] *Id.*

[11] *Id.* at 4. While prohibitions on filing for bankruptcy are beyond the scope of this alert, such provisions are generally unenforceable for public policy reasons. *See e.g., In re Shields*, 524 B.R. 769 (Bankr. E.D. Tenn. 2015); *In re Bay Club Partners-472, LLC*, No. 14-30394-rld11, 2014 Bankr. LEXIS 2051 (Bankr. D. Or. May 6, 2014); *In re Melbourne Beach, LLC*, No. 6:17-bk-07975-KSJ, 2019 Bankr. LEXIS 4113 (Bankr. M.D. Fla. Aug. 6, 2019).

[12] *Id.* at 4–5.

[13] *Id.* at 5.

[14] *Id.*

[15] *Id.* at 12.

[16] *Id.* at 8.

[17] *Id.* at 9.

[18] *Id.* at 13.

[19] *Id.* at 14, 29.

[20] *Id.* at 19.

[21] *Id.* at 28–29.

[22] Prepetition Waivers of the Automatic Stay: Lender Satisfaction Not Guaranteed: By Gregory G. Hesse and Jesse T. Moore. 2013.

[23] *In re Philadelphia Athletic Club, Inc.*, 17 B.R. 345 (Bankr. E.D. Pa. 1982); *In re Cheeks*, 167 B.R. 817 (Bankr. D.S.C. 1994); *In re Excelsior Henderson Motorcycle Mfg. Co.*, 273 B.R. 920 (Bankr. S.D. Fla. 2002).

[24] *Id.*

[25] *Id.*

[26] *In re Pease*, U.S. Bankr. Ct, District of Connecticut Case No. 93-53692, Adv. Pro. No. 94-2126 (Bankr. E.D. Tenn. Mar. 21, 1996); *Farm Credit of Central Florida, ACA v. Polk*, 160 B.R. 870 (M.D. Fla. 1993); *In re DB Capital Holdings, LLC*, Civil Action No. 10-cv-03031-PAB (D. Colo. Jul. 28, 2011); *In re DJK Enterprises LLC*, 24-60126 at 12 (Bankr. S.D. Ill. Feb. 13, 2025).

[27] *Id.*

[28] *Id.*

[29] *Id.* at 10.

[30] Hesse & Moore, *Prepetition Waivers*, 2013; *In re Powers*, 170 B.R. 480 (Bankr. D. Mass. 1994); *In re Desai*, 282 B.R. 527 (Bankr. M.D. Ga. 2002); *In re Frye*, Case No. 05-10004 (Bankr. D. Vt. May. 27, 2005); *In re Bryan Road, LLC*, 389 B.R. 297 (Bankr. S.D. Fla. 2008).

[31] *Id.*

[32] *In re DJK Enterprises LLC*, 24-60126 at 11-12 (Bankr. S.D. Ill. Feb. 13, 2025).

[33] *Pease*, 195 B.R. at 433-434.

[34] *Jeff Benfield Nursery, Inc.*, 565 B.R. at 608-609.

[35] *In re DJK Enterprises LLC*, 24-60126 at 12-13 (Bankr. S.D. Ill. Feb. 13, 2025).

[36] *Id.*

[37] *Id.*

[38] *Id.*

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