PRACTICAL ISSUES IN ASSIGNMENTS FOR THE BENEFIT OF CREDITORS

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INTRODUCTION

This article focuses on issues which often arise during the course of an assignment for the benefit of creditors ("ABC" or "assignment") and sometimes after an ABC is largely completed. Reported cases regarding ABCs are relatively few, especially modern ones, and therefore, much of what is discussed in this article is based on practical experience, as well as published and unpublished cases.

I. BRIEF OVERVIEW OF ABCS

ABCs are state or common law alternatives to bankruptcy, which trace back to English common law.[1] In an ABC, the company, or assignor, makes an assignment of all of its assets to a trustee, or assignee, who is charged with liquidating the assets and distributing the proceeds to the company's creditors, the beneficiaries of the trust formed by the ABC. Because the ABC is a trust, the consent of the creditors/beneficiaries to the ABC is not required for the assignment to be effective.

In recent years, ABCs have been used frequently in some states, such as California, Florida, Illinois, Massachusetts and Wisconsin and infrequently or rarely in other states. ABCs in some states are based on common law and in other states on statutes.[2] In some states, there is a supervising court[3] and in other states there is no formal court process unless the assignee files a separate proceeding.[4]

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[1] *See* James A. Chatz & Joy E. Levy, *Alternatives to Bankruptcy*, 17 NORTON J. BANKR. L. & PRAC. 149, 153 (2008) (discussing ABCs as common law based alternative to bankruptcy); Mette H. Kurth & Theodore A. Cohen, *Bankruptcy Practitioners, Get Your Guns:* Haberbush *and* Sherwood Partners *Set the Stage for a Showdown Between the Code and State ABC Law*, 25 AM. BANKR. INST. J. 32, 32 (July/Aug. 2006) (noting many California companies' preference of ABCs over bankruptcy due to cost-efficiency); *see also* Vivian Luo, Comment, *A Preference For States? The Woes of Preempting State Preference Statutes*, 24 EMORY BANKR. DEV. J. 513, 521–26 (2008) (discussing state collective action proceedings, and ABCs in particular, as bankruptcy alternatives).

[2] *See* Denis T. Rice, *Building a Strategic Internet IP Portfolio in a "Down" Economy*, 754 PRACTICING L. INST. 391, 419 (2003) ("ABC procedures originated in common law, but a number of states have formalized the procedures by statute . . . ."); *see also* Chatz & Levy, *supra* note 1, at 154 (noting various state statutory schemes regarding common law ABCs: some merely codify it while others essentially override it); Luo, *supra* note 1, at 523 (noting ABCs "stem from the common law right of assignment" and freedom of contract). Every state has at least one statute or rule in place that recognizes or impacts an assignment for the benefit of creditors. Provisions typically include avoidance actions, creditor notification requirements, lien creditor status and certain priority provisions. *See* Rice, *supra*, at 419 (noting some state statutes requiring

"specific types of notice, filing and accounting"); Chatz & Levy, *supra* note 1, at 154 (discussing statutes that override common law ABCs by requiring various formalities for making assignments, such as recording and notice to creditors); *cf.* Ronald J. Mann, *An Empirical Investigation of Liquidation Choices of Failed High Tech Firms*, 82 WASH. U. L.Q. 1375, 1389 (2004) (describing California's provisions requiring written notice from assignee to all creditors and equity holders within thirty days of assignment). Thirty-three states and the District of Columbia have statutory assignment for the benefit of creditor provisions. Notably, some of the states in which assignments are more common, like Illinois, do not have statutory assignments. *See* Bruce C. Scalambrino, *Representing a Creditor in an Assignment for the Benefit of Creditors*, 92 ILL. B.J. 263, 263 (2004) (outlining Illinois' codification and repeal of ABC provisions, leaving the field governed by common law since 1939); *see also* Black v. Palmer, 145 N.E.2d 797, 799 (Ill. App. Ct. 1957) ("From 1877 until 1939 there was a statute in Illinois governing voluntary assignments for the benefit of creditors." (citing ILL. REV. STAT. 1937, ch. 10 ¾)). States that have core statutory regimes include:

A. Arizona—ARIZ. REV. STAT. ANN. §§ 44-1031 through 44-1047 (West 2009);
B. Arkansas—ARK. CODE ANN. §§ 16-117-401 through 16-117-407 (West 2009);
C. Colorado—COLO. REV. STAT. ANN. §§ 6-10-101 through 6-10-154 (West 2009);
D. Delaware—DEL. CODE ANN. tit. 10, §§ 7381 through 7387 (2009);
E. Florida—FLA. STAT. ANN. §§ 727.101 through 727.116 (West 2009);
F. Georgia—GA. CODE ANN. §§ 18-2-41 through 18-2-59 (West 2008);
G. Iowa—IOWA CODE ANN. §§ 681.1 through 681.30 (West 2009);
H. Kentucky—KY. REV. STAT. ANN. §§ 379.010 through 379.170 (West 2009);
I. Massachusetts—MASS. GEN. LAWS ANN. ch. 203 §§ 40 through 42 (West 2009);
J. Michigan—MICH. COMP. LAWS ANN. §§ 600.5201 through 600.5265 (West 2009);
K. Minnesota—MINN. STAT. ANN. §§ 577.01 through 577.10 (West 2009);
L. Mississippi—MISS. CODE. ANN. §§ 85-1-1 through 85-1-19 (West 2008);
M. Missouri—MO. ANN. STAT. §§ 426.010 through 426.410 (West 2009);
N. Montana—MONT. CODE. ANN. §§ 31-2-201 through 31-2-230 (2009);
O. New Jersey—N.J. STAT. ANN. §§ 2A:19-1 through 2A:19-50 (West 2009);
P. New Mexico—N.M. STAT. ANN. §§ 56-9-1 through 56-9-55 (West 2009);
Q. New York—N.Y. DEBT. & CRED. LAW §§ 1 through 24 (McKinney 2009);
R. North Carolina—N.C. GEN. STAT. ANN. §§ 23-1 through 23-48 (West 2008);
S. North Dakota—N.D. CENT. CODE §§ 32-26-01 through 32-26-06 (2009);
T. Ohio—OHIO REV. CODE ANN. §§ 1313.01 through 1313.59 (West 2009);
U. Oklahoma—OKLA. STAT. ANN. tit. 24, §§ 31 through 50 (West 2009);
V. Pennsylvania—39 PA. STAT. ANN. §§ 1 through 154 (West 2009);
W. Rhode Island—R.I. GEN. LAWS §§ 10-4-1 through 10-4-13 (2009);
X. South Carolina—S.C. CODE ANN. §§ 27-25-10 through 27-25-160 (2008);
Y. South Dakota—S.D. CODIFIED LAWS §§ 54-9-1 through 54-9-22 (2009);
Z. Tennessee—TENN. CODE ANN. §§ 47-13-101 through 47-13-120 (West 2009);
AA. Texas—TEX. BUS. & COM. CODE ANN. §§ 23.01 through 23.33 (Vernon 2009);
BB. Utah—UTAH CODE ANN. §§ 6-1-1 through 6-1-20 (West 2008);
CC. Vermont—VT. STAT. ANN. tit. 9, §§ 2151 through 2158 (2009);
DD. Virginia—VA. CODE ANN. §§ 55-156 through 55-167 (West 2009);
EE. Washington—WASH. REV. CODE ANN. §§ 7.08.010 through 7.08.200 (West 2009);
FF. West Virginia—W. VA. CODE §§ 38-13-1 through 38-13-16 (2009);
GG. Wisconsin—WIS. STAT. ANN. §§ 128.001 through 128.25 (West 2008); and
HH. District of Columbia—D.C. CODE §§ 28-2101 through 28-2110 (2009).

Statutory assignments differ between states. Seventeen states do not have statutes governing ABCs. States that have enacted such statutes may generally be categorized into three levels of statutory requirements. The first level includes minimalist states, which have basic assignment provisions, typically ones permitting an assignment for the benefit of creditors and requiring the recording of the assignment, which permits an assignee to benefit from lien creditor status under the UCC. Outlier states in this minimalist category will typically have either a requirement to notify creditors of the ABC, or avoidance statutes, or both. The second tier includes states with a medium amount of statutory requirements, which typically have both notification requirements and avoidance provisions, in addition to the requirements seen in minimalist states. Outliers at this level have priority provisions for certain types of unsecured claims, or claims adjudication procedures, or both. Finally, states with the widest scope of statutory requirements will include all, or almost all, of these provisions. Florida has an expansive statutory scheme that includes all of these provisions. Notably, however, core assignment provisions are not based upon a uniform act[5] and therefore, are phrased and interpreted differently, as well as impose divergent requirements. Practitioners should be

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[3] *See* Freeman v. Marine Midland Bank New York, 419 F. Supp. 440, 447 (E.D.N.Y. 1976) ("Upon assignment the assignee takes title to the debtor's estate as trustee for all the creditors under the court's supervision and the estate is in custodia legis.") (citation omitted); Moecker v. Antoine, 845 So.2d 904, 910 (Fla. Dist. Ct. App. 2003) (citing FLA. STAT. ANN. § 727.101 (1997)) (explaining purpose of statute as providing uniform procedure for administering insolvent estates, all subject to supervision of circuit court); Premke v. Pan Am. Motel, Inc., 151 N.W.2d 122, 126 (Wis. 1967) ("'The circuit courts shall have supervision of proceedings under the provisions of this chapter . . . and all assignments for the benefit of creditors shall be subject to the provisions of this chapter.'" (quoting WIS. STAT. ANN. § 128.01)).

[4] *See* People v. Warfel, 328 P.2d 456, 460 (Cal. Dist. Ct. App. 1958) ("At bar we deal with common law assignments; they do not in any sense place the property *in custodia legis*. The administration of such an assignment is not subject to court control except through a plenary equity case."). *See generally* McKelvy v. Striker, 116 P.2d 921 (Colo. 1941) (stating though assignor not meeting statutory provisions may have fewer protections, assignment is nonetheless a valid common law assignment even when done with no court involvement).

