Non-Statutory Insiders Under the Bankruptcy Code After *U.S. Bank National Association v. The Village at Lakeridge, LLC*

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INTRODUCTION

Insiders have motive and means to plunder their firm. They are in a position to enrich themselves at the expense of the firm's creditors. Title 11 of the United Sates Code (the "Bankruptcy Code") therefore singles them out for closer scrutiny and more exacting treatment. Whether an entity is an insider of a firm in bankruptcy is a critical determination under a score of Bankruptcy Code provisions, from how many creditors are needed to file an involuntary petition[1] to whose votes count in determining whether a reorganization plan can be confirmed.[2] Insiders are subject to a longer preference period[3] and to heightened scrutiny for equitable subordination of their claims.[4] Their votes do not count in electing a chapter 7 trustee,[5] and they may not be employed as professionals representing a trustee or chapter 11 debtor in possession.[6]

"Insider" is a defined term in the Bankruptcy Code.[7] The problem is that the definition is not exclusive. It "includes" a list of enumerated persons and entities—

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[1] *See* 11 U.S.C. § 303(b) (2018).
[2] *See id.* § 1129(a)(10).
[3] *See id.* § 547(b)(4)(B).
[4] *See, e.g.*, Pepper v. Litton, 308 U.S. 295, 307–08 (1939) ("[T]hese rules governing the fiduciary responsibilities of directors and stockholders come into play on allowance of their claims in bankruptcy. In the exercise of its equitable jurisdiction the bankruptcy court has the power to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in administration of the bankrupt estate. And its duty so to do is especially clear when the claim seeking allowance accrues to the benefit of an officer, director, or stockholder." (footnote omitted)); Fabricators, Inc. v. Tech. Fabricators, Inc. (*In re* Fabricators, Inc.), 926 F.2d 1458, 1465 (5th Cir. 1991) ("A claim arising from the dealings between a debtor and an insider is to be rigorously scrutinized by the courts. If the claimant is not an insider, then evidence of more egregious conduct such as fraud, spoliation or overreaching is necessary. Accordingly, whether a claimant is an insider of the debtor can be fundamentally important in an equitable subordination case in that it effects the standard of scrutiny a court will apply." (citations omitted)).
[5] *See* 11 U.S.C. § 702(a)(3).
[6] *See id.* § 327(a) ("[T]he trustee . . . may employ one or more . . . professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons. . . ."); *id.* § 101(14) (defining "disinterested person" as "a person that—(A) is not a creditor, an equity security holder, or an insider").
[7] *See id.* § 101(31). Section 101(31) provides:

> The term "insider" includes—
> (A) if the debtor is an individual—
> (i) relative of the debtor or of a general partner of the debtor;
> (ii) partnership in which the debtor is a general partner;
> (iii) general partner of the debtor; or
> (iv) corporation of which the debtor is a director, officer, or person in control;
> (B) if the debtor is a corporation—
> (i) director of the debtor;
> (ii) officer of the debtor;
> (iii) person in control of the debtor;
> (iv) partnership in which the debtor is a general partner;
> (v) general partner of the debtor; or
> (vi) relative of a general partner, director, officer, or person in control of the debtor;

referred to as "statutory insiders."[8] But other, non-enumerated persons and entities may also be insiders—known as "non-statutory insiders."[9]

The federal circuit courts of appeals have been divided on the test for determining non-statutory insider status, as well as the standard for appellate review, with a strong majority applying a two-prong conjunctive test that requires both: (1) a close relationship with the debtor that is comparable to an enumerated insider; and (2) an actual non-arm's-length transaction.[10] Moreover, courts have not articulated a clear and consistent understanding of the concept of insider that could help guide decisions.

The United States Supreme Court stepped into the fray last term in *U.S. Bank National Association v. Village at Lakeridge, LLC*.[11] However, the Court declined to review the conjunctive test employed by the Ninth Circuit, granting certiorari only on the standard of appellate review the Ninth Circuit had applied to the second prong of the test.[12] Then, in a concurring opinion, Justice Sonia Sotomayor and three other justices nevertheless addressed the test for non-statutory insider status and, in doing so, made clear the Court's decision affirming the Ninth Circuit's standard of review was essentially spurious because the second prong of the conjunctive test does not properly exist.[13] Justice Sotomayor's opinion expressed "hope that courts will continue to grapple with the role that an arm's-length inquiry should play in a determination of insider status."[14] In a separate concurring opinion, Justice Anthony Kennedy also highlighted the need for further "elaboration of the principles that underlie non-statutory insider status . . . to ensure uniform and accurate adjudications in this area."[15]

This Article takes up the challenge of developing a coherent and principled approach to determining non-statutory insider status under federal bankruptcy law.

> (C) if the debtor is a partnership—
> (i) general partner in the debtor;
> (ii) relative of a general partner in, general partner of, or person in control of the debtor;
> (iii) partnership in which the debtor is a general partner;
> (iv) general partner of the debtor; or
> (v) person in control of the debtor;
> (D) if the debtor is a municipality, elected official of the debtor or relative of an elected official of the debtor;
> (E) affiliate, or insider of an affiliate as if such affiliate were the debtor; and
> (F) managing agent of the debtor.

Id.

8 *See id.*

9 *See id.* § 102(3) (stating, under the rule of construction, "'includes' and 'including' are not limiting").

10 *See, e.g.*, Anstine v. Carl Zeiss Meditec AG (*In re* U.S. Med., Inc.), 531 F.3d 1272, 1277 (10th Cir. 2008) (holding the inquiry regarding non-statutory insider status is "whether there is a close relationship [between the alleged insider and the debtor] *and* whether there is anything other than closeness to suggest that any transactions were not conducted at arm's length").

11 138 S. Ct. 960 (2018).

12 *Id.* at 965.

13 *Id.* at 970–72 (Sotomayor, J., concurring).

14 *Id.* at 973.

15 *Id.* at 969 (Kennedy, J., concurring).

It makes the case that the conjunctive test is misconceived and that a comparative test is the correct approach to deciding questions of non-statutory insider status. The text of the definition of insider with its enumerated list of statutory insiders and the legislative history of the definition clearly point to a comparative approach. Further, the text and legislative history as well as pre-Code case law and the statutory context of the nearly twenty Bankruptcy Code provisions in which the term is used reveal insider status is reserved for persons and entities with a fiduciary or fiduciary-like relationship with the debtor. This insight indicates a strict test for non-statutory insider status and provides courts with a clear theoretical framework for making the determination in a more consistent manner.

In addition, the Article recounts the story of the lawyering and judging that culminated with the Supreme Court's decision in *Lakeridge*. It is a compelling legal drama in which the debtor's attorneys parlayed the faintest chance of success into a very favorable outcome for their client by having an insider of the debtor transfer its $2,760,000 claim to the romantic partner of one of the debtor's corporate officers for no apparent reason other than he could be trusted to vote for the debtor's chapter 11 plan.[16] It is also a curious and unsatisfying story of how the Supreme Court came to issue an essentially spurious decision while bypassing the fundamental questions of justice for the litigants in the case. Justice Sotomayor's concurring opinion respectfully, but directly, outs the Court for addressing the correct standard of appellate review on a test that does not properly exist.[17] Moreover, the Court also declined to consider whether the bankruptcy court was clearly erroneous in its holding on non-statutory insider status and in its holding that the alleged insider did not vote his claim in good faith.[18] Thus, after affirming use of the clearly erroneous standard of review, it could not address the grave reservations, again expressed by the concurring justices, about the legitimacy of the claim transfer and the basis for the underlying bankruptcy court decision allowing the romantic partner's vote to count for purposes of confirming the debtor's plan.[19]

After first telling the story behind *Lakeridge*, the Article turns to consideration of the correct test for non-statutory insider status. Before concluding, it also briefly considers the proper standard of appellate review on a comparative test for non-statutory insider status.

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[16] *See* Joseph L. Schwartz & Tara J. Schellhorn, *The Appellate Standard of Review in Attempting to Spot an Insider:* Lakeridge *Creates More Questions than Answers*, 37 AM. BANKR. INST. J., May 2018 at 12, 50.

[17] *See Lakeridge* 138 S. Ct., at 969–70 (Sotomayor, J., concurring).

[18] *See id.* at 965–66 (majority opinion).

[19] *See id.* at 972–73 (Sotomayor, J., concurring).

I. THE STORY BEHIND *LAKERIDGE*

A. The Players

The Village at Lakeridge (the "debtor" or "Lakeridge") was an LLC wholly-owned by MBP Equity Partners ("MBP").[20] Lakeridge owned and operated a mixed-use commercial real estate development (retail and office buildings) in an upper-income neighborhood of Reno, Nevada.[21] With a population of about 235,000, Reno bills itself as the "Biggest Little City in the World."[22] The owners of the development, like the bankruptcy judge and the local lawyers in the case, were prominent members of the professional class in the city. The owners had made substantial investments in the development, which is high-end, even luxurious—"over the top," as one of the lawyers described it.[23]

Lakeridge had only two creditors when it filed for bankruptcy: its owner, MBP, which held an unsecured claim for $2,760,000; and U.S. Bank ("USB"), which is based in Minnesota and had acquired its claim, a loan backed by a mortgage on the Lakeridge real estate development, from the original lender through several interim assignments.[24] USB was an under-secured creditor with a secured claim for $10,800,000 and an unsecured claim for at least $6,800,000.[25]

Lakeridge filed for chapter 11 in June 2011, and the case was assigned to Judge Bruce Beesley.[26] This was Lakeridge's second chapter 11 filing. It had previously filed a case in 2006 that was closed in 2008.[27] The first case had been assigned to the other bankruptcy judge that sits in Reno, Judge Gregg Zive.[28] Upon the filing of the second case, USB filed a motion to reassign it to Judge Zive under a local rule requiring related cases to be assigned to the same judge.[29] Judge Beesley denied the motion.[30]

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20 *See id.* at 964 (majority opinion).

21 *In re* The Vill. of Lakeridge, LLC., No. 11-51994 BTB, 2013 WL 1397447, at *1 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC. (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC., 138 S. Ct. 960 (2018).

22 *See* Alicia Barber, *How Did The Biggest Little City Get Its Name?*, KUNR (Aug. 1, 2017), https://www.kunr.org/post/how-did-biggest-little-city-get-its-name#stream/0.

23 *See infra* text accompanying note 24; Telephone Interview with Janet Chubb, Loc. Couns. for USB, currently Of Couns., Kaempfer Crowell (Apr. 22, 2020) (notes on file with author).

24 *See In re* Lakeridge, 814 F.3d at 997; *In re* Lakeridge, 2013 WL 1397447, at *1.

25 *See In re* Lakeridge, 2013 WL 1397447, at *1 ("USB now holds the fully secured claim . . . which amounts to about $10 million. . . ."); Opposition to Motion for Relief from the Automatic Stay to Foreclose on Debtor's Property at 11, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. Aug. 25, 2011), ECF No. 40 (stating Lakeridge scheduled the total claim owed to USB as over $16,000,000).

26 *See* Ex Parte Motion for Reassignment of Case With Certificate of Service at 2, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. June 29, 2011), ECF No. 13.

27 *See id.*

28 *See id.*

29 *See id.* at 1–2.

30 *See* Order on Ex Parte Motion for Reassignment of Case at 1, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. July 6, 2011), ECF No. 15.

Lakeridge was represented by a small Reno firm.[31] There were two lawyers working the case. One was a very experienced lawyer for whom the law offices were named, and the other was a more recent law school graduate who had clerked for Judge Beesley.[32] They were well-versed in how the chapter 11 plan confirmation requirements would shape their single asset real estate ("SARE") client's strategy for confirming a plan—or for delaying the day of reckoning in the hope the property would recover its value. USB was represented by an Am Law 100 firm with offices in Los Angeles as well as by local counsel.[33] Its lawyers were also very reputable and experienced in chapter 11 and SARE cases in particular.

B. The Ground Rules

As a SARE debtor[34] that owed far more to its secured lender than its property was worth, Lakeridge faced a short and narrow path to reorganization in chapter 11. Because SARE cases are essentially two-party disputes between the debtor and a secured lender with a lien on all of the debtor's real estate, the Bankruptcy Code seeks to limit delay and abuse by permitting the secured creditor to foreclose on its mortgage unless the debtor within ninety days of filing the chapter 11 petition submits "a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time."[35] Major hurdles to confirming a plan in a SARE case include the requirement of an accepting impaired class of claims excluding insiders under section 1129(a)(10)[36] and the absolute priority rule.[37]

The absolute priority rule prohibits the pre-bankruptcy owners of a debtor from retaining ownership of the reorganized debtor if a non-accepting class of unsecured claims is not paid in full.[38] However, courts have long assumed there is a "new value exception" that allows the owners to retain ownership by contributing new value to

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[31] *See* Voluntary Petition at 3, The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. June 16, 2011), ECF No. 1 (reflecting Lakeridge was represented by the Law Offices of Alan R. Smith).

[32] *See id.*; *Who We Are: Holly E. Estes,* ESTES LAW PC, https://esteslawpc.com/who-we-are/ (last visited Oct. 25, 2020) (stating Holly E. Estes accepted a clerkship with Judge Beesley prior to beginning her career in private bankruptcy practice).

[33] *See* Stipulation Between Lender and Debtor Resolving Briefing Schedule for Confirmation Hearing at 1, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. July 17, 2012), ECF No. 216 (listing attorneys from Armstrong Teasdale LLP and Venable LLP as attorneys for USB).

[34] *See* 11 U.S.C. § 101(51B) (2018) (defining "single asset real estate").

[35] *Id.* § 362(d)(3). Section 363(d)(3) alternatively provides the stay will not be lifted if the debtor begins making monthly interest payments to the secured creditor at the contract rate of interest on the value of the real estate. As a practical matter, especially when the property is worth a lot less than the secured debt, this is not something the debtor can do with the cash flow from the property. But the import of the provision, which overrules *In re Timbers of Inwood Forest* with respect to SARE cases, is SARE debtors should not be permitted to use bankruptcy to shift the risk of loss in value of the property to the lender, while the debtor delays a foreclosure hoping that the value of the property will increase. *See* 808 F.2d 363, 363–64 (5th Cir. 1987).

[36] *See* 11 U.S.C § 1129(a)(10).

[37] *See id.* § 1129(b)(2)(B) (requiring the senior class of creditors be paid in full before junior classes of creditors and equity holders can receive any money or property under a plan).

[38] *See id.*

the reorganization that is substantial and necessary.[39] In *Bank of America National Trust & Savings Ass'n v. LaSalle St. Partnership*, the Supreme Court held a plan violates the absolute priority rule, if it exists, where pre-bankruptcy owners have the exclusive opportunity to acquire ownership of the reorganized debtor by contributing new value.[40] In other words, the debtor's plan must allow the under-secured lender to bid for the equity interest against the current owners, or the lender is otherwise permitted to submit its own competing plan.[41]

The section 1129(a)(10) requirement often involves a legal dispute over the debtor's classification of unsecured claims.[42] Acceptance of the plan by a class of creditors requires acceptance by more than one-half in number and two-thirds in amount of the claims in the class.[43] In a SARE case, the creditors typically are: (1) the lender, with a secured claim for the value of the property and an unsecured deficiency claim for the balance of its claim; and (2) a group of unsecured trade creditors with relatively small claims for things like utilities, management services, and landscaping.[44] The under-secured lender's deficiency claim invariably is more than large enough to control the outcome of the vote on a plan by a class that includes all unsecured creditors. Even if it is the only creditor to vote against the plan, its claim will comprise far more than one-third of the amount of the claims in the class, thus precluding acceptance if the lender opposes the plan.[45] Most circuit courts,[46] including the Ninth Circuit,[47] have held a debtor may not separately classify the lender's unsecured deficiency claim from the unsecured trade claims for the purpose of satisfying section 1129(a)(10). This prohibition preserves the lender's ability to control whether a plan is accepted by an impaired class of creditors.[48]

Interestingly, Lakeridge did not schedule any unsecured trade claims in the case.[49] This means that it was careful and deliberate in paying off all of these claims

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[39] The supposed exception originated in Supreme Court dicta. *See Case v. L.A. Lumber Prods. Co.*, 308 U.S. 106, 121 (1939) ("[T]his Court stress[ed] the necessity, at times, of seeking new money 'essential to the success of the undertaking' from the old stockholders. Where that necessity exists and the old stockholders make a fresh contribution and receive in return a participation reasonably equivalent to their contribution, no objection can be made." (footnote omitted)).