[5] *See* 9 WILLIAM L. NORTON, JR., NORTON BANKRUPTCY LAW AND PRACTICE 3d § 171:1 (2009) (describing various degrees of comprehensiveness in state ABC statutes); *cf.* Alan J. Feld, Note, *The Limits of Bankruptcy Code Preemption: Debt Discharge and Voidable Preference Reconsidered in Light of* Sherwood Partners, 28 CARDOZO L. REV. 1447, 1449 (2006) ("[A]ssignments [for the benefit of creditors] originated out of common law notions of ordinary property transfer and trust creation . . . ."). While avoidance actions and lien creditor statutes are not considered core assignment provisions, they stem from uniform acts such as the Uniform Fraudulent Transfer Act, the Uniform Fraudulent Conveyance Act, and the Uniform Commercial Code, respectively, and, therefore, are typically phrased and interpreted similarly. *See* Ziad Raymond Azar, *Bankruptcy Policy: A Review and Critique of Bankruptcy Statutes and Practices in Fifty Countries Worldwide*, 16 CARDOZO J. INT'L & COMP. L. 279, 369–70 (2008) (noting comprehensiveness of Uniform Fraudulent Transfer Act, now adopted by 39 states); *see also* Shu-Yi Oei, *Context Matters: The Recharacterization of Leases in Bankruptcy and Tax Law*, 82 AM. BANKR. L.J. 635, 660 (2008) ("Since the UCC is intended to be a uniform law, the rules and factors applied should be quite similar between states."); Michael C. Dorf, *Dynamic Incorporation of Foreign Law*, 157 U. PA. L. REV. 103, 146–47 (2008) ("[S]ome version of the UCC is in force in all fifty states."). The American Bankruptcy Institute has prepared a proposed model act for ABCs. *See* AMERICAN BANKRUPTCY INSTITUTE, GENERAL ASSIGNMENTS FOR THE BENEFIT OF CREDITORS: A PRACTICAL GUIDE (2000).

careful to refer to these provisions when conducting assignments in states in which they do not operate routinely.

ABCs can be less expensive and more flexible than bankruptcy cases.[6] They are often used to quickly sell some or all of a business, either as a going concern or to conduct an orderly winddown, and to determine claims to the proceeds therefrom.[7] Other existing materials address the basics of ABCs and why it may be desirable to make an assignment. We refer you to those materials for a more general background on ABCs.[8] This Article assumes a decision to make an assignment has occurred and then addresses issues which may arise over the course of the assignment. It does not address other out of court alternatives, such as receiverships, trade compositions, consent agreements, friendly foreclosures or other structures that may share some of the same benefits of an ABC.

II. MAKING AN ASSIGNMENT FOR THE BENEFIT OF CREDITORS

Corporate and Shareholder Authorization—After a company has decided to undertake an ABC, it must follow the requirements of its articles of incorporation and by-laws, as well as those of its state of incorporation in order to authorize the assignment. The corporate authorization to assign all assets is usually the subject of a board resolution and shareholder consent.[9] It may be difficult to obtain corporate

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[6] *See* Mike C. Buckley & Gregory Sterling, *What Banks Need to Know About ABCs*, 120 BANKING L.J. 48, 49 (2003) (describing an ABC's simplicity as non-judicial, less costly process, which allows flexibility and innovation); Lloyd King, *A Chart of Bankruptcy Jurisdiction for Admiralty Lawyers*, 59 TUL. L. REV. 1264, 1294 (1985) ("[A]ssignments for the benefit of creditors may be less time-consuming, less expensive, or otherwise preferable."); Kurth & Cohen, *supra* note 1, at 32 (noting the efficiency of ABCs).

[7] *See* David S. Kupetz, *Assignment For The Benefit Of Creditors: Exit Vehicle of Choice for Many Dot-Com, Technology, and Other Troubled Enterprises*, 11 J. BANKR. L. & PRAC. 71, 81 (2001) (stating ABCs are particularly useful "when fast action" needed for capturing value).

[8] *E.g.*, GEOFFREY L. BERMAN, GENERAL ASSIGNMENTS FOR THE BENEFIT OF CREDITORS: THE ABCS OF ABCS (American Bankruptcy Institute 2d ed. 2006) (guide on administration of ABCs and the differences various states' laws have on administration); Geoffrey L. Berman & Robert J. Keach, *"The Receivership Alternative"—A Response*, 20 AM. BANKR. INST. J. 26 (July/Aug. 2001) (discussing distinctions between states' laws on ABCs and receiverships); Geoffrey L. Berman & Catherine E. Vance, *State Law Preference Actions: Still Alive after* Sherwood Partners v. Lycos, 26 AM. BANKR. INST. J. 24 (Dec./Jan. 2008) (discussing rift in precedent concerning preemption of state law preference and avoidance actions); Jeffrey Davis, *Florida's Beefed-Up Assignment for the Benefit of Creditors as an Alternative to Bankruptcy*, 19 U. FLA. J.L. & PUB. POL'Y 17 (2008) (surveying operation of and recent amendments to Florida's comprehensive statutory scheme on ABCs); Leslie R. Horowitz & John A. Lapinski, *Advising Distressed Businesses on an Alternative to Bankruptcy*, 24 L.A. LAW. 18 (Sept. 2001) (discussing nuts and bolts of execution of assignments for the benefit of creditors, with emphasis on California state law); Paul A. Lucey, *The Liquidating "Chapter 11" in State Court*, 20 AM. BANKR. INST. J. 12, 12–13 (Feb. 2001) (discussing advantages and disadvantages of ABCs versus bankruptcy from the vantage point of receivership).

[9] *See* Scott v. Nat'l City Bank of Tampa, 139 So. 367, 369 (Fla. 1931) ("The rule is that unless otherwise provided by statute a corporate assignment must be executed by the board of directors at a meeting duly called for that purpose or be executed by an officer of the corporation duly authorized by a resolution of the board of directors."); Kolton v. K & L Furniture & Appliances, Inc., 403 N.E.2d 478, 484 (Ill. App. Ct. 1979) (determining that Illinois state law entitles shareholders of record to receive notice and have the ability to vote on assignment). *But cf.* Calumet Paper Co. v. Haskell Show-Printing Co., 45 S.W. 1115, 1115 (Miss.

authorization for an ABC of a widely-held, public company where either the articles of incorporation or state law require approval by a majority of the shareholders. For example, the Illinois Business Corporation Act requires the approval of two-thirds of the shareholders for an assignment, unless the company's articles of incorporation require a different amount, but not less than a majority.[10] A widely-held, public company incorporated in Illinois probably would not find an ABC cost-effective for this reason. More typically, closely held, non-public companies utilize the assignment process. Counsel is advised to examine the company's incorporation documents and state law to determine the specific requirements to authorize an assignment of all, or the majority, of a corporation's assets.

Selecting an assignee—In contrast to a bankruptcy trustee, an assignee is usually selected by the principals of the failing business, generally with the advice of counsel.[11] The following are key items for the company to consider in choosing an assignee.

> *Participation of Creditors in Selecting the Assignee*—If the business has a secured creditor with a lien on most or all assets, the secured creditor may participate in choosing the assignee, often through the referral of acceptable candidates. An assignee should not accept an ABC without the secured creditor's knowledge and, at least, implicit consent. Express consent is greatly preferred in order to facilitate the ABC. This is because the assignee, while having the rights of a lien creditor pursuant to Uniform Commercial Code section 9-309(12), is junior in priority to a properly perfected secured creditor. To liquidate the secured creditor's collateral, particularly where the secured creditor may not be paid in full, the assignee must have the secured creditor's consent. Usually the secured creditor and the assignee will work out an agreement to allow possession and liquidation of the secured creditor's collateral, as well as compensation for such services, usually subject to a budget for the expenses of liquidation agreed upon with the secured creditor.
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> It is unusual for unsecured creditors to participate in the selection of the assignee.[12]

1898) (stating in certain circumstances, it is not only allowed, but the duty of the board of directors is to make an assignment against stockholder's wishes).

[10] 805 ILL. COMP. STAT. ANN. 5/11-60 (2009).

[11] *See* Buckley & Sterling, *supra* note 6, at 52 (2003) ("The Assignor with the advice of its lawyer chooses the Assignee . . . ."); *see also* Gilroy v. Somerville Woolen Mills, 58 A. 651, 651–52 (N.J. Ch. 1904) (stating, under New Jersey state law, that corporations have right to appoint an assignee, unless insolvent, and any appointed assignee may be removed).

[12] *Cf.* Sprinkle v. Wallace, 42 P. 487, 488 (Or. 1895) ("[W]hen creditors are not satisfied with the assignee named by the assignor [Oregon state law] prescribes the manner of selecting an assignee in his stead."); Bruce S. Nathan, Sherwood Partners *Threatens Viability of State Law Preference*, 24 AM. BANKR. INST. J.

Independence of Assignee—ABCs are effective when creditors have confidence that corporate insiders are not "pulling the wool over their eyes" and thereby benefiting from the liquidation to the creditors' detriment. Accordingly, the assignee should neither be a relative of the principals of the business, nor be related to or associated with a potential acquirer. Just as in bankruptcy, the ABC is dependent upon the transparency of the process. Therefore, an assignee should be free of any real or apparent ties with any potential beneficiary (owners, management, guarantors, acquirers or significant creditors).

It is not uncommon for the assignee to have previously performed services for the company before the assignment, such as turnaround consulting; however, the assignee should not be a creditor.[13]

Experience of the Assignee—In states where ABCs are commonly used, small cadres of professional assignees have developed. These individuals or firms are qualified based upon professional credentials (turnaround consultants, accountants and financial advisors) and prior experience liquidating businesses. The credibility of the assignment process is enhanced by the use of experienced, professional, and independent assignees.

Special needs of the liquidation—Most professional assignees do not specialize in particular industries or types of assets. To the extent that the liquidation requires specialized expertise, the assignee will call on other professionals. For example, where one of the creditors is a multi-employer pension fund, the assignee will retain counsel with specific experience in that area. In addition, if the business has specialized operations (e.g. livestock, health care), the assignee may hire an experienced manager to operate the business as the assignee's agent. The assignee may also choose to retain the assignor's management, due to their expertise and knowledge of the business and industry for certain tasks (although the assignee overall remains in charge). In selecting the assignee,

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16, 16 (May 2005) ("The debtor selects the assignee, in contrast to a chapter 7 case, where the U.S. Trustee selects, or in rare cases creditors elect, the bankruptcy trustee.").

[13] *See* Sherwood Partners, Inc. v. Lycos, Inc., 394 F.3d 1198, 1202 (9th Cir. 2005), *cert. denied*, 546 U.S. 927 (2005) (criticized as discussed below) (noting difference between "creditor," an entity with pre-petition claims against debtor, and "custodian," which includes ABC assignees (citing 11 U.S.C. § 101 (2006))); *see also* Nathan, *supra* note 12, at 66 (discussing Ninth Circuit's, in *Sherwood*, excluding ABC assignee's claims from "creditors' claims" that can be avoided under section 544).

> the assignor should ask how the assignee will address the special needs of the liquidation.
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> *Compensation arrangements*—Compensation arrangements for assignees vary depending on the nature of the assignment. An assignee will generally request a retainer sufficient to cover the fees and expenses for pre-assignment planning, as well as early assignment activities. After the initial retainer, the assignee's fees and expenses are paid from proceeds of the liquidation. The amount of the assignee's retainer will be based upon his estimate of fees for the assignment and the planned liquidity from the sale of the assets.
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> Most assignees favor strict hourly fee arrangements, but may entertain caps on total fees.[14] "Other assignees, particularly where a business is being sold as a going concern, may favor a contingent-fee arrangement."[15]

The Trust Agreement—Most assignees have a standard form trust agreement they utilize. Assignees are generally individuals, even if they are associated with turnaround firms and use staff from their firms to help administer the ABCs. Some assignees are attorneys (active and inactive) and others are turnaround or business professionals. If the state statute or common law requires it, assignments must be in writing.[16] In addition, all (not less than all) of the assignor's property has to be absolutely and unconditionally contributed into the trust or the assignment may be invalid, or at least voidable.[17] Notably, provisions limiting an assignee's

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[14] *See* Buckley & Sterling, *supra* note 6, at 52 ("Prudent Assignees will negotiate a specific agreement providing either an hourly rate for themselves and others who work with them or a commission based on the dollar volume of the assets that flow through the assignment estate together with reimbursement of their expenses."); Posting of Bob Eisenbach to The Business Bankruptcy Blog, http://bankruptcy.cooley.com/2008/03/articles/the-financially-troubled-compa/assignments-for-the-benefit-of-creditors-simple-as-abc/print.html (Mar. 16, 2008) ("The fees charged by assignees often involve an upfront payment and a percentage based on the assets liquidated.").

[15] JONATHAN FRIEDLAND, STRATEGIC ALTERNATIVES FOR DISTRESSED BUSINESSES § 8:6 (2008).

[16] *See* IOWA CODE ANN. § 681.2 (West 2009) ("Every such assignment [for the benefit of creditors] shall be by an instrument in writing . . . ."); Bartemeier v. Cent. Nat'l Fire Ins. Co., 160 N.W. 24, 29 (Iowa 1916) (Iowa statute expressly requires assignment be in writing); *see also* Ill. Bell Tel. Co. v. Wolf Furniture House, Inc., 509 N.E.2d 1289, 1292 (Ill. App. Ct. 1987) (finding attempted ABCs invalid due to noncompliance with writing requirement); Hockaday v. Drye, 54 P. 475, 479 (Okla. 1898) (noting ABC is required to be in writing).

[17] *See* W., Oliver & Co. v. Snodgrass, 17 Ala. 549, 556–57 (1850) (declaring void assignment agreement that would exclude some creditors because "all the property must be absolutely and unconditionally devoted to the payment of the debts"); Brown Shoe Co. v. Stone, 292 S.W. 117, 120 (Ark. 1927) ("'An insolvent debtor can reserve no use or benefit to himself out of the property assigned. He may stipulate for a release, but he must dedicate all of his property, not exempt by law, to the payment of all his creditors . . . .'" (quoting McReynolds v. Dedman, 1 S.W. 552, 553 (Ark. 1886))); H. D. Lee Mercantile Co. v. Dieter, 288 P. 545, 548 (Kan. 1930) ("[A]n assignment for the benefit of creditors must assign all the debtor's nonexempt property otherwise it is void."). *But see* Perry v. Vezina, 18 N.W. 657, 658 (Iowa 1884) (recognizing that assigning all assets "'except such as the law excepts'" does not invalidate assignment).

responsibility or liability for negligence, misconduct or the like can invalidate an assignment in certain states.[18]

The trust agreement may include representations, warranties and covenants by both the assignor and its officers and directors, including: (a) accuracy and completeness of the list of creditors; (b) provision of requested information regarding the debtor's assets and liabilities; (c) performance of any and all acts reasonably necessary and proper to assist in orderly administration; and (d) execution and delivery of documents or instruments necessary or appropriate for performance of the assignee's duties.[19]

Judicial Oversight—In some jurisdictions, the assignment process is well defined by updated and detailed statutes.[20] In others, the statutes are skeletal, or absent altogether, and therefore, it is important that the trust agreement recite the assignee's rights and responsibilities in detail in order to mitigate the need for judicial review.[21] In jurisdictions with older statutes involving court supervision and where ABCs are infrequent, litigation may be presided over by a judge who has never encountered an ABC, and who may either: (i) be unenthusiastic about the case, and/or (ii) have a tremendous learning curve, which slows and complicates administration and sale of the assets (i.e. writing from scratch a playbook that a veteran bankruptcy judge would know by heart).

III. PRE-ASSIGNMENT PLANNING

Before an assignee accepts the position and executes the trust agreement, he or she should address the following key items.

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[18] *See* Tribune Co. v. R. & J. Furniture Sales, Inc., 155 N.E.2d 844, 846 (Ill. App. Ct. 1959) (holding clause relieving trustee of responsibility for wrongful acts is void); *see also* Carlton, Clark & Co. v. Baldwin, 22 Tex. 724, 731 (1859) ("The limitation of the responsibility of the trustee, so as to excuse him from being answerable for the 'negligence and misdoings' of others, is a badge of fraud.") (citation omitted). *But see* Endicott-Johnson Corp. v. Lurie, 278 P. 693, 694 (Wash. 1929) (stating while trustee is not permitted to contract against his own wrongful act, attempts to do so do not necessarily invalidate assignment).

[19] *See e.g.*, Melanie Rovner Cohen & Joanna L. Challacombe, *Assignment for Benefit of Creditors—A Contemporary Alternative for Corporations*, 2 DEPAUL BUS. L.J. 269, 283 (1990) (providing sample form whereby assignor guarantees assignee of reporting accuracy and warrants against unlawful preferences); *cf.* Isaacson v. Davis, 143 A. 788, 791 (Me. 1928) (dealing with problems, arising out of incomplete or unwarranted creditor lists, such as notification issues which may in turn deem assignment voidable).

[20] *E.g.*, VT. STAT. ANN. tit. 9, §§ 2151–58 (2008) (listing requirements for ABC, including that it: "*shall* be in writing," "*shall* be for the benefit of all the creditors," "*shall* be specific," "*shall* file in the clerk's office," etcetera) (emphasis added); Metro Burak, Inc., v. Rosenthal & Rosenthal, Inc., 380 N.Y.S.2d 758, 760 (N.Y. App. Div. 1976) (holding provisions of New York statute on ABCs mandatory and failure to meet same renders assignment ineffective).

[21] *See supra* note 2 and accompanying text (listing various levels of statutorily detailed requirements for ABCs); *cf.* James L. Ryan, *Considering Non-Bankruptcy Alternatives in the Wake of the Revised Bankruptcy Code*, 20 J. DUPAGE COUNTY B. ASS'N 24, 25–26 (2008) (noting *Bell*'s rejection of "'middle ground approaches'" and "[t]herefore . . . one must be extremely careful to comply with all the common law requirements." (citing *Ill. Bell Tel. Co*., 509 N.E.2d at 1292)).

Identification of Assets—The assignee should receive comprehensive information on the type and location of assets, including paper and electronic records and passwords, as well as on how to take control or possession of the assets.

1. *Cash and bank accounts*—Assignee should obtain lists of all bank accounts and bank contact information, as well as the purpose and use of each account (e.g. payroll, operation, location depository). Generally, the assignee will close all existing bank accounts and open new accounts in his or her name, as assignee for the benefit of creditors. Note that the Federal Employer Identification Number ("FEIN") for assignee accounts is the debtor's/assignor's FEIN, not the FEIN of the assignee. In practice, the assignee may choose to keep certain pre-assignment bank accounts open to allow transactions, such as payroll or lease payments, to clear or to collect receivables such as credit card receipts. In those cases, the assignee should have exclusive authority to transfer funds to and from any pre-assignment accounts by notifying the bank. The assignee can choose to leave sufficient funds in disbursing accounts to cover outstanding checks, or review presentments to the bank on a daily basis and transfer funds to cover such checks.

2. *Inventory and other physical assets*—The assignee will receive information on the location of all physical assets and should consider their physical security. He may wish to inspect the assets before accepting the assignment in order to determine what security measures are necessary. For example, locks may need to be changed, or at least access to keys restricted. Security codes on alarm systems may need to be changed. If practical, an immediate physical inventory count should be undertaken after possession is established. The assignee should also determine the coverage and term of insurance over physical assets.

3. *Real property*—The assignee should consider how or whether to record title in real property. The jurisdiction of the ABC, location of the property, nature of existing title (for instance—held in land trust), environmental concerns and current use of the property are all factors to consider,

as well as the cooperation of the assignor. In Illinois, for example, assignees normally do not record a change in title, but rather obtain the agreement of the assignor to execute documents necessary to dispose of the assets.[22] This agreement may be part of the trust agreement.

4. *Accounts receivable*—The assignee should review expected collections and their timing and know the location of paper and electronic records supporting amounts due.

5. *Intellectual property*—The assignee should understand the nature of intellectual property[23] and software, as well as know the location of related paper and electronic records. Contact information of employees with knowledge of those assets should be obtained. Again, the agreement of the assignor and its principals to execute any and all documents necessary to transfer intellectual property to a purchaser should be specified in the trust agreement. Where there is a material license of intellectual property to the business, it is desirable to inquire about the licensor's willingness to permit an assignment of that license.

Lien, lawsuit and judgment search—The assignee or his counsel should conduct a lien, lawsuit and judgment search on the debtor prior to accepting an assignment. The information is useful for identifying assets and creditors, as well as reviewing the validity of secured creditors' liens.

Insurance and bonds—The assignee should determine whether assets are appropriately insured prior to accepting the assignment and should add his or her name as an additional insured on existing policies. Notably, bonding requirements are dependent upon the jurisdiction. The continuation of health, workers' compensation

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[22] *See* 15A WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 7389 (perm. ed., rev. vol. 2000) (stating generally that "in the absence of a statutory provision an assignee for the benefit of creditors does not take title to property held in trust," but noting jurisdictions that differ from this general rule).

[23] *See* Stephen I. Willis & Craig T. Elson, *Managing Intellectual Property in Debtor-Creditor Relationships*, 12 AM. BANKR. INST. J. 13, 19–20 (May 1993) (discussing importance of intellectual property as collateral, specifically in debtor-creditor situations); *cf.* Rita Hayes, *Promoting Intellectual Property for Economic Growth*, 36 VAND. J. TRANSNAT'L L. 793, 794 (2003) (advocating for more comprehensive understanding of intellectual property, legally and more broadly, by "the public at large"); Kevin M. Lemley, *I'll Make Him an Offer He Can't Refuse: A Proposed Model for Alternative Dispute Resolution in Intellectual Property Disputes*, 37 AKRON L. REV. 287, 292–93 (2004) (stressing importance of in-depth understanding of intellectual property to facilitate strategic dealings).

and other employee-related insurance will depend on whether employment will continue post-assignment.

Employee severance issues—The assignee should consider whether any employees will be offered continuing employment and what benefits will be offered, such as health insurance, vacation time, severance, or retention bonuses. To ensure against any liability under existing severance agreements or the WARN Act, the assignor may effectively terminate all employees prior to the assignment.[24] Collective bargaining agreements, when present, should also be considered.