[40] 526 U.S. 434, 437 (1999).

[41] *See id.* at 456.

[42] *See* 11 U.S.C. § 1129(a)(10) ("The court shall confirm a plan only if all of the following requirements are met . . . (10) If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.").

[43] *Id.* § 1126(c).

[44] *See, e.g.*, Boston Post Rd. LP v. FDIC (*In re* Boston Post Rd. LP), 21 F.3d 477, 479 (2d Cir. 1994).

[45] *See* 11 U.S.C. § 1126(c).

[46] *See, e.g.*, Phx. Mut. Life Ins. Co. v. Greystone III Joint Venture (*In re* Greystone III Joint Venture), 995 F.2d 1274, 1280 (5th Cir. 1991).

[47] *See* Barakat v. Life Ins. Co. of Va. (*In re* Barakat), 99 F.3d 1520, 1529 (9th Cir. 1996).

[48] *See In re* Greystone III, 995 F.2d at 1279 (stating the debtor may not "classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan").

[49] *See In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB, 2013 WL 1397447, at *1 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018).

in full immediately before the filing. Lakeridge's attorneys reportedly have stated their client did not follow their instructions in this matter;[50] the filing could not be delayed—USB was scheduled to foreclose the property on the day after Lakeridge filed its petition.[51] It appears the debtor's management wanted to "do the right thing" by not involving the trade creditors in the bankruptcy. As will be seen, however, the absence of any unsecured creditors other than USB and MBP likely became an important strategic advantage in the case.

The final legal ground rule relevant to the litigation in *Lakeridge* is Bankruptcy Code section 1111(b), which provides that an under-secured creditor may elect to be treated as a fully secured creditor.[52] In making the election, the under-secured creditor must be paid the full amount of its claim,[53] but gives up its unsecured deficiency claim and, with it, control of the class of unsecured claims.[54]

C. The Debtor's Plan and USB's Objections in the Bankruptcy Court and on Appeal

Lakeridge duly filed a chapter 11 plan and disclosure statement within ninety days of filing for bankruptcy.[55] The plan placed claims and the equity ownership interest into four classes: (1) USB's secured claim, which the parties subsequently (and fatefully) stipulated to "be the sum of $10,800,000 for the purposes of plan confirmation;"[56] (2) USB's deficiency claim, which the parties also subsequently (and fatefully) stipulated to be $6,800,000,[57] less adequate protection payments made

[50] Telephone Interview with Louis Bubala III, Loc. Couns. for USB, currently Of Couns., Kaempfer Crowell (Apr. 22, 2020) (notes on file with author).

[51] *See* Motion for Relief from the Automatic Stay to Foreclose on Debtor's Property at 6, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. Aug. 11, 2011), ECF No. 26.

[52] *See* 11 U.S.C. § 1111(b)(2) (2018). This election is not quite as sweet as it sounds. While the electing under-secured creditor must be paid a number of dollars equal to the amount of its claim, the payments may be paid out over a period of time such that the present value of the stream of payments is no more than the present value of the property. *See id.* § 1129(a)(7)(B), (a)(9)(C). An under-secured creditor normally makes the election when it believes the value of its collateral will increase.

[53] *Id.* § 1129(b)(2)(A).

[54] *See* 128 Inc., W. Edge II, Inc. v. Premium Mortg., Inc., No. 8:16-CV-32-T-17, 2016 WL 4402824, at *4 (M.D. Fla. Aug. 16, 2016) (establishing when an under-secured creditor makes an election under section 1111(b)(2) of the Bankruptcy Code, it "gives up any distribution it may have been entitled to receive on account of its unsecured claim, and gives up its right to vote on the plan as an unsecured creditor").

[55] *See In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB, 2013 WL 1397447, at *1 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018) (stating Lakeridge filed the chapter 11 petition on June 16, 2011 and filed its disclosure statement and plan on September 13, 2011).

[56] Stipulation as to Value of Property at Plan Confirmation at 1, *In re* Lakeridge, No. 11-51994-BTB (Jan. 12, 2012), ECF No. 108.

[57] *See* Debtor's Second Amended Plan of Reorganization at 14–15, *In re* Lakeridge, No. 11-51994-BTB (Nov. 13, 2018), ECF No. 544 (stating the parties stipulated that the value of the property was $10,800,000 and that the allowed amount of USB's claim was $17,600,000 less all additional post-petition pre-confirmation payments to USB). USB filed a proof of claim for $21,860,000. *See* Response to Objection to Claim of U.S. Bank at 2–3, *In re* Lakeridge, No. 11-51994-BTB (Jan. 13, 2012), ECF No. 110. Thus, it stipulated to a claim that was $4,260,000 less than what it claimed it was owed for purposes of confirmation.

during the case, again for the purpose of plan confirmation; (3) the unsecured claims of MBP and of tenants for security deposits; and (4) MBP's ownership interest.[58] The plan impaired all classes except Class 4—the equity interest holder.[59]

This plan, as all of the lawyers and the judge alike would have recognized, had no chance of being confirmed and was all but dead on arrival. Designating the tenant security deposit claims as impaired claims was clearly impermissible because the plan proposed to assume all of the debtor's leases[60] (a critical necessity) and, therefore, the tenants' rights under those leases would not be impaired. The same Ninth Circuit decision that prohibits separately classifying a lender's unsecured deficiency claim and unsecured trade claims for purposes of obtaining an accepting impaired class, also squarely held the claims of tenants whose leases are being assumed are not impaired claims.[61]

Because MBP was an insider,[62] its acceptance could not satisfy section 1129(a)(10).[63] With USB opposed to the plan, there was no possibility of meeting the impaired accepting class requirement—unless, as the Supreme Court would later put it, "MBP could transfer its claim against Lakeridge to a non-insider who would then agree to the reorganization plan."[64] And while the section 1129(a)(10) problem would have appeared insurmountable, the plan had other major defects: it improperly placed USB's unsecured deficiency claim in a different class than MBP's unsecured claim; it violated the absolute priority rule by giving MBP continued ownership of the reorganized debtor without giving USB the opportunity to bid for it; and it was almost certainly not feasible in that it proposed to pay USB's secured claim by selling or refinancing the property at some time in the future.[65] The entire plan was premised on the hope that the value of the property would appreciate sufficiently to pay all claims in full, and it provided for negative amortization of interest on USB's secured claim.[66] It appeared section 1129(a)(10) would be the immediate cause of death, but there were other fatal conditions.

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[58] Debtor's Plan of Reorganization at 5–9, *In re* Lakeridge, No. 11-51994-BTB (Sept. 14, 2011), ECF No. 48.

[59] *Id.* at 5; Debtor's Disclosure Statement at 13, *In re* Lakeridge, No. 11-51994-BTB (Sept. 14, 2011), ECF No. 47.

[60] *See* Debtor's Plan of Reorganization, *supra* note 58, at 9–10; *In re* Lakeridge, 2013 WL 1397447, at *13 n.4.

[61] Barakat v. The Life Ins. Co. of Va. (*In re* Barakat), 99 F.3d 1520, 1528 (9th Cir. 1996).

[62] U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 964 (2018). The Supreme Court noted MBP was an insider because it was an entity in control of the debtor. *Id.* In addition, it was an insider by virtue of being an affiliate of the debtor. *See* 11 U.S.C. § 101(31)(E) (2018) ("'[I]nsider' includes . . . affiliate or insider of an affiliate as if such affiliate were the debtor. . . ."); *see also id.* § 101(2)(A) ("'[A]ffiliate' means . . . [an] entity that . . . owns . . . 20 percent or more of the outstanding voting securities of the debtor. . . .").

[63] *See* 11 U.S.C § 1129(a)(10).

[64] *Lakeridge*, 138 S. Ct. at 964.

[65] *See* Objection to Confirmation of Debtor's Plan of Reorganization at 3–16, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. July 19, 2012), ECF No. 222.

[66] *See* Debtor's Plan of Reorganization, *supra* note 58, at 8–9. The very point of the special SARE provision in section 362(d)(3) is to pull the plug on a case that is filed for the purpose of delaying foreclosure on the hope the value of the property will increase while the lender assumes the entire risk of decrease. Thus, section

This is where the plot thickens. The bankruptcy court scheduled a hearing on the disclosure statement for Monday, November 7, 2011.[67] Two weeks before the hearing, and six weeks after filing its plan, MBP assigned its $2,760,000 dollar claim to one Robert Rabkin for $5000.[68]

The point person for the debtor in the bankruptcy proceedings was Kathleen Bartlett, who was both an officer of the debtor and a member of MBP's board.[69] The relationship between Bartlett and Rabkin and the circumstances of the assignment of MPB's claim lie at the heart of the *Lakeridge* case. Bartlett and Rabkin were in a long-term romantic relationship.[70] Bartlett approached Rabkin with an offer to sell him MBP's $2,760,000 claim for $5000.[71] There was no negotiation over the price, nor did MPB offer to sell the claim to any other potential purchasers that might have paid more for the claim.[72] Rabkin knew little about Lakeridge or MBP when he purchased the claim. However, he did not do any due diligence before or after he purchased the claim, explaining the amount he was paying did not justify the time and expense.[73] He testified he made the purchase as an investment, not as a favor to Bartlett, and that he saw the investment as risky.[74] Rabkin testified he did not know at the time he purchased the claim that the debtor's plan provided for a payment of $30,000 on the claim.[75] He later rejected an offer by USB to purchase the claim from him for $60,000.[76]

The debtor filed notice of MBP's assignment to Rabkin about a week after it occurred, on the Friday before the Monday hearing on the disclosure statement.[77] "It does not appear that the assignment was discussed at the hearing;"[78] counsel for USB apparently was not yet aware of the transaction (or that the debtor would abandon its classification of tenants as unsecured creditors with impaired claims for their security

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362(d)(3) precludes relief from the automatic stay where the debtor makes monthly interest payments to the lender at the contract rate on the value of the property, thereby compensating the lender for the lost opportunity costs resulting from the automatic stay. *See* 11 U.S.C. § 362(d)(3).

67 Hearing Scheduled/Rescheduled, *In re* Lakeridge, No. 11-51994-BTB (Oct. 24, 2011), ECF No. 70.

68 *See* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993, 997 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018).

69 *Lakeridge*, 138 S. Ct. at 964.

70 *Id.*

71 *Id.*

72 *See In re* Lakeridge, 814 F.3d at 1004 (Clifton, J., concurring in part and dissenting in part) ("MBP did not offer the interest to anyone else. . . . There was no evidence of any negotiation over price—Rabkin didn't offer less, and MBP didn't ask for more.").

73 *Id.* at 1003 (majority opinion).

74 *Id.*

75 *Id.* at 997.

76 *Id.*

77 *See* Notice of Assignment of Claim at 1, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. Nov. 4, 2011), ECF No. 78. From the docket, it appears the notice was filed but not served on anyone.

78 *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB, 2013 WL 1397447, at *1 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018).

deposits). USB may not have seen such an assignment as a viable or likely scenario. Although the strategy was not unprecedented,[79] it is far from common and does not appear to have actually been successful in any reported case.[80] They may have speculated some previously overlooked creditor would surface.[81]

USB made the section 1111(b) election at the court hearing on the disclosure statement.[82] Whether or not the debtor concealed the transfer of MBP's claim in order to increase the likelihood USB would make the election, the election greatly enhanced Lakeridge's odds of getting a plan confirmed using Rabkin's vote to satisfy section 1129(a)(10). If USB had known of MBP's assignment to Rabkin, perhaps it would have made a different decision. As noted above, an electing under-secured creditor gives up its unsecured deficiency claim and its right to vote in the unsecured class.[83] Thus, USB left MBP as the only unsecured creditor in the case. If both USB's unsecured deficiency claim and MBP's unsecured claim had been placed in the same class as required by Ninth Circuit precedent,[84] USB's vote against the plan would have assured the plan would not be confirmed for lack of an accepting impaired class, regardless of whether MBP's acceptance was excluded. USB, apparently unaware of the transfer to Rabkin, may have figured, because MBP was indisputably a statutory insider, it could make the debtor's path to confirmation even more complicated by making the section 1111(b) election. It could require Lakeridge's plan to provide for payment in full of its claim without really giving anything up—acceptance by MPB would have been excluded and there was nothing to be gained by outvoting it.

This is where having no other unsecured creditors also became a strategic advantage for Lakeridge. A tactic often employed by secured creditors in SARE cases, such as USB, is to purchase the pre-petition unsecured trade claims, and

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[79] *See In re* Concord Square Apartments, 174 B.R. 71, 75 (Bankr. S.D. Ohio 1994) (denying secured lender's motion for relief from stay in a SARE case where insiders were considering assigning their claims and the status of the future assignees could not be evaluated until the assignments were made); *In re* Hempstead Realty Assocs., 38 B.R. 287, 290 (Bankr. S.D.N.Y. 1984) (suggesting a debtor's inability to obtain acceptance of a plan pursuant to section 1129(a)(10) might be remedied by assigning a claim from an insider to a non-insider).

[80] *See In re* Heights Ban Corp., 89 B.R. 795, 798–99 (Bankr. S.D. Iowa 1988); *see also In re* Three Flint Hill LP, 213 B.R. 292, 300–01 (D. Md. 1997) (holding an individual who purchased claims from the debtor's trade creditors at the behest of the debtor was a non-statutory insider whose votes in favor of debtor's plan had to be excluded under section 1129(a)(10)). *Cf. In re* Marble Cliff Crossing Apartments, LLC, 485 B.R. 849, 853–54 (Bankr. S.D. Ohio 2013) (holding individuals who purchased claims at the behest of the debtor were not non-statutory insiders and their votes should not be designated under section 1126(e) where the purchasers had interest in obtaining business from the debtor in the future).

[81] The debtor may have hinted at this very early in the case when, in its response to the motion for relief from stay that USB filed several weeks before Lakeridge filed its plan, it stated "[t]he debtor anticipates it will have an accepting impaired class of unsecured creditors, thus satisfying 11 U.S.C. § 1129(a)(10)." Opposition to Motion for Relief from the Automatic Stay to Foreclose on Debtor's Property, *supra* note 25, at 8. But perhaps this more immediately referred to the tenants with security deposit claims, discussed above, or to the assignment of MBP's claim to Rabkin.

[82] Transcript of Hearing Held on Nov. 7, 2011 at 74–75, *In re* Lakeridge, No. 11-51994-BTB, (Feb. 28, 2012), ECF No. 128. Federal Rule of Bankruptcy Procedure 3014 states, "[a]n election of application of § 1111(b)(2) of the Code by a class of creditors in a chapter 9 or 11 case may be made at any time prior to the conclusion of the hearing on the disclosure statement. . . ." FED. R. BANKR. P. 3014.

[83] *See supra* notes 52–54 and accompanying text.

[84] *See* Barakat v. The Life Ins. Co. of Va. (*In re* Barakat), 99 F.3d 1520, 1528 (9th Cir. 1996).

thereby assure rejection of the plan by the unsecured class. Recall that even if creditors holding more than two-thirds of the claims in a class vote to accept the plan, it will be rejected if more than one-half in the number of claims in the class are voted against the plan.[85] Once USB took the section 1111(b) election, leaving MBP as the only unsecured creditor in the case, the absence of other unsecured creditors deprived USB of the possibility of purchasing those claims and thereby controlling the vote of an unsecured class that included both Rabkin's claim and the unsecured trade claims.