Budgets—The most important pre-assignment task is preparing an estimated budget of cash receipts and disbursements, particularly when the assignee will be operating the business for a period of time.[25] If cash and cash receipts are not sufficient to fund the estimated expenses of preserving and liquidating the assets, the assignee must make arrangements to fund the shortfall before accepting the assignment.

Financing an ABC—Generally, there are three potential sources of financing for an ABC:

1. *Existing secured lender*—Unlike in bankruptcy, the assignee-trustee has no power to force a non-consensual use of cash collateral or proceeds of sale, a priming lien on existing collateral, or a sale free and clear of liens and encumbrances.[26] Therefore, it is crucial to have an understanding or agreement with existing secured lenders as to how the ABC will be financed, what collateral or proceeds the assignee will be permitted to utilize, as well as at what price and conditions the secured creditor will agree to release its recorded liens on encumbered assets.

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[24] *See In re* Gen. Assignment for Benefit of Creditors of Peter Puppet Playthings, Inc., 199 N.Y.S.2d 687, 688–89 (N.Y. App. Div. 1960) (finding assignee's termination of employee upon assignment was not for cause, but under liquidation of business provision); Laura B. Bartell, *Why Warn?—The Worker Adjustment and Retraining Notification Act in Bankruptcy*, 18 BANKR. DEV. J. 243 (2001) (arguing for broader applicability of WARN termination notice requirements on fiduciaries liquidating estates in bankruptcy).

[25] *See In re* Computer Learning Ctrs., Inc., 272 B.R. 897, 911 (Bankr. E.D. Va. 2001) (articulating importance of working within well defined budget, particularly in management transfers, such as in instances where a trustee takes charge).

[26] *See* 11 U.S.C. § 363(f) (2006) (permitting sale of property of the estate even outside ordinary course of business in the bankruptcy context).

2. *Potential purchaser/stalking horse bidder*—If the assignee is fortunate enough to have a "stalking horse" offer for the assets prior to accepting the assignment, an effective financing method is to have the bidder finance the operations while the business is marketed. Advances by the stalking horse bidder would then be part of the consideration for the assets. If the stalking horse bidder is outbid, the proceeds of the sale would be used to pay back the advances. If there is an existing secured lender who is not being paid in full, a separate agreement to allow the stalking horse advances to be repaid from proceeds would be needed.

3. *Company principals or guarantors*—A company's principals, particularly where the principals have guarantied the debt to a secured creditor, may also agree to fund assignment expenses, usually as a secured loan to the assignee. The security would typically be junior to existing security interests. This is a less common practice, but not unusual.

IV. THE CREDITOR NOTIFICATION PROCESS

Assignees will send a letter or notice to all creditors early in the assignment explaining that an assignment has occurred, how to contact the assignee, the expected general path for the business during the assignment and how to submit claims, including a bar date for filing claims, if applicable.[27] The notice may also contain a short description of reasons for the company's demise. A common form of notice also includes a summary statement of assets and liabilities of the business, so as to provide the creditors with an idea as to whether a distribution is likely and to enhance transparency in an effort to facilitate a consensual ABC. Because transparency is a key factor to the success of an ABC, liabilities should be broken out into at least the following categories—secured lenders, employees, taxing authorities and insiders or related parties. Because all assets and liabilities may not yet be identified, the statement should contain an appropriate disclaimer and disclosure of the source of the information. The following is an example—"All information was compiled using the XYZ Company's books and records and is unaudited. Accordingly, neither XYZ Company nor Jon Smith, as assignee, represents or warrants that this information is entirely accurate or complete."

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[27] *See generally* Cohen & Challacombe, *supra* note 19, at 276 (explaining notification coupled with request for creditors to submit claims under Illinois law); Eisenbach, *supra* note 14 (describing notice as including notification of bar date by which claim must be filed under California law).

It is recommended that the assignee send the notice to all applicable taxing authorities, even if records do not show a liability outstanding. Additionally, depending on circumstances such as the quality of the assignor's records, the assignee may wish to send the notice to possible creditors, for example, all vendors paid in the past twelve months. To do so, the assignee must obtain contact information for all creditors. Besides the current accounts payable listing, the assignee should seek contact information for:

1. Past and current employees (employed within the last year);
2. Landlords;
3. Lessors of equipment;
4. Counsel for both sides of outstanding lawsuits;
5. Customers who have placed outstanding deposits; and
6. Collection agencies who have notified the assignor.

Creditor consent is not necessary for an assignment to be valid.[28] Under trust law, a beneficiary of a trust need not consent to the trust. Notably, assignments can be declared void due to onerous conditions on creditors, that is, the assignment cannot force a creditor to release obligations as a condition to distribution of the corpus.[29] The assignee should be careful in drafting the notice of the assignment and claim forms to ensure there are no, and there do not appear to be, conditions for a creditor to participate in the distributions.

V. OPERATING WHILE IN AN ABC

An assignee should carefully consider whether to operate a business during an assignment, given there is some degree of risk to the assignee. Appropriate levels of insurance must be maintained, including property, liability and workers' compensation insurance.

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[28] *See* Watson v. Willerton, 258 Ill. App. 390, 399 (Ill. App. Ct. 1930) ("[ABC] of the property of an insolvent debtor will be carried into effect even though there are no assenting creditors.") (citation omitted); *see also* Star v. Johnson, 44 S.W.2d 429, 432 (Tex. Civ. App. 1931) (observing past holdings finding that non-consenting creditors cannot defeat purpose of assignment through certain specified methods), *writ of error denied*, 47 S.W.2d 608 (Tex. 1932), *aff'd*, 287 U.S. 527 (1933).

[29] *See* Consol. Pipe & Supply Co. v. Rovanco Corp., 897 F. Supp. 364, 370 (N.D. Ill. 1995) ("[A]n assignment for the benefit of creditors is invalid and unenforceable against nonparticipating creditors if it forces a creditor to accept a pro rata share of the amount owed in settlement of its claim, or if it otherwise contains conditions 'onerous' to creditors."); *see also In re* Colony Press, Inc., 83 B.R. 862, 869 (Bankr. D. Mass 1988) (naming two reasons for voiding assignments requiring release of claims: fraudulent transfer law and "general policy against unfair coercion"); Gessler v. Myco Co., 172 N.E.2d 503, 504 (Ill. App. Ct. 1961) ("[A]n assignment must not contain a condition requiring a full release in order for a creditor to secure partial payment.").

There are generally three circumstances where an assignee would consider operating the assignor's business:

> *The assignee has accepted an offer for the assets as a going concern, subject to higher and better offers*—In this circumstance, the assignee should structure the transaction so that the prospective purchaser is responsible for funding cash shortfalls and/or operating losses starting from the acceptance of the offer. The assignee should obtain a sufficient deposit or security from the purchaser to cover anticipated shortfalls and losses. As part of its offer, the purchaser may obtain bid protection, i.e. any higher and better offer must be higher than the first offer plus the purchaser's expected or actual funding of the operations.
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> *Completion of work in process*—Where the business has work in process or partially completed orders for its customers, the assignee may determine that the maximum proceeds will be generated by completion. Again, the assignee must carefully budget and locate a funding source for the costs of completion (such as existing cash, borrowings from a secured lender, or even additional deposits from customers). Of course, the customer should be contacted to determine whether it wants the product completed.
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> *Retail liquidations*—ABCs can be effective in the liquidation of small retail establishments. The assignee should be familiar with local "going out of business sale" ordinances, or hire a retail liquidator to assist in the process. The assignee does not have the same powers of a bankruptcy trustee and cannot require landlords to allow a going out of business sale if the lease prohibits it.[30] The assignee may need to use gentler signage to promote the retail liquidation.

Other practical issues in operating a business during an ABC include:

> *Employment and Independent Contractor Issues*—Often, the assignee does not continue to offer certain benefit programs such as

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[30] *See In re* Tobago Bay Trading Co., 112 B.R. 463, 467 (Bankr. N.D. Ga. 1990) (allowing trustee in bankruptcy to conduct liquidation despite lease provision prohibiting it, as such provision is ignored under 11 U.S.C. section 365(b)(2)(a) and (e)(1)(A)); *see also In re* Ames Dep't Stores, Inc., 136 B.R. 357, 359 (Bankr. S.D.N.Y. 1992) ("[T]o enforce the anti-GOB sale clause of the Lease would contravene overriding federal policy requiring Debtor to maximize estate assets by imposing additional constraints never envisioned by Congress."); *cf. In re* Lisbon Shops, Inc., 24 B.R. 693, 695 (Bankr. E.D. Mo. 1982) (stating bankruptcy court's authority to alter private rights for benefit of estate (citing 11 U.S.C. §§ 365(e), 522(f))).

health insurance, 401(k) plans, vacation and paid time off because of the expense, time and risk in continuing the programs. For example, if the company was partially or fully self-insured for health coverage for employees, the assignee cannot reasonably take on that undefined exposure. Even if health coverage was provided under a conventional group plan, the ability of the assignee to offer health insurance benefits to the employees will depend upon the contractual provisions of the health insurance contract. Note that if health insurance cannot be maintained, COBRA coverage to former employees would also be cancelled. Unless the assignee reasonably believes that funds will be sufficient to pay all liabilities in that category (the priority of employee claims may differ from state to state), it is advisable not to allow paid time off that may be payments of pre-assignment earnings because these constitute pre-assignment liabilities. Often the assignee may need to increase wages slightly to reflect the discontinuance of benefit programs. Also, the assignee may consider retention agreements with key employees. Former employees are sometimes engaged as independent contractors to try to avoid some of these issues. Where there are unionized employees subject to a collective bargaining agreement, an additional level of analysis is needed.

Specialized Operational Knowledge—If the business has specialized operations, the assignee may hire an experienced manager to operate the business as the assignee's agent. The assignee may also choose to retain the assignor's management due to their expertise and knowledge of the business and industry. Another option, when the assignee has accepted a purchaser's offer (subject to higher and better offers), may be to hire the purchaser as the managing agent.

VI. MARKETING AND SALES OF ASSETS

Assignees often market assets for sale, either as a going concern or on a liquidation basis post-shutdown. The marketing and sale processes tend to be expedited and often are a final attempt to realize value after pre-assignment marketing efforts did not generate sufficient interest/bid prices.[31] Sales are generally

[31] *See* Cohen & Challacombe, *supra* note 19, at 276–77 (citing speedy process as reason to choose ABC over bankruptcy); Feld, *supra* note 5, at 1448–49 (listing advantages of ABCs as their expeditious and less costly nature); Luo, *supra* note 1, at 522 (recognizing ABCs "as a 'cheap, expeditious, and convenient mode of arriving at the objects intended by [the Bankruptcy Law]'" (quoting Mayer v. Hellman, 91 U.S. 496, 498 (1875))).

advertised in newspapers[32] and often there is specific targeted marketing to competitors or other potential financial or strategic buyers.

Unlike bankruptcy, there typically are no powerful free and clear rights of section 363 of the Bankruptcy Code, nor the assignability rights for most leases and contracts under section 365 of the Bankruptcy Code (nor the benefit of the provisions finding that insolvency is not a default where sections 362 and 365 of the Bankruptcy Code apply).[33] There also may not be the ability to get judicially blessed bid procedures in advance of conducting an auction. As a result, the rules can be less clear in an assignee's sale and there may be more opportunities for losing bidders or other parties to challenge the conduct of the sale in some jurisdictions.[34] The assignee or the winning buyer may also need to strike deals with the contract counterparties or lessors for contracts or leases he wants assigned as part of the assignee's sale.

There is mixed law on whether a sale of assets on credit is permitted.[35] As a practical matter, assignees generally want immediate cash and, other than perhaps a modest holdback escrow, are generally reluctant to accept notes, earn-outs, stock or other non-cash consideration. A valid pre-assignment secured creditor, of course, can foreclose and accept whatever consideration is commercially reasonable under the UCC or other applicable law.[36]

A creditor, shareholder, or perhaps even a bidder who wants to challenge the sale may be able to challenge the accepted bid in certain jurisdictions and under certain circumstances.[37] Reasonable decisions of the assignee in the sale process, however, are likely to be deferred to by most courts.[38]

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[32] *See, e.g.*, *Consol. Pipe & Supply Co*., 897 F. Supp. at 367 (enumerating marketing efforts of assignee in ABC, including numerous newspaper ads and mass mailing to potential buyers).

[33] *See* Joel B. Weinberg, *California General Assignments: Still Alive, Kicking and Useful*, 29 CAL. BANKR. J. 293, 311 (2007) ("There is no state law analogue to section 365 of the Bankruptcy Code."); *see also* Kupetz, *supra* note 7, at 74 (noting vast difference between unified, detailed Bankruptcy Code and state-governed ABCs). *But see* Davis, *supra* note 8, at 22 ("With but a few exceptions, these powers [under Florida expansive ABC statutory scheme] parallel, and in at least one instance exceed, those of a trustee in bankruptcy." (citing FLA. STAT. § 727.108(1)(b) (2007))).

[34] *Compare* Ward v. Resolution Trust Corp., 796 F. Supp. 256, 259 (S.D. Tex. 1992) (finding no standing for unsuccessful bidder challenging sale by receiver for failure to show injury in fact as result of losing bid), *appeal dismissed*, 996 F.2d 99 (5th Cir. 1993), *with In re* Goyette & Lavigne, 244 F. 638, 640 (D. Mass. 1917) ("[A]ssignee's mistake as to his ownership of the articles here in question, and his selling them when he had no right to do so, imposed a liability on him, but one of a purely personal character [and] . . . impressed no trust or lien in the buyer's favor on the proceeds of the sale . . . ."), *and In re* Willett's Assignment, 23 A.2d 194, 197 (R.I. 1941) (reversing and holding that highest bidder had right to completion of sale when assignee tried to back out of sale and make new arrangement).

[35] *Compare* Pierce v. Brewster, 32 Ill. 268 (1863) (holding that subsequent assignment agreement annulling previously allowed sale on credit created new valid assignment), *with* Watson v. Willerton, 258 Ill. App. 390, 390 (Ill. App. Ct. 1930) (finding no evidence of particular agreement allowing for sale on credit).

[36] *See* U.C.C. § 9-627 (2000) (setting out standard for determining commercial reasonableness of sale); *see also In re* Gen. Indus., Inc., 79 B.R. 124, 131 (Bankr. D. Mass. 1987) (discussing various methods of determining reasonableness of sale).

[37] *See* Kabro Assocs. of W. Islip, LLC v. Colony Hill Assocs. (*In re* Colony Hill Assocs.), 111 F.3d 269, 273–74 (2d Cir. 1997) (analyzing various views on who has standing to challenge bankruptcy sale procedure and ultimately holding that losing bidders have such standing); *In re* Harwald Co., 497 F.2d 443, 444–45

VII. CLAIMS ADJUDICATION AND ATTEMPTS BY CREDITORS TO ENFORCE

The ABC trust is deemed separate from the pre-assignment entity[39] and therefore, any judgments or garnishments obtained or liens filed against the assignor entity after the assignment has occurred are generally not deemed to attach to the assets in the hands of the assignee.[40] This may be true regardless of whether the creditor or sheriff exercising remedies knew the assignment had taken place,[41] although not in all states and situations.[42]

Conversely, there is no automatic stay in an assignment[43] and often no clear means to block a foreclosure sale, judgment levy, or the like where the lien was in place pre-assignment. The assignee generally stands in the shoes of the assignor as of the date of the assignment and does not acquire greater rights than those held by the assignor .[44] To the extent assets are in multiple states, the assignee may want to consolidate physical assets to a single state or perhaps have multiple assignments in

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(7th Cir. 1974) (finding that losing bidder challenging intrinsic structure of bankruptcy sale "brings himself within the zone of interests which the Bankruptcy Act seeks to protect and to regulate" and therefore has standing to sue); *In re* Willett's Assignment, 23 A.2d 194, 196 (R.I. 1941) (holding highest bidder had standing to sue where lower court ordered new arrangement, post auction, to further benefit estate).

[38] *See* First Fed. Sav. & Loan Ass'n of Coeur D'Alene v. Marsh, 143 P.2d 297, 303 (Wash. 1943) (giving broad allowance to assignees to sell assets as they deem best, even if without notice of sale to creditors); Southworth v. Stout, 44 N.E.2d 225 (Ind. App. 1942) (en banc) (affirming the overruling of stockholders' objection to sale despite sale being private and argument that claims could have been satisfied by sale of less property); *see also* Mann, *supra* note 2, at 1419 (noting that even courts that are generally hostile to ABCs do not normally "intervene to second-guess business and liquidation decisions of the assignee").

[39] *See* City of New York v. United States, 283 F.2d 829, 831 (2d Cir. 1960) (observing transfer of title and creation of trust at time of assignment under New York law); Ill. Bell Tel. Co. v. Wolf Furniture House, Inc., 509 N.E.2d 1289, 1292 (Ill. App. Ct. 1987) ("The assignment 'passes the legal and equitable title to the property absolutely, beyond the control of the assignor.'" (quoting Browne-Chapin Lumber Co. v. Union Nat'l Bank of Chicago, 42 N.E. 967, 970 (Ill. 1886))); Cohen & Challacombe, *supra* note 19, at 270 ("The assignee then acts to insulate the debtor from his creditors because the legal title of the assigned assets passes from the debtor to the assignee.") (citation omitted).

[40] *See* Cohen & Challacombe, *supra* note 19, at 270 ("Although a creditor can proceed against the debtor for payment of his claim, the debtor, having relinquished all interest in the assets assigned, has no remaining assets which a creditor could garnish to satisfy claims."); *see also* Consol. Pipe & Supply Co. v. Rovanco Corp., 897 F. Supp. 364 (N.D. Ill. 1995) (observing post-assignment judgment creditor's attachment of assigned property is invalid); Int'l Brown Drilling Corp. v. Ferguson Trucking Co., 347 P.2d 773, 776 (Colo. 1959) ("[A]ssignment vests a legal title in the assignee, places the property beyond the control of the assignor and beyond the reach of any of his creditors . . . .").

[41] *See* Lowe v. Kean, 29 N.E. 1036 (Ill. 1892) (noting possible requirement of return of property levied post-assignment but before assignee had taken possession); *see also* Goodin v. Newcomb, 49 P. 821, 823 (Kan. Ct. App. 1897) (denying unwinding of assignment by post-assignment attachment despite assignee not yet having possession of property).

[42] *See*, *e.g.*, Anderson v. Zelensky, 15 P.2d 934, 935 (Wash. 1932) (noting past holding where assignment not binding on creditor who was not sent required notice).

[43] 11 U.S.C. § 362 (2006) (automatic stay in bankruptcy).

[44] *See* Chicago Title & Trust Co. v. Cent. Trust Co. of Ill. (*In re* Mossler Co.), 239 F. 262, 264 (7th Cir. 1917) (stating that assignee in insolvency is in no better position than assignor as against lienholders); Courtney v. Byram, 129 P.2d 721 (Cal. Dist. Ct. App. 1942) (allowing sale by state of collateral encumbered by tax lien despite ABC).

the main states, or other protections against extra-territorial attachment of assets. In one matter, a creditor attached a receivable from a customer where the customer and creditor were located in a jurisdiction outside of the state where the main assets were located and the assignment took place.

The priorities of different claims are determined by state law, which while they may have some similarities, are not identical to those under the Bankruptcy Code.[45] For example, tax and wage claims have been recognized as priority claims in ABCs.[46] Absent specific statutory authority (such as certain real estate taxes), priority claims would not prime prior properly recorded secured claims as to assets validly encumbered by such liens. The state law priorities, however, may be different from bankruptcy priorities in terms of (i) the amount of the priority, (ii) the order of the relative priorities and (iii) the extent of the priorities. For instance, most states would not recognize a priority for goods sold within twenty days of the assignment comparable to that found in section 503(b)(9) of the Bankruptcy Code as amended in 2005.[47] Likewise, some states may provide that tax claims have a higher priority than wage and benefit claims or that some of the caps or limitations on the amount of the priority claim may not be the same as those provided in the Bankruptcy Code.[48] Reclamation claims under Article 2 of the UCC may also be

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[45] *See* 11 U.S.C. § 507 (2006) (setting out priority of unsecured claims in bankruptcy).

[46] *See* Div. of Labor Law Enforcement v. Plotnek, No. 601-781, 1953 Cal. App. LEXIS 2055, at *7–8 (Cal. Super. Ct. July 29, 1953) (granting priority to tax claims incurred pre-ABC, followed by department of labor claims); *see also* Smith v. Toman, 14 N.E.2d 478, 479–80 (Ill. 1938) (observing common law rule that state claims take priority over other claims); Clift v. Tax Comm'n, 88 P.2d 372, 375–76 (Okla. 1939) (observing past case holding granting tax claims priority despite general creditors' challenge).

[47] *Compare* N.Y. DEBT. & CRED. LAW § 23 (2001):

> In all general assignments of the estates of debtors for the benefit of creditors no preference created therein, other than for the wages or salaries of or moneys held in trust for employees under section twenty-one-a and section twenty-two or cash deposits upon purchases for future delivery of merchandise or services under section twenty-two, shall be valid.

with FLA. STAT. ANN. § 727.114 (1) (West. 2009) (delineating priority of distribution of claims without indication for special treatment of claims of goods sold to assignor within twenty days prior to assignment), *with* 11 U.S.C. § 503(b)(9) (2006):

> After notice and a hearing, there shall be allowed administrative expenses . . . including . . . the value of any goods received by the debtor within 20 days before the date of commencement of a case under this title in which the goods have been sold to the debtor in the ordinary course of such debtor's business.