As noted above, USB did seek to purchase MBP's claim from Rabkin. USB's counsel offered Rabkin $50,000 for the claim during a deposition of Rabkin concerning his relationship with Lakeridge, MBP, and Kathleen Bartlett, just as it would have offered to purchase the claims of trade creditors if there had been any.[86] Rabkin said he would consider it.[87] "[I]n an attempt to compel an immediate answer," USB "increased its offer to $60,000," which Rabkin, again, declined to accept on the spot.[88]

Remarkably, USB's offer completely backfired on it. Judge Beesley would later call it "appalling" and apologize to Rabkin "on behalf of the legal profession,"[89] although the offer would have given Rabkin an immediate 1200% return on his "investment."

After an evidentiary hearing at which Bartlett and Rabkin testified, Judge Beesley held, as a matter of law, Rabkin inherited MBP's insider status and, therefore, was a

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[85] 11 U.S.C. § 1126(a) (2018).

[86] *See In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB, 2013 WL 1397447, at *2 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018).

[87] *In re* Lakeridge, 814 F.3d at 997.

[88] *Id.* In the deposition, Rabkin testified he had purchased MBP's claim as a speculative investment, not as a favor to Bartlett, and that he had not known prior to the deposition that his payout under Lakeridge's plan was to be $30,000. *Id.* There seems to be a bit of a discrepancy on this point. The Ninth Circuit's recitation of the facts says Rabkin did not know before the deposition that his payout under the plan was to be $30,000, whereas the Bankruptcy Appellate Panel's opinion says Rabkin purchased the claim as a business investment and expected to be paid a pro rata dividend of $30,000 under the plan. *Compare id.*, *with In re* Lakeridge, 2013 WL 1397447, at *1. In a separate affidavit, Rabkin expressed another reason for purchasing the claim: a desire to keep the business in local hands. *See* Declaration of Robert Rabkin in Support of Debtor's Opposition to U.S. Bank's Motion at 2, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. July 13, 2012), ECF No. 214. On the advice of his lawyer, Rabkin declined to answer questions about what was discussed at a meeting he attended shortly before the deposition with his attorney and counsel for Lakeridge. *See In re* Lakeridge, 2013 WL 1397447, at *1. The bankruptcy court denied USB's motion to compel based on the common interest privilege. *See id.* at *12. USB appealed this ruling, too. *See id.* at *1. The Bankruptcy Appellate Panel remanded the issue for a finding on whether the parties had an agreement to pursue a joint strategy, noting:

> Lakeridge and Rabkin shared a common interest in that they both wanted to obtain confirmation of the plan of reorganization, Lakeridge as the debtor and plan proponent, and Rabkin for his financial interests. As a result, while they had separate counsel, they were engaged in furtherance of a common legal enterprise.

Id. at *12.

[89] *Id.* at *10.

statutory insider whose acceptance of the debtor's plan had to be excluded.[90] He may have been prepared to rule in favor of Lakeridge on this issue, but Judge Zive had just held the purchaser of a claim from an insider is automatically an insider, a transcript of which USB's attorneys urgently submitted in the *Lakeridge* case.[91] This apparent setback for the debtor would prove to be a blessing in disguise.

No further determinations were necessary, but the bankruptcy court went on to conclude Rabkin was not a non-statutory insider and he did not vote his claim in bad faith.[92] These were mixed questions of law and fact. On the latter issue, the court explained Rabkin was not compelled to accept USB's offer to purchase the claim, the purchase was a legitimate investment, and Bartlett had not asked him to vote for the plan.[93] In concluding Rabkin was not a non-statutory insider, the bankruptcy court explained Rabkin did not exercise control over Lakeridge, cohabit with Bartlett, pay her bills or living expenses, and had never purchased expensive gifts for her.[94]

The debtor appealed the purely legal question, and USB cross-appealed on the other two mixed questions of law and fact to the Ninth Circuit Bankruptcy Appellate Panel ("BAP").[95] In a not-for-publication opinion, the BAP brusquely dispatched the bankruptcy court's legal conclusion that Rabkin automatically acquired MBP's insider status with his purchase of the claim, stating the ruling was both unsupported by the very cases it purported to rely on and conflicted with multiple published decisions by the panel.[96] Applying a clearly erroneous standard of review, the BAP affirmed the bankruptcy court's holding that Rabkin was not a non-statutory insider.[97] It also

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90 *Id.* at *2.

91 *See* Amended Request for Judicial Notice in Support of Objection to Confirmation of Debtor's Plan of Reorganization at 2–3, *In re* Lakeridge, No. 11-51994-BTB (July 19, 2012), ECF No. 227; Notice of Supplemental Authority Regarding U.S. Bank's Motion to (A) Designate Claim Of Robert Rabkin as an Insider Claim or (B) Disallow Such Claim For Voting Purposes Pursuant to 11 U.S.C. §§ 1126(e), 1129(a) and 105(a) at 2, *In re* Lakeridge, No. 11-51994-BTB (July 23, 2012), ECF No. 228.

92 *In re* Lakeridge, 2013 WL 1397447, at *2–3. USB had also filed a motion to disallow Rabkin's claim for voting purposes, arguing "Debtor's representative is making a mockery of the Chapter 11 process by attempting to confirm a plan by selling MBP's insider claim to her boyfriend and calling it an impaired accepting class." U.S. Bank's Motion to (A) Designate Claim Of Robert Rabkin as an Insider Claim or (B) Disallow Such Claim For Voting Purposes Pursuant to 11 U.S.C. §§ 1126(e), 1129(a) and 105(a) at 7, *In re* Lakeridge, No. 11-51994-BTB (July 1, 2012), ECF No. 194. In a similar vein, USB wrote in its Objection to Confirmation, "[t]he plan requires this Court to make findings of fact and reach conclusions of law that turn the bankruptcy process on its head." Objection to Confirmation of Debtor's Plan of Reorganization, *supra* note 65, at 2.

93 *In re* Lakeridge, 2013 WL 1397447, at *3, *10.

94 *Id.* at *2.

95 *See id.* at *3.

96 *Id.* at *7 ("The bankruptcy court's conclusion is not supported in the case law it cited for the proposition and, indeed, it is inconsistent with the Panel's published decisions. The Panel has on multiple occasions explained that 'insider determination . . . is made on a case-by-case basis, after the consideration of various factors.'"). *See also In re* Caviata Attached Homes, LLC, No. BK-09-52786, 2010 WL 8500043, at *2 (Bankr. D. Nev. 2010). Although this is patently correct, *see supra* notes 7–10 and accompanying text, USB sought review of the decision at both the Ninth Circuit and the Supreme Court. The Ninth Circuit affirmed the BAP, and the Supreme Court denied certiorari on the question. *See* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993, 1003 (9th Cir. 2016); U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 965 (2018).

97 *In re* Lakeridge, 2013 WL 1397447, at *6–7.

affirmed the bankruptcy court's ruling that Rabkin had not voted his claim in bad faith.[98]

Lakeridge's next turn of good fortune was USB's decision to appeal the BAP ruling to the Ninth Circuit—it took the Ninth Circuit nearly three years to decide the appeal.[99] In a series of agreed cash collateral orders while the appeals were pending, the debtor continued to operate the business, paying to USB only its net income.[100] Instead, USB could have returned to the bankruptcy court and litigated its other objections to confirmation. As noted above, the treatment of USB's secured claim was a major problem for Lakeridge. In addition, USB might have changed its section 1111(b) election, giving it control of the unsecured class and depriving Lakeridge of any impaired accepting class even with Rabkin entitled to vote on the plan. Perhaps it felt it could not get a fair shake in the bankruptcy court.

At the oral argument before the Ninth Circuit panel, it appeared that two of the three judges were prepared to hold the bankruptcy court was clearly erroneous on the non-statutory insider question. However, the panel ultimately affirmed the BAP with one judge dissenting.[101] The majority adopted the conjunctive test and applied a clearly erroneous standard of review, first, to whether the relationship between Rabkin and the debtor was comparable to that of a statutory insider and, second, to whether the transaction between Rabkin and MBP was conducted at arm's length.[102] Dissenting, Judge Richard Clifton would have used a *de novo* standard of review, but in any event thought the bankruptcy court had clearly erred in its holding that Rabkin was not an insider.[103] The "facts make it clear that this transaction was negotiated at less than arm's length," he wrote, "I don't have to know the precise details of the relationship between Rabkin and Bartlett to conclude that it offers the only logical explanation for Rabkin's actions here. He did a favor for a friend, and if it made some money for himself, so much the better."[104] In a separate opinion, the Ninth Circuit panel unanimously affirmed the holding that Rabkin did not vote his claim in bad faith.[105]

Again, USB might have chosen to return to the bankruptcy court and litigate its other objections to confirmation. Instead, it sought review by the Supreme Court. There was ample reason to feel it had not received justice in the case so far, a sense that was validated by Judge Clifton's dissent.

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[98] *Id.* at *10.

[99] *See In re* Lakeridge, 814 F.3d at 998.

[100] *See* Status Report Re Status of: (A) Ninth Circuit Appeal; and (B) Continued Hearings on: (1) U.S. Bank's Motion for Relief from the Automatic Stay to Foreclose on Debtor's Property; and (2) Motion for Authority to Use Cash Collateral at 3–4, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. Nov. 25, 2015), ECF No. 400 ("[T]he Cash Collateral Order . . . requires the Debtor to pay to U.S. Bank the net monthly operating income for the preceding month.").

[101] *In re* Lakeridge, 814 F.3d at 1003.

[102] *See id.* at 1001–03.

[103] *Id.* at 1006 (Clifton, J., concurring in part and dissenting in part).

[104] *Id.* at 1004–05.

[105] U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 634 F. App'x 619, 620 (9th Cir. 2016) (mem.).

The Supreme Court, short one justice because Justice Neil Gorsuch had not yet been confirmed to replace Justice Antonin Scalia, mustered the votes to grant certiorari on the standard of appellate review, but not on the test for non-statutory insider status.[106] Justice Gorsuch would join Justice Sotomayor's concurring opinion addressing the test for non-statutory insider status, suggesting if he had been on the Court at the time certiorari was considered, he would have been an additional vote in favor of granting certiorari on that question.[107] The Court also denied certiorari on the other issues in the case—whether Rabkin had voted his claim in bad faith, whether he became an insider by virtue of purchasing the claim from an insider, and whether the bankruptcy court was clearly erroneous in holding Rabkin was not an insider.[108]

D. The Supreme Court's Odd Predicament

At the oral argument, it quickly became apparent the Court had created an awkward predicament for itself by denying certiorari on the test for non-statutory insider status while granting certiorari on the standard for appellate review on that question. And it surfaced repeatedly. Justices Sotomayor, Gorsuch, Samuel Alito, John Roberts, and Elena Kagan each noted the predicament at least once at various points over the course of the petitioner's, respondent's, and government's arguments.[109] Justice Gorsuch made the point most cogently in an exchange with USB's counsel (Mr. Geyser):

> JUSTICE GORSUCH: Can we [decide what the right standard of review is] when we don't know what the right legal test is? And -- and don't we run the risk, perhaps, of sending the wrong signal to lower courts that we're adopting . . . the Ninth Circuit's formulation of what the test is?
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> MR. GEYSER: Well, Your Honor, I -- I think a couple of different points to that. The first is there is some degree of difficulty of

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[106] *See* U.S. Bank N.A. *ex rel*. CWCapital Asset Mgmt. LLC v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 965 (2018).

[107] *See id.* at 970 (Sotomayor, J., concurring).

[108] *See id.* at 965. As mentioned *supra*, in concluding Rabkin did not vote his claim in bad faith, the bankruptcy court stated Bartlett did not ask Rabkin to vote for the plan. *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB, 2013 WL 1397447, at *3 (B.A.P. 9th Cir. Apr. 5, 2013), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018). This finding is naïve at best. Once Rabkin purchased the claim, it would be worthless if he did not vote it in favor of the plan. Moreover, Rabkin's lawyer instructed him not to answer questions in his deposition concerning a meeting he had with Lakeridge's attorney on grounds of the common interest privilege. *Id.* at *1. The bankruptcy court refused to compel Rabkin to testify based on the privilege. *Id.* at *11. The common interest: confirmation of the debtor's plan!

[109] *See* Transcript of Oral Argument at 6, 14, 40–41, 64–65, *Lakeridge*, 138 S. Ct. 960 (No. 15-1509).

> measuring between two points without knowing what one of the points is, but --
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> JUSTICE GORSUCH: This seems to me a high degree of difficulty. It's like one of those high dives, you know, it's a -- it's a 10 out of 10 difficulty.[110]

After a discussion of different circuit court approaches to non-statutory insider status, USB's counsel delivered the oral argument's best line in response to a question from Justice Gorsuch, and then Chief Justice Roberts charted the Court's way forward:

> JUSTICE GORSUCH: Should we wait to see what the courts of appeals sort out on all this before we decide what the standard of review is?
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> MR. GEYSER: Your Honor, if the Court would like to dismiss the case as improvidently granted, we'll take a win any way we can get it.
>
> (Laughter.)
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> . . .
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> CHIEF JUSTICE ROBERTS: I suppose that we could articulate what the right answer is based on a particular understanding of the test, and I gather there's little dispute about that.
>
> We certainly can determine exactly what we're looking at and then make it clear and send it back.[111]

Thus, the Court never addressed USB's fundamental grievance. Here again, the concurring justices pointed to the potential injustice. Both Justice Sotomayor in her concurring opinion joined by Justices Kennedy, Thomas, and Gorsuch, and Justice Kennedy in a separate concurring opinion, expressed concerns about the soundness of the bankruptcy court's holdings that Rabkin was not an insider and did not vote his claim in bad faith.[112] Both cited Judge Clifton's dissenting opinion in the Ninth Circuit appeal.[113] Justice Sotomayor thought Rabkin may have improperly agreed to vote for Lakeridge's plan in return for obtaining the claim from MPB.[114] She found it:

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[110] *Id.* at 41.
[111] *Id.* at 45–46.
[112] *See Lakeridge*, 138 S. Ct. at 969–70 (2018) (Sotomayor, J., concurring); *id.* at 696 (Kennedy, J., concurring).
[113] *Id.* at 972 (Sotomayor, J., concurring); *id.* at 969 (Kennedy, J., concurring).
[114] *See id.* at 972 n.2 (Sotomayor, J., concurring).

> [T]roubl[ing] . . . that neither the Bankruptcy Court nor the Ninth Circuit considered whether Rabkin's purchase of MBP's claim for $5000 was for value. . . . Indeed, we have no concrete information about what benefit MBP received from the transaction aside from the prospect of Rabkin's vote in the cramdown.[115]

Justice Kennedy questioned whether the bankruptcy court was clearly erroneous in its holding that Rabkin was not a non-statutory insider, emphasizing that question was not before the Court and, therefore, the Court's holding should not be read to suggest otherwise.[116]

E. The Settlement After Remand

The Supreme Court issued its decision two years after USB filed its writ of certiorari. When the case finally returned to the bankruptcy court more than six years after Judge Beesley had denied confirmation of the debtor's plan on the ground that Rabkin was an insider because he acquired his claim from an insider, Lakeridge's property had appreciated by about $7,000,000.[117] Lakeridge sold the property pursuant to a settlement agreement with USB in December 2018 for $17,600,000.[118] Although the proceeds were not enough to pay USB in full, it conceded nearly $2,000,000 of the sale's proceeds to the debtor.[119] Why?