[48] *See* COLO. REV. STAT. § 6-10-130 (2008):

> The valid claims of servants, laborers, and employees of the assignor, for wages earned during the six months immediately preceding the date of the assignment, *not to exceed fifty dollars*, to any one person then unpaid, which claims are still held by the person who earned them, and all taxes assessed under the laws of this state, or of the United States, are preferred claims and shall be paid in full prior to the payment of the dividends in favor of other creditors.

entitled to priority status, as may certain deposit claims or certain governmental claims, fines and penalties which are not true tax claims.[49] Finally, there may be states where the relative priority of certain claims is unclear or there are other types of claims (such as PACA claims) which are not addressed by state law. One approach to consider in those circumstances is to set forth a priority in the trust agreement itself or, where available, to seek guidance from a chancery or other court on the relative priorities of competing claims.

Assignees may have powers under the UCC to avoid unperfected liens,[50] but, except in certain states, do not have the powers comparable to those a bankruptcy trustee would have to avoid preferentially perfected liens or liens which may be fraudulent transfers.[51] Nevertheless, assignees sometimes use the threat of a subsequent bankruptcy filing to get concessions from creditors whose liens or claims would be vulnerable to attack in a bankruptcy proceeding.

It is generally not proper to condition receipt of a distribution in an assignment upon the creditor releasing the debtor who made the assignment or any insiders/guarantors.[52] This goes beyond merely conditioning an assignment on a release and requires that the assignee not engage in conduct which could be read to be an attempt or request to obtain a release of the debtor or any guarantor or co-

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(emphasis added); N.C. GEN. STAT. § 23-10(2) (2007) ("[T]rustee . . . shall pay as speedily as possible . . . [w]ages due to workmen, clerks, traveling or city salesmen, or servants, which have been earned *within three months* before registration of said deed of trust or deed of assignment . . . .") (emphasis added); OHIO REV. CODE ANN. § 1313.43 (2006) ("Taxes of every description assessed against the assignor upon personal property held by him before his assignment for the benefit of creditors must be paid by the assignee or trustee out of the proceeds of the property assigned *in preference to any other claims* against the assignor.") (emphasis added).

[49] *See* DEL. CODE ANN. tit. 19, § 3363 (2005) (indicating adjudicated reclamation claim would be granted priority status after exceptions for taxes and wage claims); N.Y. DEBT. & CRED. LAW § 22(1) (McKinney 2001) (granting priority to claims for cash deposits left with assignor not to exceed $300); *see also* Weinberg, *supra* note 33, at 301–02 (indicating "[d]ebts due to the United States," a category which takes second priority under California priority scheme, is broader than corresponding priority provided by the Bankruptcy Code).

[50] *See* U.C.C. § 9-317(a)(2)(A) (2000) (giving, under Revised Article 9, lien creditors priority over unperfected security interests and unperfected agricultural liens); *cf.* 11 U.S.C. § 544(a)(1) (2006) (affording bankruptcy trustee, as of time of filing, same rights as judgment lien creditors for purposes of avoiding previously unperfected liens).

[51] *See* 11 U.S.C. §§ 547–48 (2006) (allowing trustee to avoid certain preferential or fraudulent transfers, defined broadly to include grants or perfection of liens); *In re* Gen. Assignment for Benefit of Creditors of Toys Galore, Inc., 437 N.Y.S.2d 227, 229 (N.Y. County Ct. 1981) (superseded by statute on other grounds) (allowing late filing of claim as unsecured due to failure to perfect).

[52] *See* Simmons Hardware Co. v. Rhodes, 7 F.2d 352, 354 (8th Cir. 1925) ("[I]f as found by the jury such condition for release and satisfaction of all the indebtedness of the maker of the assignment was made, then the entire assignment of the benefit of creditors was void and non-enforceable . . . ."); Fed. Deposit Ins. Corp. v. Juron, 713 F. Supp. 1116, 1120 (N.D. Ill. 1989) (holding that even if agreement were an ABC it would be voidable as it required "releases and covenants not to sue"). *But see* H. B. Claflin Co. v. Dacus, 59 F. 998 (C.C.D.S.C. 1894) (upholding validity of ABC and creditor's release even when such release was obtained as condition for distribution).

maker. Creditors can seek to compel a distribution or an accounting if the assignee fails to do so.[53]

VIII. SUBSEQUENT VOLUNTARY OR INVOLUNTARY BANKRUPTCY CASE

Creditors who are unhappy that they did not get paid pre-assignment or concerned that there will not be any distribution to them in the assignment sometimes threaten to file an involuntary petition against the assignor entity or, in fact, actually file such an involuntary petition.[54] Since the assignor is often not paying its debts as they become due pre-assignment, that defense to an involuntary petition is generally not available. One can, of course, examine whether the petitioning creditors are sufficient in number and claim amount and whether any of those claims are disputed as to liability or amount. The most typical response, however, to an involuntary petition is a request that the bankruptcy court abstain in favor of the state law assignment.[55]

Section 305 of the Bankruptcy Code governs abstention and permits a bankruptcy court to dismiss or suspend bankruptcy proceedings if, under the totality of the circumstances, "the interests of creditors and the debtor would be better served."[56] Dismissal or suspension is warranted "'for example, if an arrangement is being worked out by creditors and the debtor out of court, there is no prejudice to the rights of creditors in that arrangement, and an involuntary case has been commenced by a few recalcitrant creditors to provide a basis for future threats to

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[53] *See* Field v. Flanders, 40 Ill. 470 (Ill. 1886) (examining general right of creditors to obtain judgment vacating fraudulent preference of insiders, ensuring that assignment sale treats all creditors equally); *see also* Hexter v. Loughry, 6 Ill. App. 362 (Ill. App. Ct. 1880) (describing process and allowed times for creditors to sue assignee).

[54] *See* Wechsler v. Macke Int'l Trade, Inc. (*In re* Macke Int'l Trade, Inc.), 370 B.R. 236, 252 (B.A.P. 9th Cir. 2007) (noting lower court's finding that involuntary petition "was motivated by the petitioning creditor's desire to find a more sympathetic forum to continue its fight against the debtor"). *But cf.* Canner v. Webster Tapper Co., 168 F. 519, 523 (1st Cir. 1909) ("A creditor who assents in writing to an assignment . . . is ordinarily estopped to allege it as an act of bankruptcy for the purposes of an involuntary petition against the assignor.").

[55] *See In re* Kass, 114 B.R. 308, 309 (Bankr. S.D. Fla. 1990) (noting bankruptcy court can dismiss case if debtor and creditor interests are better served, such as when state remedies for petitioning creditor are adequate); *In re* Beacon Reef Ltd. P'ship, 43 B.R. 644, 646 (Bankr. S.D. Fla. 1984) (holding abstention proper where dispute was primarily between two active remaining partners and state law provided adequate remedies); *see also In re* Win-Sum Sports, Inc., 14 B.R. 389, 394 (Bankr. D. Conn. 1981) (holding in favor of abstention as bankruptcy was being used as alternative to state proceeding merely to resolve intra-company management and stockholder issues).

[56] 11 U.S.C. § 305(a)(1) (2006). *See* Pennino v. Evergreen Presbyterian Ministries (*In re* Pennino), 299 B.R. 536, 538–39 (B.A.P. 8th Cir. 2003) (stating abstention should only be used in extraordinary circumstances, after analyzing specific facts and factors, including: "(1) whether the case is a two-party dispute, (2) the economy and efficiency of administration; (3) the availability of another case or forum to protect the interests of the parties; (4) alternative means of achieving equitable distribution of assets," as well as "(5) the purpose for which bankruptcy jurisdiction has been sought." (citing *In re* Iowa Trust, 135 B.R. 615, 621 (Bankr. N.D. Iowa 1992))); *In re* Trina Assocs., 128 B.R. 858, 866–67 (Bankr. E.D.N.Y. 1991) (stressing particular facts of case must be analyzed in determining dismissal under section 305).

extract full payment.'"[57] While circumstances may differ dramatically, abstention cases fall into typical scenarios, with each scenario governing the outcome of a request for abstention.

A motion to abstain will generally be denied and an order for relief entered if so doing would protect or augment the distribution to unsecured creditors, as well as not prejudice the debtor.[58] However, if either prejudice to the debtor cannot be shown, or there is a lack of evidence concerning the need to protect or the ability to augment the distribution to unsecured creditors, abstention will issue.[59]

Since the pre-assignment business entity which made the assignment still exists, it may also be eligible to file a voluntary bankruptcy petition.[60] In *Automotive Professionals, Inc*., the State of Illinois sought to impose a conservatorship on an entity after an ABC for that entity had been effectuated.[61] After a limbo period, the entity filed a voluntary chapter 11 petition.[62] The state moved to dismiss the case on various grounds, including alleging that the assignor had no power to file a bankruptcy petition post-assignment. In a memorandum opinion, the bankruptcy

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[57] *In re* Kenval Mktg. Corp., 38 B.R. 241, 245 (Bankr. E.D. Pa. 1984) (quoting H.R. REP. No. 95-595, at 325 (1977), *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6281). *See In re* Inv. Corp. of N. Am., 39 B.R. 758, 759 (Bankr. S.D. Fla. 1984) (holding in favor of abstention after considering following factors: (i) filing was by "few disgruntled creditors", (ii) motivation was to obtain control of business, (iii) existence of pending state actions, (iv) out of court arrangements, and (v) promising prospect of viability of debtor's business).

[58] *See In re Kenval Mktg. Corp.*, 38 B.R. at 245 (denying motion to abstain after finding avoidance powers under Bankruptcy Code would augment estate more than parallel state powers would in particular case); *see also In re* Fultz, No. 03-14009, 2004 Bankr. LEXIS 195, at *4–5 (Bankr. N.D. Fla. Feb. 13, 2004) (discussing section 305's allowance of abstention when it benefits creditors and debtors; "in a case where there are potential recoveries, it is clearly not in the best interest of the creditors to dismiss"); *In re* Spade, 258 B.R. 221, 226 (Bankr. D. Colo. 2001):

> Notwithstanding the plain language of the statute, the bankruptcy court formulated its own rule that abstention under § 305 is appropriate: "*only if each and every one of the following factors exist:* 1. The petition was filed by a few recalcitrant creditors and most creditors oppose bankruptcy; 2. There is a state insolvency proceeding or other equitable and concrete out-of-court arrangement pending; and 3. Dismissal or suspension is in the best interests of the debtor and all creditors."

(citing *In re* RAI Mktg. Servs., Inc., 20 B.R. 943, 946 (Bankr. D. Kan. 1982)), *appeal denied sub nom.*, Profutures Special Equity Fund, L.P. v. Spade (*In re* Spade), 269 B.R. 225 (D. Colo. 2001).