Recall that in 2012 USB and Lakeridge had stipulated that the value of the property was $10,800,000 and that the total amount of USB's claim was $17,600,000 less adequate protection payments, both "for the purposes of plan confirmation."[120] Lakeridge insisted USB was still bound by these stipulations over six years later,[121] which would have meant USB was entitled to receive only about $11,500,000 on its claim. USB countered that the stipulations were no longer binding because the bankruptcy court had denied confirmation of the plan (which had been reversed on appeal) and that the valuation was stale.[122] If the stipulations were no longer binding, USB would now be an over-secured creditor with the right to post-petition interest

115 *Id.*

116 *Id.* at 969 (Kennedy, J., concurring).

117 *Compare* Stipulation as to Value of Property at Plan Confirmation, *supra* note 56, at 1 (stating the value of the property was $10,800,000), *with* Order Approving Motion to Approve Sale of Property Free and Clear of Liens, Claims and Encumbrances; to Approve Assumption and Assignment of Certain Contract and Leases; and Granting Related Relief at 3, *In re* The Vill. at Lakeridge, LLC, No. 11-51994-BTB (Bankr. D. Nev. Dec. 4, 2018), ECF No. 552 (stating the purchase price of the property was $17,900,000).

118 *See* Order Approving Motion to Approve Sale of Property Free and Clear of Liens, Claims and Encumbrances; to Approve Assumption and Assignment of Certain Contracts and Leases; and Granting Related Relief, *supra* note 117, at 3.

119 *See id.* at 4.

120 Stipulation as to Value of Property at Plan Confirmation, *supra* note 56, at 1.

121 *See* Motion for Order Approving Compromise and Settlement Agreement at 5, *In re* Lakeridge, No. 11-51994-BTB (Oct. 19, 2018), ECF No. 508 ("Debtor asserts that the 2012 Stipulations are still binding on U.S. Bank. . . .").

122 *See id.* at 4.

and attorneys' fees as part of its claim. USB also contended it was entitled to the appreciation in the value of the property as a result of its section 1111(b) election.[123] In a status conference, Judge Beesley requested the parties go to mediation.[124]

In mediation, USB agreed to payment of half of the net proceeds of sale in excess of $12,600,000 (and a $50,000 carve-out for debtor's counsel[125]) to Lakeridge.[126] The sale proceeds yielded about $2,200,000 to MBP under the agreed formula.[127] The settlement provided Rabkin would receive $200,000 for his claim, to be paid by Lakeridge.[128] This was a whopping forty times what he paid for the claim, yet a bargain for MBP, which would have lost ownership of the development without Dr. Rabkin's $5000 "investment."

II. THE LEGISLATIVE HISTORY OF THE BANKRUPTCY CODE DEFINITION OF "INSIDER"

Turning now to the test for non-statutory insider status, the origins of the Bankruptcy Code's definition of "insider" are something of a mystery.[129] The term was introduced with the enactment of the Bankruptcy Code in 1978.[130] It was not a defined term under the former Bankruptcy Act. Moreover, the most significant Bankruptcy Code provisions that use the term, including the insider preference provision[131] and the chapter 11 plan confirmation requirement of at least one impaired accepting class excluding insiders,[132] have no antecedents in the Bankruptcy Act.[133]

The legislative history of the definition is brief but informative. Both the House and Senate Judiciary Committee Reports identically state: "An insider is one who has a sufficiently close relationship with the debtor that his conduct is made subject to

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123 *See id.* at 6.

124 *See id.*

125 Debtor's Second Amended Plan of Reorganization, *supra* note 57, at 25–26. The total tab for debtor's attorneys' fees in the case was over $450,000.

126 *Id.* at 26.

127 *See id.* at 26–27.

128 *See* Findings of Fact, Conclusions of Law and Order Approving Debtor's Motion For Order Approving Compromise and Settlement Agreement at 26, *In re* Lakeridge, No. 11-51994-BTB (Nov. 26, 2018), ECF No. 548.

129 Several commentators writing shortly after the enactment of the Bankruptcy Code in 1978 suggested, without any supporting legal citation, the concept of insider was derived from Securities law. *See* John Tuskey, Note, *Term Insider within Section 547(b)(4)(B) of the Bankruptcy Code*, 57 NOTRE DAME LAW. 726, 731 (1982) ("Congress intended the same broad concept of control found in the securities law."); Walter Ray Phillips, *Insider Provisions of the New Bankruptcy Code*, 55 AM. BANKR. L.J. 363, 367 (1981) ("The 'insider' is new to the Code. The term came from prior statutes. The law to examine is Section 10(b) of the Securities Exchange Act of 1934.").

130 SEN REP. NO. 95-989, at 25 (1978), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5787, 5810; H.R. REP. NO. 95-595, at 312 (1977), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5936, 6269 ("'Insider' . . . is a new term.").

131 11 U.S.C. § 547(b)(4) (2018).

132 *Id.* § 1129(a)(10).

133 *See* Alec P. Ostrow, *Insider "Includes"? Include Me Out*, 7 AM. BANKR. INST. L. REV. 601, 611 (1999) (discussing pre-Code practice regarding insiders).

closer scrutiny than those dealing at arms [sic] length with the debtor."[134] This statement is somewhat misleading, however, in that insiders are not only subjected to closer scrutiny, but rather, most of the Bankruptcy Code provisions that use the term actually treat insiders adversely based on their insider status.[135]

The 1973 Report of the Commission on Bankruptcy Laws of the United States (the "1973 Commission Report"),[136] which led to the enactment of the 1978 Bankruptcy Code, contained four provisions, including a longer preference period, that would subject enumerated persons and entities to closer scrutiny and adverse treatment based on their close relationship with the debtor. As detailed in the following table, the enumerated persons and entities varied across the different provisions.[137] While the draft provisions did not use the term "insider," the explanatory notes accompanying each of the provisions referred to the enumerated persons and entities collectively as "insiders."[138] These lists apparently were the root

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[134] S. REP. NO. 95-989, at 25; H.R. REP. NO. 95-595, at 312. The rest of the paragraph goes on to restate much of the statute:

> If the debtor is an individual, than [sic] a relative of the debtor, a partnership in which the debtor is a general partner, a general partner of the debtor, and a corporation controlled by the debtor are all insiders. If the debtor is a corporation, then a controlling person, a relative of a controlling person, a partnership in which that debtor is a general partner, and a general partner of the debtor are all insiders. If the debtor is a partnership, then a general partner of or in the debtor, a relative of a general partner in the debtor, and a person in control are all insiders. In addition, affiliates of the debtor and managing agents are insiders.

S. REP. NO. 95-989, at 25; H.R. REP. NO. 95-595, at 312.

[135] *See e.g.*, 11 U.S.C. § 547(b)(4) (extending the ninety-day preference period to one year for insiders); *id.* § 1129(a)(10) (excluding votes of insiders in favor of a chapter 11 plan of reorganization).

[136] *See generally* H.R. REP. NO. 93-137 (1973) (Conf. Rep.).

[137] *Id.* pt. II, at 90–91, 99–100, 115, 166. "Affiliate" and "member of the immediate family" were defined terms. *See id.* at 1, 4.

[138] *Id.* at 91 (referring to "other fiduciaries and insiders"); *id.* at 92 (referring to "other fiduciaries or insiders" and to "the debtor's attorney, other fiduciaries, or insiders"); *id.* at 105 (referring to "insiders of a business debtor"); *id.* at 106 (referring to "insider of a debtor corporation"); *id.* at 116 (referring to "a corporate insider"). In addition, the 1973 Commission Report included analysis and evaluation of the then existing system of bankruptcy administration, which at several points touched on issues concerning "insiders" of the debtor. In explaining the new category of preferences between one year and three months before bankruptcy, the report stated, "[o]nly transfers to persons having a close relationship to the debtor are open to attack . . . ; they are members of the immediate family, partners, affiliates, directors, officers, and managing agents." *Id.* pt. I, at 201. In regard to disallowance of claims, the report stated, "in company with other recommendations of the Commission against insider manipulation of failing enterprises at the expense of creditors, any inflated claims of persons in control or their allies for compensation for personal services should be reduced to the reasonable value of the services." *Id.* at 213. On the subject of the appointment of a trustee, the report discussed at some length "the differing positions from which the general investor and the 'insider' frequently approached reorganizations," relying extensively on a highly influential SEC report by William O. Douglas that focused on the problem of the conflict of interests between "reorganizers" and investors in bankruptcy. *Id.* at 249–50; SECURITIES & EXCHANGE COMM'N, REPORT ON THE STUDY AND INVESTIGATION, PERSONNEL AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES: PART I, STRATEGY AND TECHNIQUES OF PROTECTIVE AND REORGANIZATION COMMITTEES 24–26, 29 (1937) [hereinafter Protective Committee Report] (providing a series of questions and answers intended to explore the conflict of interest between reorganizers and investors in bankruptcy). Relatedly, in discussing the incorporation of the absolute priority

of the definition of insider enacted as part of the Bankruptcy Code.[139] While each of the four provisions concerned pre-bankruptcy transactions with the debtor, the Bankruptcy Code definition of "insider" is used in both a number of such provisions and also in provisions that limit insiders' participation rights in the bankruptcy case itself.[140]

Insider Provisions in the 1973 Report of the Commission on Bankruptcy Laws of the United States

Provision	Enumerated persons and entities
Section 4-311(b): "*Examination of Transactions with Officers, Affiliates, and Immediate Family of Debtor*. . . . [T]he administrator may examine any payment of money or transfer of property made by the debtor within one year prior to the date of the petition or thereafter and any obligation incurred by the debtor within that time to make such a payment or transfer, to"	"any officer, member of the board of directors or similar controlling body, or controlling equity security holder or other person in control if the debtor is a corporation, or to a general partner or other person in control if the debtor is a partnership, or to an affiliate or a member of the immediate family of the debtor."
Section 4-403(b)(4): "*Claims of Creditors*. . . . Any claim . . . shall be allowed except to the extent . . . that . . . a claim for personal services . . . exceeds the reasonable value of such services [rendered by]"	"an attorney, a member of the immediate family, a director, an officer, or a managing agent of or for the debtor. . . ."
Section 4-406(a): "*Subordinated Classes of Claims*. The following claims are subordinated . . . (3) any claim, whether secured or unsecured, of "	"any principal officer, director, or affiliate of a debtor, or of any member of the immediate family of such officer, director, or affiliate. . . ."
Section 4-607: "*Preferences. (a) Right to Recover*. [A] trustee may recover property of the debtor transferred . . . (2) within the period commencing one year before and ending three months before the date of the petition [to]"	"a member of the immediate family, a partner, an affiliate, a director, an officer, or a managing agent of or for the debtor. . . ."

III. PRE-CODE CASE LAW

rule in chapter X of the former Bankruptcy Act, the report stated, "[t]he target of the [Protective Committee Report] was the ability of a few insiders, whether representatives of management or major creditors, to use the reorganization process to gain an unfair advantage." H.R. REP. NO. 93-137, pt. I, at 255.

[139] *See* H.R. REP. NO. 93-137, pt. I, at 255 ("The target of the Report was [to remove] the ability of a few insiders . . . to use the reorganization process to gain an unfair advantage."); *see also* Ostrow, *supra* note 133, at 611 (discussing the 1973 Commission Report's proposal regarding insider preferences).

[140] *See infra* notes 268–77 and accompanying text.

The Bankruptcy Code concept of insider likely was shaped by the pre-Code case law on equitable subordination.[141] The pre-Code and Code case law alike hold insiders are subject to heightened scrutiny with respect to their pre-bankruptcy dealings with the debtor.[142] The classic exposition of the doctrine of equitable subordination is in *Pepper v. Litton*,[143] where the Supreme Court wrote:

> That equitable power [to subordinate or disallow claims] also exists in passing on claims presented by an officer, director, or stockholder in the bankruptcy proceedings of his corporation. The mere fact that an officer, director, or stockholder has a claim against his bankrupt corporation or that he has reduced that claim to judgment does not mean that the bankruptcy court must accord it pari passu treatment with the claims of other creditors. Its disallowance or subordination may be necessitated by certain cardinal principles of equity jurisprudence. A director is a fiduciary. So is a dominant or controlling stockholder or group of stockholders. Their powers are powers in trust. . . . *The essence of the test is whether or not under all the circumstances the transaction carries the earmarks of an arm's length bargain.* If it does not, equity will set it aside. While normally that fiduciary obligation is enforceable directly by the corporation, or through a stockholder's derivative action, it is, in the event of bankruptcy of the corporation, enforceable by the trustee. *For that standard of fiduciary obligation is designed for the protection of the entire community of interests in the corporation-creditors as well as stockholders.*
>
> As we have said, the bankruptcy court in passing on allowance of claims sits as a court of equity. Hence these rules governing the fiduciary responsibilities of directors and stockholders come into play on allowance of their claims in bankruptcy, in the exercise of its equitable jurisdiction the bankruptcy court has the power to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in administration of the bankrupt estate. And its duty so to do is especially clear when the claim seeking allowance accrues to the benefit of an officer, director, or stockholder. That is

[141] Ironically, the Bankruptcy Code provision on equitable subordination does not actually employ the term "insider." *See* 11 U.S.C. § 510 (2018). Although courts addressing equitable subordination issues under the Bankruptcy Code refer to its definition of insider, it would seem, given that section 510 does not actually use the term, strictly speaking, they would be governed by the pre-Code concept rather than the Bankruptcy Code definition.

[142] *See, e.g.*, Pepper v. Litton, 308 U.S. 295, 306–08 (1939); Fabricators, Inc., v. Tech. Fabricators, Inc. (*In re* Fabricators), 926 F.2d 1458, 1465 (5th Cir. 1991).

[143] 308 U.S. 295.

> clearly the power and duty of the bankruptcy courts under the reorganization sections. . . .
>
> [A] sufficient consideration may be simply the violation of rules of fair play and good conscience by the claimant; a breach of the fiduciary standards of conduct which he owes the corporation, its stockholders and creditors. He who is in such a fiduciary position cannot serve himself first and his cestuis second. He cannot manipulate the affairs of his corporation to their detriment and in disregard of the standards of common decency and honesty. He cannot by the intervention of a corporate entity violate the ancient precept against serving two masters. He cannot by the use of the corporate device avail himself of privileges normally permitted outsiders in a race of creditors. He cannot utilize his inside information and his strategic position for his own preferment. He cannot violate rules of fair play by doing indirectly through the corporation what he could not do directly. He cannot use his power for his personal advantage and to the detriment of the stockholders and creditors no matter how absolute in terms that power may be and no matter how meticulous he is to satisfy technical requirements. . . .[144]

Thus, the Court closely links the concept of insider with having a fiduciary relationship with the debtor and the duty of loyalty that is owed by a fiduciary to the debtor. This is echoed in the legislative history to Bankruptcy Code section 101(31), which as noted above, explains "insider" by reference to "dealing at arms [sic] length with the debtor."[145]

IV. THE CIRCUIT SPLIT ON THE TEST FOR NON-STATUTORY INSIDER STATUS

This Part reviews the circuit split on the test for non-statutory insider status, and then reports the various explanations courts and commentators have offered for the Bankruptcy Code concept of insider status.

A. The Different Circuit Court Approaches to Non-Statutory Insider Status

1. The majority conjunctive test

Nine of the eleven federal circuit courts of appeals have considered the test for non-statutory insider status. The prevailing approach is a conjunctive test that "focuse[s] on two factors in making that determination: (1) the closeness of the

[144] *Id.* at 306–12 (emphasis added) (footnotes and citations omitted).
[145] *See supra* note 134 and accompanying text.

relationship between the transferee and the debtor; and (2) whether the transactions between the transferee and the debtor were conducted at arm's length."[146] The Fifth,[147] Ninth,[148] Tenth,[149] Eleventh,[150] and possibly the Third[151] Circuits have adopted this test, which is endorsed by the leading bankruptcy law treatise.[152] All except one of the circuit court cases adopting the conjunctive test were avoidance actions concerning a pre-bankruptcy transfer, and the large majority of these were insider preference actions. The one exception is the Ninth Circuit decision in *Lakeridge* that concerned section 1129(a)(10), which provides a chapter 11 plan may not be confirmed unless it is accepted by at least one class of impaired claims, excluding the vote of any insider.[153] In adopting the conjunctive test, the Ninth Circuit in *Lakeridge* relied on a Tenth Circuit case, *Anstine v. Carl Zeiss Meditec AG* (*In re U.S. Medical, Inc.*),[154] which involved an alleged insider preference claim.

In re U.S. Medical[155] is an illustrative, extensively reasoned, and often-cited case in which the Tenth Circuit adopted the conjunctive test, holding the inquiry regarding non-statutory insider status is "whether there is a close relationship [between the alleged insider and the debtor] *and* whether there is anything other than closeness to suggest that any transactions were not conducted at arm's length."[156] In holding the creditor was not a non-statutory insider, the court rejected the trustee's argument that closeness alone is sufficient to establish the creditor was a non-statutory insider.[157] The debtor was a distributor of medical equipment.[158] The creditor, Meditec,

[146] Mia. Police Relief & Pension Fund v. Tabas (*In re* The Fla. Fund of Coral Gables, Ltd.), 144 F. App'x. 72, 75 (11th Cir. 2005).

[147] *See* Browning Interests v. Allison (*In re* Holloway), 955 F.2d 1008, 1011 (5th Cir. 1992).

[148] *See* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993, 996 (9th Cir. 2016), *aff'd sub nom.* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960 (2018); *Lakeridge*, 138 S. Ct. at 965 ("The Ninth Circuit . . . endorsed a two-part test for non-statutory insider status."). *But see* Wake Forrest Inc. v. Transamerica Title Ins. Co. (*In re* Greer W. Inv. LP), No. 94-15670, 1996 WL 134293, at *3 (9th Cir. Mar. 25, 1996) (adopting a "functional" similarity approach focusing "on the nature of the relationship between the purported insider and the debtor. The goal is to determine whether the relationship in question is fraught with the same potential for improper influence as the relationships specifically enumerated in the statute").

[149] *See* Weinman v. Walker (*In re* Adam Aircraft Indus.), 805 F.3d 888, 894 (10th Cir. 2015) ("We have held . . . even someone not specifically listed in the statute can be considered an insider if he or she ha[s] a sufficiently close relationship with the debtor that . . . conduct is made subject to closer scrutiny than those dealing at arm's length with the debtor." (quotations omitted)); Anstine v. Carl Zeiss Meditec AG (*In re* U.S. Med., Inc.), 531 F.3d 1272, 1277 (10th Cir. 2008); Rupp v. United Sec. Bank (*In re* Kunz), 489 F.3d 1072, 1078–79 (10th Cir. 2007).

[150] *See In re* Coral Gables, 144 F. App'x at 75 (adopting the conjunctive test).

[151] *See* Schubert v. Lucent Techs. Inc. (*In re* Winstar Commc'ns, Inc.), 554 F.3d 382, 396–97 (3d Cir. 2009).

[152] *See* 5 COLLIER ON BANKRUPTCY ¶ 547.03[6], at 547-39 (Richard Levin & Henry J. Sommer eds., 16th ed. 2020) (stating the two factors to consider when determining insider status are: "(1) the closeness of the relationship between the parties; and (2) whether the transaction was negotiated at arm's length").

[153] *See In re* Lakeridge, 814 F.3d at 996 (citing 11 U.S.C. § 1129(a)(10) (2018)).

[154] *See id.* at 1001 (citing *In re* U.S. Med.,531 F.3d at 1277).

[155] 531 F.3d 1272.

[156] *Id.* at 1276 (citing *In re* Krehl, 86 F.3d 737, 742 (7th Cir. 1996)).

[157] *See id.* at 1273–74, 1276–77, 1282 ("[The closeness-alone] approach does not comport with the intent of Congress nor the case law. . . .").

[158] *Id.* at 1274.

produced aesthetic lasers.[159] The parties formed a "strategic alliance" based on a distributorship agreement and a stock purchase agreement.[160] Under the distribution agreement, the debtor became Meditec's exclusive distributor in North America, and Meditec obtained the right to appoint a member of the debtor's board of directors.[161] Under the stock purchase agreement, Meditec obtained a 10.6% equity interest in the debtor for $2,000,000 in cash and a $2,000,000 credit against the purchase of inventory.[162] Meditec appointed its president (Seitz) to the debtor's board.[163] Seitz attended all board meetings and "had access to all of Debtor's financial information but did not participate in any vote concerning payment to [Meditec]."[164] The bankruptcy court "specifically found" the following:

> [N]o evidence that Dr. Seitz, as [Meditec's] representative, controlled, sought to control, or exercised any undue influence on Debtor; rather, Dr. Seitz was sensitive to 'potential conflicts of interest' and both Dr. Seitz and Debtor's senior management 'attended to the kinds of formalities one would expect to see in dealings between third parties at arm's length.' Likewise, the bankruptcy court found no evidence that [Meditec's] 10% share of Debtor allowed [Meditec] to control or attempt to exercise any undue influence on Debtor.[165]

The court also rejected the trustee's argument that Meditec was a non-statutory insider because of its access through Seitz to all of the debtor's financial information.[166]

2. The closeness approach

Several of the circuit courts have focused on the closeness of the relationship between the alleged insider and the debtor, which is functionally a comparative test. It starts with the statement in the legislative history that "[a]n insider is one who has a sufficiently close relationship with the debtor,"[167] and is based on the premise that the common characteristic shared by the enumerated insiders is their closeness to the debtor.

The Third Circuit's test appears to require only closeness to the debtor and not to make an actual non-arm's-length transaction an absolute requirement. In *Schubert v.*

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[159] *Id.*
[160] *Id.*
[161] *Id.*
[162] *Id.*
[163] *Id.*
[164] *Id.*
[165] *Id.* (citations omitted).
[166] *See id.* at 1280–81 (finding Dr. Seitz took care to avoid potential conflicts of interest and never relied on insider information for an improper purpose).
[167] SEN REP. NO. 95-989, at 25 (1978), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5787, 5810; H.R. REP. NO. 95-595, at 312 (1977), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5936, 6269.

Lucent Technologies Inc. (*In re Winstar Communications, Inc.*), the court stated non-statutory insider status turns on "whether there is a close relationship [between the debtor and creditor] and . . . anything other than closeness to suggest that any transactions were not conducted at arm's length."[168] Arguably, however, the court was applying the conjunctive test; it cited *In re U.S. Medical* as authority for its statement of the rule,[169] and the case in fact involved transactions found not to be arm's length.[170]

In *In re Winstar*, the debtor was a corporation that provided telecommunications services, and was constructing a global broadband telecommunications network during the 1990's.[171] The creditor and alleged insider, Lucent, was a "corporation that 'design[ed] and deliver[ed] telecommunications systems, services, and products, including software.'"[172] Prior to the arrangements at issue, Lucent and the debtor were in an arm's-length vendor-debtor relationship, where the debtor purchased goods from Lucent.[173] In 1998, the parties entered into a "strategic partnership" where Lucent "agreed to help finance and construct [the debtor's] global broadband telecommunications network."[174] The agreement included a $2,000,000,000 line of credit from Lucent secured by a lien on "virtually all of [the debtor's] assets."[175] It also included a supply agreement, under which Lucent took primary responsibility for the construction of the debtor's network and provided the debtor would purchase 65% of the equipment and services from Lucent during the first year of the contract and 70% thereafter.[176] The debtors released Lucent's lien on its assets after it repaid the approximately $1,200,000,000 it borrowed from Lucent through funds from a revolving credit and term loan the debtor obtained from a group of bank lenders.[177] Thereafter, the parties entered into a second credit agreement for a $2,000,000,000 line of credit with the ability to borrow up to $1,000,000,000 at any one time, in exchange for a security interest in the debtor's subsidiaries' assets and a security interest senior to the bank lenders for equipment financed by Lucent.[178] After a competitor of Lucent entered into an agreement with the debtor to join the bank lenders through a $200,000,000 loan, Lucent compelled the debtor to pay it all of the available proceeds from the competitor's loan (approximately $188,200,000)

[168] 554 F.3d 382, 396–97 (3d Cir. 2009) (alterations in original) (quoting *In re* U.S. Med., 531 F.3d at 1277).
[169] *See id.*
[170] *Id.* at 399–400 ("We cannot conclude that the Bankruptcy Court's finding that the parties did not deal at arm's length was clearly erroneous.").
[171] *Id.* at 391.
[172] *Id.* (quoting *In re* Winstar Commc'ns, Inc., 348 B.R. 234, 252 (Bankr. D. Del. 2005)).
[173] *Id.*
[174] *Id.*
[175] *Id.* (quoting *In re* Winstar Commc'ns, 348 B.R. at 252).
[176] *Id.* at 391–92 ("In sum, under the October 1998 agreements [the debtor] obtained financing for its network construction and Lucent obtained a major customer for its products and services.").
[177] *Id.* at 392.
[178] *Id.*

pursuant to the second credit agreement, which was the alleged preferential transfer at issue.[179]

Based on the bankruptcy court's "extensive findings" that Lucent was the dominant party in the relationship by the time of the alleged preferential transfer, and that it possessed the ability to coerce the debtor into transactions not in the debtor's best interests, the Third Circuit held Lucent was a non-statutory insider.[180] For example:

> [Lucent] controlled many of [the debtor's] decisions relating to the buildout of the network; forced the purchase of its goods well before the equipment was needed and in many instances never needed at all; treated [the debtor] as a captive buyer for Lucent's goods; and used [the debtor] as a means for Lucent to inflate its own revenue.[181]

Accordingly, the Third Circuit held the bankruptcy court did not err in finding the parties did not deal at arm's length.[182] However, unlike the Tenth Circuit in *In re U.S. Medical*, the Third Circuit did not explicitly state a finding of a non-statutory insider requires the existence of a non-arm's-length transaction.[183]

The Fourth Circuit requires a "sufficiently close relationship," which is to be determined by whether the alleged insider "exercise[s] sufficient authority over the debtor so as to unqualifiably dictate corporate policy and the disposition of corporate assets."[184] In *Koch v. Rogers* (*In re Broumas*), the chapter 7 trustee initiated an adversary proceeding against Rogers and his law firm, the alleged insiders, to avoid and recover allegedly preferential transfers by the debtors under section 547(b) of the Bankruptcy Code.[185] Particularly, the trustee sought to avoid and recover transfers that included the granting of two deeds of trust on the debtors' residence in favor of the Rogers' law firm, the granting of two deeds of parcels of land to Rogers, the assignment of title to a first mortgage on a third parcel of land to Rogers, and certain cash transfers to Rogers and his firm stemming from a wash-trade scheme.[186] The

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[179] *See id.* at 393–94 ("[T]he Second Credit Agreement with Lucent obligated [the debtor] to pay any such increase in the Bank Facility to Lucent. Failure to do so would constitute an event of default under the Second Credit Facility.").

[180] *Id.* at 397–400 ("Not only was Lucent both a major creditor and supplier of [the debtor], but, according to the Bankruptcy Court, it had the ability to coerce [the debtor] into a series of transactions that were not in [the debtor's] best interests, such as the Software Pool transaction, the improper bill and hold transactions, and other purchases of unneeded equipment.").

[181] *Id.* at 397 (internal quotations and alterations omitted) (quoting *In re* Winstar Commc'ns, Inc., 348 B.R. 234, 280 (Bankr. D. Del. 2005)).

[182] *Id.* at 399–400.

[183] *Compare id.*, *with* Anstine v. Carl Zeiss Meditec AG (*In re* U.S. Med., Inc.), 531 F.3d 1272, 1280 (10th Cir. 2008) (holding "a creditor *may only* be a non-statutory insider of a debtor when the creditor's transaction of business with the debtor is not at arm's length" (emphasis added)).

[184] Butler v. David Shaw, Inc., 72 F.3d 437, 443 (4th Cir. 1996) (quoting *In re* Babcock Dairy Co., 70 B.R. 662, 666 (Bankr. N.D. Ohio 1986)).

[185] No. 97-1183, 1998 WL 77842, at *1 (4th Cir. Feb. 24, 1998).

[186] *Id.* at *1–2.

Fourth Circuit held the evidence "fully support[ed] the bankruptcy court's finding that . . . Rogers and [the debtors] had a sufficiently close relationship."[187] The debtors and Rogers held a "multifaceted relationship" over a fifteen-year period, which included relationships such as "creditor and debtor, principal and agent, joint venturers, attorney and client, landlord and tenant, and close friends."[188] Moreover, the parties made numerous loans to each other, Rogers permitted the debtors to make withdrawals from Rogers' and his law firm's bank accounts, the parties were involved in investment deals without written agreements, the parties made numerous bank stock purchases in furtherance of the wash-trade scheme, and Rogers agreed to represent the debtor in litigation without a written fee agreement.[189] Accordingly, the Fourth Circuit affirmed the bankruptcy court's holding that Rogers was a non-statutory insider of the debtors.[190]

The Eighth Circuit has stated simply an "'insider' is one who does not deal at arm's length with the debtor."[191] In a subsequent case, the Eighth Circuit BAP elaborated, "the ultimate issue is whether the creditor has a sufficiently close relationship to management to presume that that creditor unfairly received special treatment."[192] In *Seaver v. Glasser* (*In re Top Hat 430, Inc.*), the alleged preferential transfer involved the repayment of a loan provided by Ms. Glasser (the ex-wife of the debtor's president and alleged insider) and her current husband.[193] The bankruptcy court found, "although the transaction was not at arm's length, [Glasser] was not an insider."[194] On appeal, the trustee argued several aspects of the parties' relationship established a sufficiently close relationship to presume Glasser unfairly received special treatment.[195] Particularly, Glasser was the ex-spouse of and had three children with the debtor's president; Glasser (and her current husband) made a loan to the debtor without receiving the debtor's financial records; Glasser and her husband received personal guarantees while other lenders did not; and Glasser was repaid while other lenders were not.[196] The Eighth Circuit BAP rejected the trustee's argument and held, although terms of the Glasser's loan favored Glasser and her husband in some ways, there was no evidence showing the negotiations between the parties were not in each's own best interests.[197] More importantly, there was no evidence the repayment of

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187 *Id.* at *8.

188 *Id.* at *1, *8.

189 *Id.* at *8.

190 *See id.* ("In light of this evidence, we cannot say that the bankruptcy court's finding that Rogers was an insider is clearly erroneous.").

191 Carlson v. Farmers Home Admin. (*In re* Newcomb), 744 F.2d 621, 625 n.4 (8th Cir. 1984).

192 Seaver v. Glasser (*In re* Top Hat 430, Inc.), 568 B.R. 314, 319 (B.A.P. 8th Cir. 2017); *see also* Wake Forest Inc. v. Transamerica Title Ins. Co. (*In re* Greer W. Inv. LP), No. 94-15670, 1996 WL 134293, at *3 (9th Cir. Mar. 25, 1996) (using a comparative test that the Ninth Circuit subsequently declined to follow in *Lakeridge*).

193 *See* 568 B.R. at 316.

194 *Id.* at 317.

195 *See id.* at 319–20.