[59] *See In re* Bailey's Beauticians Supply Co., 671 F.2d 1063, 1067 (7th Cir. 1982) (affirming bankruptcy court's order of abstention where outside compromise and assignee's work benefited over ninety percent of creditors, and bankruptcy would mandate duplicative work by trustee); *In re* M. Egan Co., 24 B.R. 189, 192 (Bankr. W.D.N.Y. 1982) (granting motion to abstain due to duplication of work, costs, lack of showing of preference, and jurisdictional issues if heard in bankruptcy court); *cf. In re Iowa Trust*, 135 B.R. at 621–22 (discussing various court formulations of factors to consider in deciding abstention issue).

[60] *See*, *e.g.*, *In re* Aero Bulk Mfg. Co., 221 F. Supp. 627, 633 (W.D. Mo. 1963) (discussing specific claims within voluntary bankruptcy filed after attempted ABC).

[61] *In re* Auto. Prof'ls, Inc., 370 B.R. 161, 167 (Bankr. N.D. Ill. 2007) (describing company's distress, ABC, and subsequent order of conservation filed against it by Illinois Director of Insurance, essentially freezing assignee's activities).

[62] *Id*. (noting filing was after Complaint for Rehabilitation filed against API and before issue was resolved).

court rejected this argument and denied the motion to dismiss.[63] The court specifically noted that the term "custodian" as defined in section 101(11) of the Bankruptcy Code includes "assignee under a general assignment for the benefit of the debtor's creditors" and that custodians are subject to turnover actions, thus showing that post-assignment bankruptcy filings were contemplated as a possibility.[64]

Section 543(a) of the Bankruptcy Code requires a custodian, including an assignee pursuant to section 101(11)(B), with knowledge of commencement of a bankruptcy proceeding, to refrain from administering or disbursing property of the debtor's estate. In addition, the assignee is required to: (i) turnover property of the estate as of the date the assignee gains actual knowledge of commencement,[65] and (ii) file an accounting of property of the estate in its possession.[66] The assignee is excepted from all but the accounting requirement if it was appointed or took possession of the assets more than one-hundred and twenty days prior to the petition filing,[67] "unless compliance with such subsections is necessary to prevent fraud or injustice."[68] In addition, the bankruptcy court shall undertake to protect all of the entities to which the assignee has become obligated, provide reasonable compensation for the trustee's services, and surcharge the assignee for improper or excessive disbursements.[69] The last of these requirements is excepted if the assignee was appointed or took possession of the assets more than one-hundred and twenty days prior to the petition filing, or the disbursement was blessed by a pre-petition

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[63] *Id*. at 166 (holding State's arguments lacked merit and that API could file bankruptcy petition "despite the order of conservation issued by state court").

[64] *Id*. at 182 (stating assignment of property pre-petition does not remove property from bankruptcy estate (citing 11 U.S.C. §§ 101(11)(B), 543(b) (2000))); *see* 11 U.S.C. § 101(11)(B) (2006) (defining term "custodian" to include assignees for benefit of creditors); 11 U.S.C. § 543 (2006) (requiring custodian to deliver debtor's property to trustee); Rosenberg v. Friedman (*In re* Carole's Foods, Inc.), 24 B.R. 213, 214 (B.A.P. 1st Cir. 1982) (discussing congressional intent that property transferred in ABC becomes part of bankruptcy estate) (citing H.R. REP. NO. 95-595, at 370 (1977)).

[65] 11 U.S.C. § 543(b) (2006) (mandating custodian turn over property of debtor to trustee "on the date that such custodian acquires knowledge of the commencement of the case").

[66] 11 U.S.C. § 543(b)(2) (2006) (requiring custodian file accounting of property of debtor which came into custodian's control); *see* FED. R. BANKR. P. 6002(a) (requiring custodian who must return property under Bankruptcy Code to also promptly file and transmit to the United States Trustee a report and account of such property); *see also* LAWRENCE W. AHERN, III & NANCY FRAAS MACLEAN, BANKRUPTCY PROCEDURE MANUAL § 6002:01 (2008 ed.) (suggesting Federal Rule of Bankruptcy Procedure 6002(a) merely "implements" section 543(b)(2)'s requirement that custodian returning property file accounting).

[67] 11 U.S.C. § 543(d) (2006). *See*, *e.g.*, *In re* Auto. Prof'ls, Inc., 370 B.R. 161, 182 (Bankr. N.D. Ill. 2007) (requiring turnover where the assignment was within statutory time).

[68] 11 U.S.C. § 543(d). *See In re* Sundance Corp., 83 B.R. 746, 747 (Bankr. D. Mont. 1988) ("[S]ubsection (d) [of section 543] is an abstention policy which permits the custodianship to continue if the best interest of creditors and stockholders is served, or the property has been assigned by the Debtor for the benefit of creditors."); *In re* Colony Press, Inc., 83 B.R. 862, 869, 864 (Bankr. D. Mass 1988) (noting bankruptcy court's discretion in not forcing custodian's turnover if creditors' interests would be served better).

[69] 11 U.S.C. § 543(c) (2006). *See In re* Snergy Props., Inc., 130 B.R. 700, 705 (Bankr. S.D.N.Y. 1991) ("[C]ustodian is entitled to apply to the bankruptcy court pursuant to 11 U.S.C. § 543(c)(2) for reasonable compensation for services rendered and costs and expenses incurred . . . ."); *see also In re* Sevitski, 161 B.R. 847, 855 (Bankr. N.D. Okla. 1993) (scrutinizing excessive fee applications in mismanaged receivership requiring requested administrative expenses to be written-down).

court order. Finally, all of the requirements discussed may be excepted if the debtor's creditors or equityholders, or both, would be better served by the assignee retaining possession.

IX. DISCOVERY AND INVESTIGATION

Unlike bankruptcy, where there is Bankruptcy Rule 2004 discovery for pre-litigation investigation[70] and then discovery under the Federal/Bankruptcy Rules for contested matters and adversary proceedings,[71] there often is no clear right to seek discovery as part of an investigation or otherwise in an ABC.[72] There may also be issues about how much investigation an assignee must or should do and what happens if there is a material cause of action (such as preference, fraudulent transfer, equitable subordination or the like) which could have been brought in a bankruptcy case but which the assignee may or may not have standing to bring.

X. LITIGATION

Assignees also initiate litigation from time to time. There may be challenges to the assignee's standing to do so, especially for actions which are more creditor actions than company actions. The Florida Supreme Court recently upheld an assignee's standing to bring a legal malpractice claim related to a private placement memorandum in the case of *Cowan*,[73] rejecting the argument that the rights were personal to the company and not assignable to the ABC trust. As has been

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[70] *See In re* Dinubilo, 177 B.R. 932, 940 (E.D. Cal. 1993) (stating that Rule 2004 "is generally used as a prelitigation device, during the short time period before a matter becomes contested"); *see also In re* Bakalis, 199 B.R. 443, 447 (Bankr. E.D.N.Y. 1996) (finding scope of Rule 2004 "'unfettered and broad,'" and likening it to "'fishing expedition'" trying to discover assets and unearth frauds (quoting *In re* GHR Energy Corp., 33 B.R. 451, 453 (Bankr. D. Mass. 1983))).

[71] *See In re* Barnes, 365 B.R. 1, 6 (Bankr. D.D.C. 2007) ("Once an adversary proceeding is pending, discovery related thereto must be conducted pursuant to the Federal Rules of Civil Procedure, and Rule 2004, a pre-litigation tool, is displaced."); *see also In re* Bennett Funding Group, Inc., 203 B.R. 24, 28 (Bankr. N.D.N.Y. 1996) (distinguishing between Rule 2004 and narrower provisions for discovery, stating the accepted rule that once a contested matter has commenced, discovery must comply with Federal Rule of Bankruptcy Procedure 7026 as opposed to 2004). *But see In re* Table Talk, Inc., 51 B.R. 143, 145 (Bankr. D. Mass. 1985) ("Bankruptcy Rules 7026 through 7037 apply the Federal Rules of Civil Procedure only in adversary proceedings . . . .").

[72] *See* David S. Kennedy et al., *Professionalism: Dealing with Unprofessional Conduct in Bankruptcy*, 36 U. MEM. L. REV. 575, 616 (2006) ("Rule 2004 is unique to bankruptcy law and procedure, in that it affords few of the procedural safeguards common to other Rules."); *see also* Kupetz, *supra* note 7, at 72 ("Unlike federal bankruptcy proceedings, assignments for the benefit of creditors are governed by state law."); Manuel D. Leal, *Discovery Under Bankruptcy Procedure: A "Trap Door?"*, 84 N.D. L. REV. 111 (2008) (discussing differences between bankruptcy and non-bankruptcy discovery rules, even in the dichotomy where bankruptcy rules are supposedly adopting non-bankruptcy rules).

[73] Cowan Liebowitz & Latman, P.C. v. Kaplan, 902 So. 2d 755, 757 (Fla. 2005) ("[B]ecause lawyers preparing private placement memoranda, like independent auditors, owe a duty to those who rely on statements contained in their published documents, parties may assign claims for legal malpractice committed in preparing them."), *limited to its facts as stated in*, Law Office of David J. Stern, P.A. v. Sec. Nat'l Servicing Corp., 969 So. 2d 962 (Fla. 2007).

happening in bankruptcy cases, the *in pari delicto* defense (with the defendant claiming the pre-assignment assignor entity is to blame or is a wrongdoer at least in part and therefore, cannot recover) may be raised in certain litigation initiated by the assignee.[74]

Some state statutory schemes permit an assignee to bring avoidance actions.[75] However, the Ninth Circuit Court of Appeals has injected some modicum of doubt over an assignee's ability to prosecute those actions with its decision in *Sherwood*.[76] *Sherwood* held that California's preference statute was preempted because the state statute impeded the twin goals of the Bankruptcy Code, namely: fresh start and equitable distribution.[77] To support its holding, the *Sherwood* court relied upon a series of United States Supreme Court decisions—*Stellwagen*,[78] *International Shoe*[79] and *Pobreslo*[80]—which held generally that state statutory discharge provisions are preempted by the Bankruptcy Code.[81] While some commentators describe the *Sherwood* court as misinterpreting the scope of these cases, the court acknowledged their limitation to preemption of discharges[82] and chose to extend their reasoning nonetheless.[83]

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[74] *See* Official Comm. of Unsecured Creditors of PSA, Inc. v. Edwards, 437 F.3d 1145, 1150–52 (11th Cir. 2006) (permitting any *in pari delicto* defenses that would have been available against assignor to be asserted against bankruptcy trustee as assignee of debtor's rights), *cert. denied sub nom.*, Laddin v. Reliance Trust Co., 549 U.S. 811 (2006); Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., 267 F.3d 340, 357 (3d Cir. 2001) (permitting use of *in pari delicto* defense where wrongdoers' conduct is imputed to trustee), *questioned*, *In re* Adelphia Commc'ns Corp., 365 B.R. 24, 50–55 (Bankr. S.D.N.Y. 2007); Terlecky v. Hurd (*In re* Dublin Sec., Inc.), 133 F.3d 377, 380 (6th Cir. 1997) (applying *in pari delicto* defense to dismiss trustee's claims).

[75] *See*, *e.g.*, CAL. CIV. PROC. CODE § 1800(b) (West 2008) (granting assignee power to recover preferences); MINN. STAT. ANN. § 577.07 (West 2009) (granting assignee avoidance powers over fraudulent transfers); WIS. STAT. ANN. § 128.07(c)(2) (West 2007) (granting avoidance power to assignee).

[76] Sherwood Partners, Inc. v. Lycos, Inc., 394 F.3d 1198 (9th Cir. 2005) (holding assignee's attempt to avoid pre-assignment transfer using avoidance powers under California law preempted by the Bankruptcy Code).

[77] *Id*. at 1203–06. *See* Grogan v. Garner, 498 U.S. 279, 286 (1991) (acknowledging fresh start as "central purpose" of Bankruptcy Code); BFP v. Resolution Trust Corp., 511 U.S. 531, 563 (1994) (Souter, J., dissenting) ("[E]quitable distribution for creditors and ensuring a 'fresh start' for individual debtors, [are two policies] which the Court has often said are at the core of federal bankruptcy law.").

[78] Stellwagen v. Clum, 245 U.S. 605 (1918) (holding Ohio insolvency statutory scheme was not preempted by bankruptcy law).

[79] Int'l Shoe Co. v. Pinkus, 278 U.S. 261 (1929) (holding Arkansas insolvency distribution laws were preempted by bankruptcy law).

[80] Pobreslo v. Joseph M. Boyd Co., 287 U.S. 518 (1933) (holding Wisconsin garnishment laws not preempted by bankruptcy law).

[81] *See id.* at 523–24 ("[T]hat part of [Wisconsin law] relating to discharge is entirely superseded by the federal act . . . ." (quoting Hazelwood v. Olinger Bldg. Dep't Stores, Inc. 236 N.W. 591, 592 (Wis. 1931))); *Int'l Shoe Co*., 278 U.S. at 265 ("Congress did not intend to give insolvent debtors seeking discharge . . . choice between the relief provided by the Bankruptcy Act and that specified in state insolvency laws."); *Stellwagen*, 245 U.S. at 615 ("It is settled that a state may not pass an insolvency law which provides for a discharge . . . as to creditors in other states, and this although no general federal bankruptcy act is in effect.").

[82] *See* Sherwood Partners, Inc. v. Lycos, Inc., 394 F.3d 1198, 1203 (9th Cir. 2005) ("We know, because the Supreme Court has repeatedly told us, that state statutes that purport to . . . [give] debtors a discharge of their debts, are preempted."), *criticized by* Ready Fixtures Co. v. Stevens Cabinets, 488 F. Supp. 2d 787, 790

Soon thereafter, two California courts of appeals were presented with the same issue in *Haberbush* and *Credit Managers*,[84] and after finding they were not bound by *Sherwood* and discussing its weaknesses, rejected its reasoning and holding *in toto*.[85] The California Supreme Court denied petitions for review in both cases. While the law in California on this issue is clearly dependent on the forum, *Sherwood* has much greater implications for the country at large. The decision, and its interpretation of *Stellwagen*, *International Shoe* and *Pobreslo*, can be read broadly to preempt any state law that may be interpreted to conflict with the twin goals of the Bankruptcy Code, especially in the area of state law avoidance actions.[86] Every case presented with a similar issue and citing to *Sherwood* has either rejected it outright,[87] or limited its holding.[88]

No clear trend away from the reasoning of *Sherwood* has yet been defined. Undoubtedly, courts will be presented with arguments either to adopt its holding or

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(W.D. Wis. 2007) ("The problems with the *Sherwood* decision are manifold . . . .") *and* Feld, *supra* note 5, at 1452 ("Accordingly, *Sherwood* must be viewed as wrongly decided.").

[83] *See Sherwood Partners, Inc*., 394 F.3d at 1203 ("What goes for state discharge provisions also holds true for state statutes that implicate the federal bankruptcy law's other major goal, namely equitable distribution.").

[84] Credit Managers Ass'n of Cal. v. Countrywide Home Loans, Inc., 50 Cal. Rptr. 3d 259 (Ct. App. 2006) (considering whether federal bankruptcy law preempts California ABC avoidance provisions), *petition for review denied*, No. S148010, 2007 Cal. LEXIS 602 (Cal. Jan. 24, 2007); Haberbush v. Charles & Dorothy Cummins Family Ltd. P'ship, 43 Cal. Rptr. 3d 814 (Ct. App. 2006) (deliberating whether bankruptcy legislation preempts California ABC avoidance laws), *petition for review denied*, No. S144977, 2006 Cal. LEXIS 10482 (Cal. Aug. 30, 2006).

[85] *Credit Managers Ass'n of Cal*., 50 Cal. Rptr. 3d at 266 (holding California ABC avoidance statutes not preempted by federal bankruptcy law); *Haberbush*, 43 Cal. Rptr. 3d at 820 (holding California ABC avoidance law not preempted by bankruptcy law). *But see Sherwood Partners, Inc*., 394 F.3d at 1206 (holding California ABC avoidance statutes preempted by bankruptcy law).

[86] *Sherwood Partners, Inc*., 394 F.3d at 1203 (observing "[t]hat the state discharge statute may be compatible with (or even identical to) the federal discharge statute makes no difference" and "it does not even matter whether a federal bankruptcy act is in effect . . . . Such state procedures are preempted simply because the ability to grant a discharge is 'one of the principal requisites of a true bankruptcy law.'" (quoting Stellwagen v. Clum, 245 U.S. 605, 615–16 (1918))); *see* Burkart v. Coleman (*In re* Tippett), 542 F.3d 684, 689 (9th Cir. 2008) ("In general, '[a]bsent explicit pre-emptive language, . . . field pre-emption [occurs] where the scheme of federal regulation is so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it.'") (quoting Gade v. Nat'l Solid Wastes Mgmt. Ass'n, 505 U.S. 88, 98 (1992)). *But see Sherwood Partners, Inc*., 394 F.3d at 1207 (Nelson, J., dissenting) (conceding state discharge statutes are void, but opining that distribution regulations are not preempted).

[87] *Ready Fixtures Co*., 488 F. Supp. 2d at 792 (rejecting *Sherwood* as "non-binding and unpersuasive circuit court precedent," and holding Wisconsin's preference provisions are not preempted by the Bankruptcy Code); Steven M. Spector, P.C. v. Melee Entm't L.L.C., No. 07C-03-191 PLA, 2008 Del. Super. LEXIS 48 (Del. Super. Ct. Feb. 6, 2008) (agreeing with *Haberbush* and *Credit Managers* that Bankruptcy Code does not preempt California preference statute); APP Liquidating Co. v. Packaging Credit Co., No. 05-C-846, 2006 U.S. Dist. LEXIS 60195, at *8 (E.D. Wis. Aug. 24, 2006) (agreeing with dissent in *Sherwood* "that the arguments to invalidate a preference provision are equally applicable to voluntary assignment laws, generally").

[88] *See*, *e.g.*, Viz Media, L.L.C. v. Steven M. Spector, P.C., No. C07-00660 MJJ, 2007 U.S. Dist. LEXIS 29442 (N.D. Cal. Apr. 10, 2007) (holding *Sherwood* binding on issue of preemption of California preference statute, but not for purposes of subject matter jurisdiction); *cf. In re Tippett*, 542 F.3d 684 (holding California bona fide purchaser statute was not preempted by Bankruptcy Code despite majority's consideration of *Sherwood* preemption analysis).

to expand its reasoning, the latter of which can arguably extend to the preemption of all assignment statutes, despite the fact that assignment and bankruptcy proceedings have harmoniously co-existed for decades. Assignment practitioners, especially those practicing in California, should advise themselves on this issue and remain astutely aware of its development.

XI. CORPORATE ISSUES

While an assignee in many ways effectively functions as a single officer and single member board of directors, he or she does not take those positions for the debtor corporate entity.[89] The original corporate structure remains, although in some instances some of the pre-assignment officers or directors may have resigned. While the corporation they control may now be assetless, there may still be some residual powers and responsibilities, like the power to file a voluntary bankruptcy case or to dissolve, and the responsibility to file tax returns or wind down benefit plans. Generally, these responsibilities remain with the corporation and are not responsibilities of the assignee.

XII. WINDDOWN ISSUES

While most assets are generally either sold or collected (e.g. accounts receivable, tax refunds, etc.) during an ABC, it is possible that certain assets may not be, especially if they have some issue associated with them like a legacy liability (say environmental issues) or enforceable anti-assignment provisions. Occasionally, suits or claims are raised after the assets have been turned to cash and most or all of the money distributed. In a cashless estate, the assignee may not have any funds to pay defense costs and satisfy late arising claims.

CONCLUSION

Anticipating issues such as the ones discussed in this article can make an ABC run much more smoothly. Given the relatively sparse statutory/common law framework in many states, there is also room for flexible and creative solutions to issues in selling or liquidating a business and attendant assets.[90] While there can

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[89] *See* Geoffrey L. Berman, *Common Law Assignments for the Benefit of Creditors: The Reemergence of the Nonbankruptcy Alternative*, 21 CAL. BANKR. J. 357, 357 (1993) (describing assignee as having exclusive control over the marshalling of assets, liquidation, and distribution of proceeds); Cohen & Challacombe, *supra* note 19, at 276 (detailing responsibilities of assignee as paralleling those of single officer/board of directors, including: (i) taking physical control of facilities, equipment and documents, (ii) control of operations—including deciding which employees to keep on—and (iii) oversight and examination of all business practices); John W. Easterbrook, *Bankruptcy Petitions Versus Assignments for the Benefit of Creditors: A "Win" for Bankruptcy?*, 122 BANKING L.J. 415, 415–16 (2005) (describing assignee as solely responsible for company's assets).

[90] *See* Scot Boulton, *How Uniform Will the Uniform Trust Code Be: Vagaries of Missouri Trust Law Versus Desires for Conformity*, 67 MO. L. REV. 361, 377 (2002) (discussing Missouri's relatively liberal

always be unique issues from business to business and state to state, these are some of the more common issues which are encountered in working through the ABC process.

allowance of assignments as a flexibility that can be advantageous); Davis, *supra* note 8, at 18 (describing ABCs as a creative invention to prevent unrestrained creditor race to collect); Kupetz, *supra* note 7, at 73 (extolling ABCs as flexible in nature).