196 *Id.*

197 *Id.* at 320. The Eighth Circuit BAP held the aspects of the parties' relationship neither alone, nor collectively, created a close enough relationship. *Id.* First, Glasser and debtor's president had been divorced

Glasser's loan was at less than arm's length.[198] Accordingly, the Eighth Circuit BAP affirmed the bankruptcy court's holding that Glasser did not have sufficient closeness to establish her insider status.[199]

3. The Seventh Circuit's several approaches

The Seventh Circuit has taken several approaches to determining non-statutory insider status. In the most recent of three cases in which it has addressed the question, the panel applied a comparative ("similarity") test in deciding an LLC member was a statutory insider because an LLC member is substantially similar to a corporate director, one of the enumerated insiders of a corporate debtor.[200] In *In re Longview Aluminum, LLC*, the chapter 11 trustee brought an action to set aside and recover payments made to Mr. Forte, an LLC member of the debtor and the alleged insider.[201] The alleged preferential transfer at issue, which occurred approximately five months before the filing of the debtor's chapter 11 petition, was a transfer of $200,000 for a settlement agreement regarding a lawsuit filed by Forte.[202] The bankruptcy court held Forte was an insider and the district court affirmed.[203] On appeal, the Seventh Circuit stated "[w]hen the position held by the alleged insider is not enumerated . . . , the relevant inquiry for the court is to consider whether the relationship at issue is similar to or has characteristics of any of the defined relationships."[204] In doing so, a court is to "not only look to the [alleged insider's] title, but also his relationship to the company."[205] Accordingly, because, under Delaware law, both directors and LLC members "generally have the authority" to manage a corporation and LLC, respectively, "[an LLC member] is analogous to a director".[206] As to the Forte's relationship to the debtor, the Seventh Circuit held Forte maintained rights and control over the debtor LLC as a member of the LLC, despite the other members' efforts to prevent his management and participation in the debtor's affairs (the subject

for more than fifteen years, and their children were grown. *Id.* at 319–20. Second, Glasser and her husband testified they made the loan due to her confidence in the debtor's president from their past relationship and that they consulted with their accountant and financial manager about the loan. *Id.* at 320. Third, the trustee failed to prove the personal guaranty was the result of any untoward negotiations because all of the debtor's loans from various lenders had different terms. *Id.* Finally, the fact that Glasser was repaid does not establish her insider status; to hold otherwise "would make an insider out of anyone who gets paid within a year prior to bankruptcy." *Id.*

[198] *See id.*

[199] *Id.* at 321.

[200] *See In re* Longview Aluminum, LLC, 657 F.3d 507, 509–11 (7th Cir. 2011) (holding the similarity approach has the best application to the statute for non-statutory insiders).

[201] *See id.* at 508.

[202] *See id.* at 508–09 (detailing settlement terms and activities between the parties).

[203] *See id.* at 509.

[204] *Id.* at 510.

[205] *Id.* ("[I]t is not simply the title 'director' or 'officer' that renders an individual an insider; rather, it is the set of legal rights that a typical corporate director or officer holds." (quotation and citation omitted)).

[206] *Id.* (citing DEL. CODE ANN. tit. 8 § 141(a) (West 2020); DEL. CODE ANN. tit 6 § 18-402 (West 2020)).

of the settled lawsuit).[207] Thus, the lower courts correctly held Forte, as an LLC member, was an insider by applying the similarity approach.[208]

In the first case, *In re Krehl*, the Seventh Circuit held "[a]ccess to inside information can be sufficient to confer insider status even where there is no legal right or ability to exercise control over a corporate entity," where the alleged insider remained "the only one who knew what was going on."[209] Here, the alleged insider, Mr. Krehl, "was the president, the sole shareholder, and a director of [the debtor corporation.]"[210] The Seventh Circuit noted, prior to resigning from his position as president and director, "Krehl was for all intents and purposes the corporate entity itself."[211] He also managed the debtor's daily operations, established corporate policies, and knew everything there was to know about the debtor corporation.[212] Moreover, the Seventh Circuit held Krehl's resignation shortly after the debtor's bankruptcy was converted to chapter 7 did not "eviscerate his historically close relationship" to the debtor because, even after the resignation, the debtor still belonged to Krehl, and the longstanding relationship provided him with information that enabled the diversion of accounts and materials to his successor corporation.[213] Accordingly, the "[a]ccess to inside information [was] sufficient to confer [non-statutory] insider status" on Krehl.[214]

In another case, the Seventh Circuit stated the alleged insider controlled the debtor and, further, that "while 'insider' includes a 'person in control of the debtor,' it is not limited to such persons; it includes any entity so closely related to the debtor as to 'suggest that any transactions were not conducted at arm's length.'"[215]

B. Explanations of the Bankruptcy Code Concept of Insider

Reflecting the divergent approaches to determining non-statutory insider status, courts and commentators also have not articulated a clear and consistent understanding of the insider concept that would help guide the courts in determining questions of non-statutory insider status. Some have stated control over the debtor is the essence of insider status.[216] However, as others have pointed out, this cannot be

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[207] *See id.* at 508, 510–11.

[208] *See id.* at 511.

[209] 86 F.3d 737, 743 (7th Cir. 1996); *see also* Anstine v. Carl Zeiss Meditec AG (*In re* U.S. Med., Inc.), 531 F.3d 1272, 1278 (10th Cir. 2008) (interpreting *In re Krehl* as adopting the conjunctive test).

[210] *In re* Krehl, 86 F.3d at 739.

[211] *Id.* at 742.

[212] *Id.*

[213] *See id.* at 743 ("It is unlikely that an outsider would have been able to accomplish any or all of these things [without such access to inside information].").

[214] *See id.*

[215] *In re* S. Beach Sec., Inc., 606 F.3d 366, 377 (7th Cir. 2010) (citations omitted) (quoting Schubert v. Lucent Techs. Inc. (*In re* Winstar Comm'ns. Inc.), 554 F.3d 382, 396–97 (3d Cir. 2009)).

[216] *See, e.g.*, Butler v. David Shaw, Inc., 72 F.3d 437, 443 (4th Cir. 1996) (stating, to be a non-statutory insider, the entity "must exercise sufficient authority over the debtor so as to unqualifiably dictate corporate policy and the disposition of corporate assets" (quoting Hunter v. Babcock (*In re* Babcock Dairy Co.), 70 B.R. 662, 666 (Bankr. N.D. Ohio 1986))); *In re* A. Tarricone, Inc., 286 B.R. 256, 265 (Bankr. S.D.N.Y. 2002) ("The

the case because the enumerated statutory insiders include "person[s] in control of the debtor."[217] Given that the enumerated list is not exclusive, it follows that control is not necessarily required to find non-statutory insider status. Moreover, some of the enumerated insiders, such as relatives of the debtor,[218] are not typically or necessarily in control of the debtor. Certainly, influence or control over the debtor is a common characteristic of many enumerated insiders, albeit not necessarily determinative in and of itself.[219]

Some courts and commentators have written that access to inside information is the core concept underlying insider status.[220] As with control, however, while access to inside information is a common attribute of many enumerated insiders, it is not an invariable trait. Some, such as relatives of the debtor, do not typically or necessarily have inside knowledge of the debtor's financial affairs.[221] As with the element of

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nature of the relationships listed in all of the subparts of Section 101(31) are such that influence can be assumed, and it is therefore unnecessary to prove that there is actual control if such a relationship has been established."). *Cf.* Rupp v. United Sec. Bank (*In re* Kunz), 489 F.3d 1072, 1079 (10th Cir. 2007) ("[T]he legislative intent [was] that a person with a relationship designated in the statute be treated as an insider because of the high potential for control inherent in those relationships. . . ."); Stalnaker v. Gratton (*In re* Rosen Auto Leasing, Inc.), 346 B.R. 798, 804 (B.A.P. 8th Cir. 2006) ("An insider is one who does not deal at arm's length with the debtor. . . . However, the creditor would have to exert control over the debtor before gaining insider status. . . . [T]he closeness of the relationship between the two parties is also relevant.").

[217] 11 U.S.C. § 101(31)(A)(iv), (B)(iii), (B)(vi), (C)(ii), (C)(v) (2018). *See In re* Winstar Comm'ns, 544 F.3d at 396 ("To hold [a finding of control is necessary for an entity to be a non-statutory insider] would render meaningless Congress's decision to provide a non-exhaustive list of insiders . . . because the 'person in control' category would function as a determinative test."); Joseph L. Schwartz, Tara J. Schellhorn & Michael Trentin, *A Look Inside "Insider" Status: An Argument for a Multi-Factor Test to Identify "Non-Statutory Insiders,"* 27 NORTON J. OF BANKR. L. AND PRAC. 733, 738 (2018) (noting the Fourth Circuit's control approach has been criticized by other courts because the Bankruptcy Code expressly makes one a statutory insider when they are "in control of the debtor").

[218] *See* 11 U.S.C. § 101(31)(A)(i) (listing an "insider" as a "relative of a debtor").

[219] *See, e.g.*, Seaver v. Glasser (*In re* Top Hat 430, Inc.), 568 B.R. 314, 319 (B.A.P. 8th Cir. 2017); *see also* Anstine v. Carl Zeiss Meditec AG (*In re* U.S. Med., Inc.), 531 F.3d 1272, 1277–79 (10th Cir. 2008) (adopting the conjunctive test, and stating control over debtor and access to inside information are relevant considerations); Friedman v. Sheila Plotsky Brokers, Inc. (*In re* Friedman), 126 B.R. 63, 69–70 (B.A.P. 9th Cir. 1991); Carlson v. Farmers Home Admin. (*In re* Newcomb), 744 F.2d 621, 625 n.4 (8th Cir. 1984).

[220] *See In re* Krehl, 86 F.3d 737, 743 (7th Cir. 1996) (finding the alleged insider's access to inside information warranted the conclusion that he was a non-statutory insider, even though he had resigned as an officer and director of the debtor corporation); Tuskey, *supra* note 129, at 729–30 ("The primary reason for such exacting scrutiny of insiders is that persons with a close relationship to the debtor naturally have access to more information. Thus, insiders, can exert greater influence on the debtor, which causes insider transactions to be less vulnerable to the market pressures that help control arm's-length transactions." (footnotes omitted)); Phillips, *supra* note 129, at 365 ("Insiders may exercise judgment or control over a debtor and be able to know the financial condition of the debtor. It is safe to assume that insiders have knowledge. Armed with that knowledge, insiders may act to satisfy or protect their claims when they become aware of a risky financial situation.").

[221] Further, as originally enacted in the Bankruptcy Code, section 547 eliminated the "reasonable cause to believe" requirement under the Act, while retaining (but subsequently deleting) it for avoidance of insider preferences made between ninety days and one year before bankruptcy. This separate requirement for avoidance of a transfer to an insider between ninety days and one year before bankruptcy—a requirement that requires some level of knowledge on the part of the transferee—supports an inference that insiders are not insiders based on their knowledge of the debtor's financial position. Congress repealed the knowledge

control, access to inside information is a common feature of enumerated insiders and is commonly a factor in deciding non-statutory insider status under the Bankruptcy Code.[222]

Relying on the legislative history to section 101(31),[223] a number of courts have focused simply on the closeness of the relationship between the alleged insider and the debtor and whether the alleged insider deals at arm's length with the debtor as the guiding principle.[224]

In an often-quoted passage, the Ninth Circuit BAP explained the concept of insider in *Friedman v. Sheila Plotsky Brokers, Inc.* (*In re Friedman*)[225] as follows:

> First, the Code assigns insider status to entities or relatives of the debtor, or of persons in control of a related entity, whose affinity or consanguinity gives rise to a conclusive presumption that the individual or entity commands preferential treatment by the debtor. Second, insider status may be based on a professional or business relationship with the debtor, in addition to the Code's *per se* classifications, where such relationship compels the conclusion that the individual or entity has a relationship with the debtor, close enough to gain an advantage attributable simply to affinity rather than to the course of dealings between the parties.[226]

In several cases, courts have sought to explain the concept of "insider" in the particular context of Bankruptcy Code section 1129(a)(10), which provides acceptances by insiders must be excluded in determining whether at least one class of impaired claims has accepted a plan.[227] In *In re South Beach Securities, Inc.*,[228] the Seventh Circuit stated "[t]he exclusion . . . is intended to prevent conflicts of interest that can arise when a creditor has substantial influence over the debtor beyond what is implicit in being a creditor."[229] In *In re Featherworks Corp.*,[230] the bankruptcy court similarly explained:

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requirement in 1984. *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 462(b), 98 Stat. 333, 378 (codified as amended at 11 U.S.C. § 547(b)).

222 *See, e.g., In re* U.S. Med., 531 F.3d at 1277 ("Courts have also assessed the presence or absence of control of the debtor by the creditor and whether the creditor has access to inside information." (footnote omitted)).

223 *See supra* notes 138–49 and accompanying text.

224 *See In re* Top Hat, 568 B.R. at 319 ("[T]he ultimate issue is whether the creditor has a sufficiently close relationship to management to presume that that creditor unfairly received special treatment."); *In re* Newcomb, 744 F.2d at 625 n.4 ("[A]n insider is one who does not deal at arm's length with the debtor.").

225 126 B.R. 63 (B.A.P. 9th Cir. 1991). *Cf.* Stalnaker v. Gratton (*In re* Rosen Auto Leasing, Inc.), 346 B.R. 798, 804 (B.A.P. 8th Cir. 2006).

226 *In re* Friedman, 126 B.R. at 69–70 (footnote omitted).

227 11 U.S.C. § 1129(a)(10) (2018).

228 606 F.3d 366 (7th Cir. 2010).

229 *Id.* at 377.

230 25 B.R. 634 (Bankr. E.D.N.Y. 1982), *aff'd*, 36 B.R. 460 (E.D.N.Y. 1984).

> An insider . . . does not have the same interest as the [other] creditors. The creditors will benefit only to the extent of their distributive share . . . [insiders] will benefit by retaining effective ownership of a functioning company. . . . [They] are influenced by totally different considerations from those motivating the other creditors. . . .[231]

V. THE CASE FOR A COMPARATIVE TEST

This Part makes the case that the conjunctive test for non-statutory insider status is misconceived, and that a solely comparative approach is plainly supported by the text of the definition of insider and the legislative history. It further demonstrates the touchstone for determining questions of non-statutory insider status should be whether the alleged insider has (or at the time of the challenged transfer, had) a fiduciary or fiduciary-like relationship with the debtor.

A. The Conjunctive Test is Misconceived

The conjunctive test is inconsistent with the Bankruptcy Code's definition of insider. As Justice Sotomayor succinctly put it in *Lakeridge*, "[b]ecause each of [the enumerated] persons or entities are considered insiders regardless of whether a particular transaction appears to have been conducted at arm's length, it is not clear why the same should not be true of non-statutory insiders."[232]

More to the point, the conjunctive test is bad statutory interpretation because more than half of the nearly twenty Bankruptcy Code provisions that use the term insider do not concern avoidance of pre-bankruptcy transactions, but rather, involve a putative insider's participation or other rights in the bankruptcy proceeding itself.[233] While the insider preference provision is by far the most active battleground over whether a person or entity is an insider, the term is also used in Bankruptcy Code provisions such as those excluding insiders from voting on the appointment of a trustee in chapter 7 cases[234] and from the count of plan acceptances under section 1129(a)(10).[235] While the relevant time for determining insider status for purposes of avoiding a pre-bankruptcy transaction is the time of the transaction, the time for

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[231] *Id.* at 640. *See also* Wake Forest Inc. v. Transamerica Title Ins. Co. (*In re* Greer W. Inv. LP), No. 94-15670, 1996 WL 134293, at *4 (9th Cir. Mar. 25, 1996) ("[T]he concern in cases such as this, in which the debtor is attempting to cram down a plan of reorganization, is 'to forestall the voting of a creditor who is so beholden to or controlled by the debtor as to in effect be an alter ego of the debtor.'" (quoting *In re* Gilbert, 104 B.R. 206, 210 (Bankr. W.D. Mo. 1989))); *In re* Blaine Richards & Co., 10 B.R. 424, 432 (Bankr. E.D.N.Y. 1981) ("The purpose of the definition is to reach persons, like directors, stockholders, alter egos, and related corporations, who are part of management, rather than true creditors.").

[232] U.S. Bank Nat'l Ass'n *ex rel.* CWCaptial Asset Mgmt. LLC v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 971 (2018) (Sotomayor, J., concurring).

[233] *See infra* note 269 and accompanying text.

[234] *See* 11 U.S.C. § 702(a)(3) (2018) ("A creditor may vote for a candidate for trustee only if such creditor . . . is not an insider.").

[235] *See id.* § 1129(a)(10).

determining insider status under one of the latter provisions is during the pending case.[236] To require an actual non-arm's-length transaction would flatly preclude finding that someone is a non-statutory insider in the latter cases, no matter how close the relationship to the debtor—unless by coincidence there was some actual associated transaction between the alleged insider and the debtor.[237]

This was the case in *Lakeridge*. The issue was whether the sole vote by a creditor in favor of the debtor's plan had to be excluded under section 1129(a)(10) because the holder of the claim was a non-statutory insider.[238] Thus, the question concerned the creditor's relationship with the debtor as of the time for confirmation of the plan. As it happened, the creditor voting the claim was not the original holder of the claim, rather, he had acquired it from an insider of the debtor after the filing of the bankruptcy case.[239] Certainly, the circumstances under which he obtained the claim could be relevant to determining whether his relationship with the debtor was comparable to a statutory insider; however, an actual non-arm's-length transaction could not be essential.

Yet, the Supreme Court's majority opinion in *Lakeridge* focused on the transaction by which the alleged non-statutory insider had obtained the claim from a statutory insider, and not on the somewhat broader question of the relationship between the alleged insider and the debtor as of the time for voting on the debtor's plan.[240] This was unavoidable because the Court had denied certiorari on the test for non-statutory insider status and took as a given that the conjunctive test applied by the Ninth Circuit was correct for purposes of addressing the narrow issue on which it granted certiorari, the proper standard of appellate review.[241] In her concurrence, Justice Sotomayor hypothetically applied a comparative analysis to the facts of the case in which she focused on the relationship between the alleged insider and the debtor.[242]

The point that non-statutory insider status need not entail an actual transaction is clearly illustrated in the line of cases holding insiders who acquired their claims from non-insiders are treated as insiders for purposes of section 1129(a)(10). The courts have uniformly concluded an insider does not acquire the original claim holder's non-

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[236] *See infra* note 279 and accompanying text.

[237] Otherwise, the same definition would have different meanings in different Bankruptcy Code sections. *See* 11 U.S.C. § 103(a) ("[C]hapters 1 [which of course includes section 101(31)], 3, and 5 of this title apply in a case under chapter 7, 11, 12, or 13 of this title. . . ."). *See also* Ostrow, *supra* note 133, at 618–19 ("Although there is nothing logically unsound about having different levels of inclusion for insider relationship for the different insider provisions, . . . the notion of a statutory definition seems to mandate that the defined word mean the same thing each time it is used."). *See also id.* at 618–19 nn.100–01 (discussing how the term "insider" might be read more or less broadly depending on the purpose of the particular provision in which it is used).

[238] *See* U.S. Bank Nat'l Ass'n *ex rel.* CWCaptial Asset Mgmt. LLC v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 963 (2018) ("[C]rucially for this case, the consent of a creditor who is also an 'insider' of the debtor does not count for [the purpose of section 1129(a)(10)].").

[239] *See id.* at 964.

[240] *See id.* at 965.

[241] *See id.* at 965–68.

[242] *Id.* at 971–72 (Sotomayor, J., concurring).

insider status with the purchase of the non-insider's claim.[243] That the claim originated in an arm's-length transaction is not determinative of the claim holder's status in the subsequent bankruptcy case. Conversely, the courts are very largely in agreement that a creditor who acquires a claim from an insider does not necessarily acquire the insider's status as an insider.[244] Creditor and claim are two different things.[245] This latter issue also arose in *Lakeridge*, and the Supreme Court denied certiorari on it, too.[246]

B. The Comparative Approach is Supported by the Text of Section 101(31) and its Legislative History

Given that the Bankruptcy Code's definition of insider is a non-exclusive list of persons and entities, which includes no explicit prescription for determining who beyond the enumerated insiders may qualify as an insider, all that is left in order to interpret and apply the definition is to extrapolate from the enumerated list in deciding on non-statutory insiders.[247] Further, the legislative history of the definition is entirely

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[243] *See In re* Three Flint Hill LP, 213 B.R. 292, 301–02 (D. Md. 1997) (affirming the bankruptcy court determination that the creditor, who purchased several claims against the debtor at the debtor's behest, was a non-statutory insider for purposes of section 1129(a)(10)); *In re* Holly Knoll P'ship, 167 B.R. 381, 385 (Bankr. E.D. Pa. 1994) (holding the transferee of the non-insider's claim was not necessarily entitled to vote as a non-insider; "[t]he motivation behind the vote of an insider is the same regardless of how the insider got the claim"); *In re* Applegate Prop., Ltd., 133 B.R. 827, 833 (Bankr. W.D. Tex. 1991) (holding a corporation related to the debtor that purchased claims from non-insiders was a non-statutory insider for purposes of section 1129(a)(10); "[o]bviously, the motivation behind the vote is precisely the same regardless of how the insider came by the claim"); *In re* Gilbert, 104 B.R. 206, 211 (Bankr. W.D. Mo. 1989) ("[S]tatus of a creditor's right to vote is determined at the time the vote is taken, not at the time the debt arises."); *In re* Featherworks Corp., 25 B.R. 634, 640 (Bankr. E.D.N.Y. 1982), *aff'd*, 36 B.R. 460 (E.D.N.Y. 1984) (holding it is the creditor's status at the time of the vote, not at the time the debt arises, that matters for purposes of section 1129(a)(10)); *In re* Concord Square Apartments, Ltd., 174 B.R. 71, 75 (Bankr. S.D. Ohio 1994) (holding "the 'insider' status of a claimant does not, as a matter of law, transfer with a claim upon the sale or assignment of that claim to a third party" because there is a distinction between status of a claim and status of a claim holder, and the section 101(31) definition of "insider" describes the claim holder, not the claim). *Accord In re* Heights Ban Corp., 89 B.R. 795, 799 (Bankr. S.D. Iowa 1988) (holding the transferee of the claim was a non-statutory insider in its own right, not by virtue of transfer of the claim from an insider); *In re* Blesi, 43 B.R. 45, 47–48 (Bankr. D. Minn. 1984) (concerning insider status for purposes of section 702(a)(3)); *In re* Poage, 92 B.R. 659, 663–64 (Bankr. N.D. Tex. 1988). *But see* Wake Forest Inc. v. Transamerica Title Ins. Co. (*In re* Greer W. Inv. LP), No. 94-15670, 1996 WL 134293, *4 (9th Cir. Mar. 25, 1996) (finding insider status was automatically inherited by the transferee); U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. LLC v. Vill. at Lakeridge, LLC (*In re* Vill. at Lakeridge, LLC), 814 F.3d 993, 1001 n.10 (9th Cir. 2016) (recognizing the ruling in *In re Greer*, but noting a Ninth Circuit rule prohibits parties from citing or relying on unpublished dispositions issued before 2007).

[244] *See, e.g., In re* Lakeridge, 814 F.3d at 999–1000 ("Because insider status is not a property of a claim, general assignment—in which an assignee takes a claim subject to any benefits and defects of the claim—does not apply.").

[245] *See id.* at 999 ("[B]ankruptcy law distinguishes between the status of a claim and that of a claimant.").

[246] *See Lakeridge*, 138 S. Ct. at 965.

[247] *See id.* at 971 (Sotomayor, J., concurring) ("Assuming [section] 101(31) encompasses such 'non-statutory insiders,' the only clue we have as to which persons or entities fall within that category is the list of enumerated insiders and the presumption of lack of arm's length that follows from that label."). As Professor Ostrow states:

consistent with this approach. As noted above, the House and Senate Judiciary Committee Reports state: "An insider is one who has a sufficiently close relationship with the debtor that his conduct is made subject to closer scrutiny than those dealing at arms [sic] length with the debtor."[248] This statement broadly describes all insiders, statutory and non-statutory, by reference to their relationship with the debtor, tacitly assuming non-statutory insiders are comparable to the enumerated statutory insiders.

Recognizing "courts must develop some principled method of determining what other individuals or entities fall within the term 'insider' other than those expressly provided," the concurring justices in *Lakeridge* laid out "two possible legal standards that are consistent with the understanding that insider status inherently presumes that transactions are not conducted at arm's length:"

> First, it could be that the inquiry should focus solely on a comparison between the characteristics of the alleged non-statutory insider and the enumerated insiders, and if they share sufficient commonalities, the alleged person or entity should be deemed an insider regardless of the apparent arm's-length nature of any transaction.
>
> Second, it could be that the test should focus on a broader comparison that includes consideration of the circumstances surrounding any relevant transaction. If a transaction is determined to have been conducted at less-than-arm's-length, it may provide strong evidence in the context of the relationship as a whole that the alleged non-statutory insider should indeed be considered an insider. Relatedly, if the transaction does not appear to have been undertaken at arm's length, that may be evidence, considered together with other aspects of the parties' relationship, that the alleged non-statutory insider should not, in fact, be deemed an insider.[249]

> The major tools of statutory construction having little utility, the minor implements must be examined. Since the open-ended definition "includes" an eighteen-item enumeration, it appears useful to work with the implements that relate to lists. Such as:
>
> > That several items in a list share an attribute counsels in favor of interpreting the other items as possessing that attribute as well.
>
> This doctrine is related to two others bearing Latin names: *noscitur a sociis*, which means that a word in a statute "gathers meaning from the words around it"; and *ejusdem generis*, which provides that "when a general term follows a specific one, the general term should be understood as a reference to subjects akin to the one with specific enumeration." In the case of "insider," which is a definition, *noscitur a sociis* is not directly applicable, because "insider" does not appear in the middle of a list, and *ejusdem generis* also does not strictly apply, because "insider" does not appear at the end of a list. Nevertheless, all of these related doctrines convey the same common sense notion: the word at issue has to mean something not too different from the items in the list.

Ostrow, *supra* note 133, at 615–16 (footnotes omitted).

[248] SEN REP. NO. 95-989, at 25 (1978), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5787, 5810; H.R. REP. NO. 95-595, at 312 (1977), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5936, 6269. *See also* Ostrow, *supra* note 133, at 607.

[249] *Lakeridge,* 138 S. Ct. at 971–72 (Sotomayor, J., concurring) (citation omitted).

C. Insiders are Persons or Entities with a Fiduciary or Fiduciary-Like Relationship with the Debtor

The essence of insider status is a fiduciary or fiduciary-like relationship with the debtor. The definition of an insider with its list of enumerated insiders, the legislative history of the definition, the relevant pre-Code case law, and the statutory context of the use of the term across nearly twenty Bankruptcy Code provisions all evince this understanding of the term. The prototypical or average insider is a fiduciary of the debtor or vice versa.

Recognizing that "insider" roughly corresponds to fiduciary can help clarify and guide the judicial inquiry concerning non-statutory insider status, but is by no means a panacea:

> The concept of a confidential relationship cannot be reduced to a catalogue of specific circumstances, invariably falling to the left or right of a definitional line. The essence of such a relationship is trust and reliance on one side, and a corresponding opportunity to abuse that trust for personal gain on the other.[250]

Thus, the central object of the definition of insider is to identify persons and entities who would be expected to act in the best interest of the bankruptcy estate (future or present), or vice versa, under circumstances that require loyalty, trust, and good faith, even as the insider's interests may conflict with those of the estate.[251] Because a fiduciary owes his or her beneficiary strict duties of loyalty and care, this conception of insider is restrictive, setting a high standard for finding a person or entity is a non-statutory insider.[252]

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[250] *In re* Estate of Scott, 316 A.2d 883, 885 (Pa. 1974) (citation omitted). *See also* Indus. Gen. Corp. v. Sequoia Pac. Sys. Corp., 44 F.3d 40, 43–44 (1st Cir. 1995) (applying Massachusetts law); Mahaska Bottling Co. v. PepsiCo Inc., 271 F. Supp. 3d 1054, 1081 (S.D. Iowa 2017) (applying Iowa law); Martinelli v. Bridgeport Roman Catholic Diocesan Corp., 10 F. Supp. 2d 138, 153–54 (D. Conn. 1998) (applying Connecticut law), *aff'd in part, vacated in part*, 196 F.3d 409 (2d Cir. 1999).

[251] *See* RESTATEMENT (THIRD) OF TRUSTS § 2 cmt. b (AM. L. INST. 2003) ("[A] person in a fiduciary relationship to another is under a duty to act for the benefit of the other as to matters within the scope of the relationship. . . . [T]he fiduciary is under a duty not to profit at the expense of the other. . . ."). Black's Law Dictionary defines "fiduciary" as:

> 1. Someone who is required to act for the benefit of another person on all matters within the scope of their relationship; one who owes to another the duties of good faith, loyalty, due care, and disclosure <the corporate officer is a fiduciary to the corporation>. 2. Someone who must exercise a high standard of care in managing another's money or property <the beneficiary sued the fiduciary for investing in speculative securities>.

Fiduciary, BLACK'S LAW DICTIONARY (11th ed. 2019).

[252] Schwartz, Schellhorn & Trentin argue the similarity (comparative) approach "is a bit too restrictive and is therefore . . . not the correct test for determining non-statutory insider status." Schwartz, Schellhorn & Trentin, *supra* note 217, at 744. They further argue:

1. The text of the definition of "insider"

A review of the enumerated insiders in section 101(31) reveals that, with only one or possibly two exceptions, every one of them is either a fiduciary of the debtor or the debtor is a fiduciary of the insider.[253] And the one or two exceptions prove the rule. The one clear exception is the inclusion of relatives in the definition of an insider.[254] The Bankruptcy Code, in turn, defines "relative" as "individual related by affinity or consanguinity within the third degree . . . or individual in a step or adoptive relationship within such third degree."[255] In other words, the definition of insider extends to persons who are as distant from the debtor as grandparents-in-law or grandchildren-in-law. Certainly, relatives do not have a fiduciary relationship with a debtor simply by virtue of their family relationship. However, including them is entirely consistent with the purpose of identifying persons who presumptively have a relationship of trust and reliance with the debtor and who are in a position to abuse that trust for personal gain. In financial dealings with the debtor, relatives generally have an identity of interest with the debtor and are prone to self-dealing in the same way as any of the other enumerated insiders.

> [C]ourts should apply a more flexible [multi-factor] approach. . . . [One] that examines, principally, whether the alleged insider's relationship with the debtor is sufficiently close to compel the conclusion the conduct or transaction at issue is attributable to affinity rather than to normal arm's-length business dealings between the parties. . . .

Id. at 745.

253 Section 101(31)(E) adds "affiliate, or insider of an affiliate as if such affiliate were the debtor" to the list of enumerated insiders. 11 U.S.C. § 101(31)(E) (2018). "Affiliate" is itself a defined term. *See id.* § 101(2)(A). Additionally:

> The legislative history of Section 101 [defining affiliate] indicates that the terms 'directly or indirectly' in subsections (A) and (B) of Section 101(2) were used in the section to resolve uncertainty where there is an opportunity to control and where the existence of opportunity is tantamount to indirect control. . . .

Phillips, *supra* note 129, at 366. Further:

> The definition of 'affiliate' under the Code is taken from Bankruptcy Rule 901(3). The minimum percentage of control, however, was reduced to 20 percent from 25 percent. This reduction was in recognition of the fact that large corporations with affiliated status may be more readily controlled by less shares because their stock ownership is widely held. Rule 901(3) evolved from the definition of 'affiliate' contained in the Investment Company Act of 1940. The Investment Company Act also covered both direct and indirect control or ownership as well as the inclusion of officers and directors in its definition of 'affiliate.'

Id. at 368.

254 *See* 11 U.S.C. § 101(31)(A)(i), (B)(vi), (C)(ii), (D).

255 *Id.* § 101(45).

The other possible exception is the inclusion of "persons in control."[256] Like the non-statutory insider determination (and unlike the other enumerated insiders), there is not a bright-line boundary on what constitutes a person in control of the debtor. Yet, persons that actually control a debtor necessarily have a relationship of trust and reliance with the debtor and are in a position to abuse that trust for personal gain.[257]

While it is clear the quintessential insider is a person or entity having a fiduciary relationship with the debtor, the inclusion of enumerated statutory insiders that may have a tenuous relationship with the debtor arguably implies a comparative test, under which persons or entities with similarly attenuated relationships qualify as non-statutory insiders. Specifically, the fact that "relative" includes such distant relationships as grandparents- or grandchildren-in-law arguably means persons with comparably tenuous connections with the debtor would qualify as insiders.[258] The answer must be that the comparison is with the entire group of statutory insiders, not any one of the statutory insiders considered in isolation. Across the range of statutory insiders, the comparable non-statutory insider has a fiduciary or fiduciary-like relationship. Again, the average insider is a fiduciary of the debtor or vice versa.

2. Legislative history and pre-Code case law

The reference in the legislative history to "those dealing at arm's length with the debtor" is a direct reference to the concept of fiduciary.[259] As recounted above, the precursors of the definition of "insider" in the 1973 Bankruptcy Commission Report closely linked the concept with persons and entities having a fiduciary relationship with the debtor.[260] And the definition was almost certainly informed by pre-Code jurisprudence, most significantly, the Supreme Court's decision in *Pepper v. Litton* on equitable subordination, which focused on the fiduciary obligations of corporate officers, directors, and shareholders and defined fiduciary obligation in terms of whether the parties were dealing at arm's length.[261] An arm's-length transaction is a transaction conducted as between strangers, whereas a non-arm's-length transaction

[256] *See id.* § 101(31)(A)(iv), (B)(iii), (vi), (C)(v).

[257] *See generally* 2 BANKR. SERV. LAWS. ED. § 12:273 (2020) ("To identify 'insider,' . . . is to identify people or entities with high potential to gain advantage through their relationship with debtor."); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 177 (AM. L. INST. 1981) (stating a contract is voidable where it is the result of "unfair persuasion of a party who is under the domination of the person exercising the persuasion or who by virtue of the relation between them is justified in assuming that the person will not act in a manner inconsistent with his welfare").

[258] Justice Alito suggested as much during the oral argument in *Lakeridge*. Transcript of Oral Argument, *supra* note 109, at 37.

[259] *See* SEN REP. NO. 95-989, at 25 (1978), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5787, 5810; H.R. REP. NO. 95-595, at 312 (1977), *as reprinted in* 1978 U.S.C.C.A.N. (92 Stat. 2549) 5936, 6269.

[260] *See supra* notes 136–40 and accompanying text.

[261] *See* 308 U.S. 295, 306–12 (1939) ("The essence of the test is whether or not under all circumstances the transaction carries earmarks of an arm's length bargain. . . . For that standard of fiduciary obligation is designed for the protection of the entire community of interests in the corporation-creditors as well as stockholders.").

is a transaction conducted between parties having a relationship of trust and confidence.[262]

3. The definition of "insider" in the context of the Bankruptcy Code provisions in which it is used

The use of the term in several Bankruptcy Code provisions indicates, while the concept of fiduciary is at the root of the meaning of "insider," not all insiders will be fiduciaries and not all fiduciaries will be insiders. The definition does not use the term "fiduciary."[263] Further, there are several Bankruptcy Code provisions that list insiders along with persons who are generally considered to be fiduciaries. Section 303(b) excludes "any employee or insider" from being counted as a creditor for purposes of determining how many creditors are needed to commence an involuntary bankruptcy case;[264] and section 502(b)(4) disallows claims for "services of an insider or attorney of the debtor [to the extent they exceed] the value of such services."[265] Reading insider to encompass all fiduciaries would run afoul of the rule of statutory construction that seeks to give meaning to all of the words in a statute.[266] It would be unnecessary to add employees or attorneys to these provisions if the term insider already encompasses all fiduciaries. Thus, a non-fiduciary, such as the debtor's unmarried significant other, might well be considered a non-statutory insider, and employees of the debtor would not necessarily be excluded from the vote on a plan under of section 1129(a)(10).[267]

"Insider" is used in almost twenty provisions across the Bankruptcy Code and once in the Federal Rules of Bankruptcy Procedure. In addition, insider status is relevant to equitable subordination under section 510, although the term "insider" is

[262] *See* U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge (*In re* The Vill. at Lakeridge), 814 F.3d 993, 1001 n.11 (9th Cir. 2016) (finding an arm's-length transaction is one where two parties are either unaffiliated, or behave as though they are); *see also* Jones v. Harris Assocs. L.P., 559 U.S. 335, 347 (2010) ("The essence of the test [of whether there has been a breach of fiduciary duty] is whether or not under all the circumstances the transaction carries the earmarks of an arm's length bargain." (quoting *Pepper*, 308 U.S. at 306–07)). Professor Ostrow asserted, if the quoted statement in the House and Senate Judiciary Committee Reports "is correct, then anyone with a fiduciary relationship to the debtor must be included." Ostrow, *supra* note 133, at 607. Thus, he argued the statement "must be rejected as the controlling formulation" because several Bankruptcy Code provisions (sections 303(b) and 502(b)(4)) list insiders along with other fiduciaries, indicating "insider" is not coextensive with fiduciary. *Id.* at 609–10. This takes the statement too literally. It indicates the central concern of the insider concept is fiduciaries, but it need not be read as either exclusive or as covering all fiduciaries.

[263] *See* 11 U.S.C. § 101(31) (2018).

[264] *Id.* § 303(b)(2).

[265] *Id.* § 502(b)(4).

[266] *See* Ostrow, *supra* note 133, at 607–09.

[267] *Compare In re* Blaine Richards & Co., 10 B.R. 424, 432 (Bankr. E.D.N.Y. 1981) (holding debtor's accountant, who was privy to a great deal of confidential information, was not an insider for purposes of section 303(b)), *with In re* Rimell, 111 B.R. 250, 254 (Bankr. E.D. Mo. 1990) (holding attorneys with claims against the debtor, and currently representing the debtor in the involuntary case, were insiders for purposes of section 303(b)).

not actually used in the statute.[268] These instances fall into two basic categories: (1) provisions that deal with pre-bankruptcy transactions; and (2) provisions that operate to limit an insider's participation or other rights in the pending bankruptcy case itself.[269] That the term is used in both of these contexts is consistent with the idea that

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[268] *See* 11 U.S.C. § 510(c).

[269] The following chart lists the Bankruptcy Code provisions falling in either of the two categories:

Pre-bankruptcy Transactions with the Debtor	Post-bankruptcy Rights in the Pending Case
11 U.S.C. § 502(b)(4): "[T]he court . . . shall allow such claim . . . except to the extent that (4) if such claim is for the services of an *insider* or attorney for the debtor, such claim exceeds the value of such services. . . ." (emphasis added).	11 U.S.C. § 101(14): "The term 'disinterested person' means a person that — (A) is not a creditor, an equity security holder, or an *insider*. . . ." (emphasis added). Disinterestedness is in turn a requirement for the employment of professionals under 11 U.S.C. §§ 327(a), 701, 702 and 1104(b).
11 U.S.C. § 510(c): "[T]he court may—(1) under the principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or to all or part of an allowed interest to all or part of another allowed interest. . . ."	11 U.S.C. § 303(b)(2): "An involuntary case against a person is commenced by the filing with the bankruptcy court of a petition . . . (1) by three or more entities, each of which is either a holder of a claim . . . (2) if there are fewer than 12 such holders, excluding any employee or *insider* of such person. . . ." (emphasis added).
11 U.S.C. § 522(d)(10)(E)(i): "The following property may be exempted . . . (10) The debtor's right to receive . . . (E) a payment under a stock, bonus, pension, profit sharing, annuity, or similar plan or contract . . . to the extent reasonably necessary to support the debtor . . . unless—(i) such plan or contract was established by or under the auspices of an *insider* that employed the debtor at the time the debtor's rights under such plan or contract arose. . . ." (emphasis added).	11 U.S.C. § 503(c): "[T]here shall neither be allowed, nor paid—(1) a transfer made to, or an obligation incurred for the benefit of, an *insider* of the debtor for the purpose of inducing such person to remain with the debtor's business, absent a finding by the court based on the evidence . . . (2) a severance payment to an *insider* of the debtor . . . or (3) other transfers or obligations that are outside the ordinary course of business . . . including transfers made to, or obligations incurred for the benefit of, officers, managers, or consultants hired after the date of the filing of the petition." (emphasis added).
11 U.S.C. § 523(a)(2): "A discharge . . . does not discharge an individual debtor from any debt . . . (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an *insider*'s financial condition; (B) use of a statement in writing . . . (ii) respecting the debtor's or an *insider*'s financial condition. . . ." (emphasis added).	11 U.S.C. § 702(a)(3): "A creditor may vote for a candidate for trustee only if such creditor . . . (3) is not an *insider*." (emphasis added).
11 U.S.C. § 547(b)(4)(B): "[T]he trustee may avoid any transfer of an interest of the debtor in property . . . (4) made . . . (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an *insider*. . . ." (emphasis added). *See also* 11 U.S.C. §§ 547(i), 550(c)(2).	11 U.S.C. § 727(a)(7): "The court shall grant the debtor a discharge, unless . . . the debtor has committed any act specified in paragraph (2), (3), (4), (5), or (6) of this subsection . . . in connection with another case . . . concerning an *insider*. . . ." (emphasis added).

the essence of insider status is a fiduciary relationship with the debtor or its near-equivalent.

In each of these two categories, the potential for exploiting the fiduciary relationship at the expense of creditors and the bankruptcy estate runs in a different direction. The definition of "insider," with its enumerated persons and entities, plainly contemplates the fiduciary obligation may run either to or from the debtor. For example, if the debtor is an individual, insider includes both a partnership in which the debtor is a general partner and a general partner of the debtor, and if the debtor is a corporation, insider includes both a director of the debtor and a partnership in which the debtor is a general partner.[270] In the provisions dealing with pre-bankruptcy transactions, it is the owners or managers of the debtor, acting on behalf of the debtor, who may have made a transfer that benefited an insider (who may be an owner or manager) at the expense of creditors.[271] In the provisions concerning

11 U.S.C. § 548(a)(1)(B)(ii)(IV): "The trustee may avoid any transfer (including any transfer to or for the benefit of an *insider* under an employment contract) . . . if the debtor voluntarily or involuntarily . . . (B)(i) received less than a reasonably equivalent value in exchange for such transfer . . . and [(ii)](IV) made such transfer to or for the benefit of an *insider*, or incurred such obligation to or for the benefit of an *insider*, under an employment contract and not in the ordinary course of business." (emphasis added).	11 U.S.C. § 1104(c)(2): "If the court does not order the appointment of a trustee under this section, then . . . the court shall order the appointment of an examiner to conduct such an investigation of the debtor as is appropriate . . . [if] (2) the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an *insider*, exceed $5,000,000." (emphasis added).
11 U.S.C. § 747: "[U]nless all other customer net equity claims have been paid in full, the trustee may not pay . . . any net equity claim of a customer that was, on the date the transaction giving rise to such claim occurred—(1) an *insider*; (2) a beneficial owner of at least five percent of any class of equity securities of the debtor . . . (3) a limited partner with a participation of at least five percent in the net assets or net profits of the debtor; or (4) an entity that, directly or indirectly, through agreement or otherwise, exercised or had the power to exercise control over the management or policies of the debtor." (emphasis added).	11 U.S.C. § 1129(a)(5)(B): "The court shall confirm a plan only if all of the following requirements are met: . . . the proponent of the plan has disclosed the identity of any *insider* that will be employed or retained by the reorganized debtor, and the nature of any compensation for such *insider*." (emphasis added).
	11 U.S.C. § 1129(a)(10): "If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any *insider*." (emphasis added).
	FED. R. BANK. P. 1007(d): "[A] debtor . . . shall file with the petition a list containing the name . . . of the creditors that hold the 20 largest unsecured claims, excluding *insiders*. . . ." (emphasis added).

[270] *See* 11 U.S.C. § 101(31).

[271] *See, e.g., In re* FBN Food Servs., Inc., 175 B.R. 671, 687 (Bankr. N.D. Ill. 1994) ("In this case, the evidence shows that Waxman, acting on behalf of Quest Equities [as one of its officers and directors], which

participation and other rights in the bankruptcy proceeding, it is the insider (who may be an owner or manager), acting for the benefit of but not on behalf of the owners or managers of the debtor, at the expense of creditors.[272] In both contexts, there is a non-arm's-length relationship between the parties that may be exploited to benefit the insider at the expense of creditors, but the putative insider is the recipient of the benefit in the first category and the grantor of the potential benefit in the second category.[273]

In either category, the overriding concern is policing persons and entities having a relationship of trust and reliance with the debtor who are positioned to self-deal at the expense of creditors. With respect to pre-bankruptcy transactions, sections 502(b)(4), 510(c), 522(d)(10)(E)(i), 547(b)(4)(B), 548(a)(1), and 747(1) are all quite simply safeguards against self-dealing by persons with conflicts of interest who are in a position to benefit at the expense of other creditors.[274]

With respect to participation rights in bankruptcy, the purpose of the insider concept is likewise to ensure the governance and operations in bankruptcy will be consistent with the trustee or DIP's fiduciary obligations to creditors and ensure the trustee or DIP is constrained against taking advantage of their positions to benefit themselves at the expense of creditors. Thus, insiders cannot be employed as professionals in the case[275] or vote on the election of a trustee in chapter 7 cases,[276] and their acceptances do not count when determining whether a class of impaired claims has accepted a plan.[277]

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was an insider of the Debtor, and acting on behalf of River Bank [as its president] controlled and dominated Basile and Kaufman, two other insiders of the Debtor, in order to direct the transfer of money via the Settlement Agreement to River Bank[, one of the creditors].").

[272] *See, e.g., In re* Holly Knoll P'ship, 167 B.R. 381, 384–88 (Bankr. E.D. Pa. 1994) ("Weingartner [as its sole officer, director, shareholder, and limited partner] is a 'person in control' of Debtor and, under § 101(31)(C)(v), is an insider of Debtor. It would appear that the assignment to E.W. Real Estate was structured to avoid the application of § 101(31)(C)(v) and consequential infirmity of the ballot.").

[273] *See* Wake Forest Inc. v. Transamerica Title Ins. Co. (*In re* Greer W. Inv. LP), No. 94-15670, 1996 WL 134293, at *4 (9th Cir. Mar. 25, 1996) ("Litigation over whether a person is an insider occurs most frequently in the context of a claim of preferential transfer. 'The focus in these cases is whether the creditor's relationship with the debtor places the creditor in a position to influence or *control the debtor's actions* such that the interests of other creditors are frustrated.' By contrast, the concern in cases such as this, in which a debtor is attempting to cram down a plan of reorganization, is 'to forestall the voting of a creditor who is so beholden to or controlled by the debtor as to in effect be an alter ego of the debtor.'" (citations omitted)); *see also In re* Gilbert, 104 B.R. 206, 210 (Bankr. W.D. Mo. 1989) ("The focus in measuring the relative control in [the] context [of section 1129(a)(10)], however, is not necessarily on the extent of a creditor's control over the debtor. A disproportionate amount of control held by either the debtor or a creditor over the other could support the exclusion or invalidation of a creditor's vote on the basis of insider status.").

[274] The one provision that doesn't quite fit this mold is section 523(a)(2), which simply allows a creditor to rely on a written financial statement from the debtor concerning either the debtor's or an insider's financial condition. *See* 11 U.S.C. § 523(a)(2).

[275] *See id.* § 327(a) ("[T]he trustee . . . may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons. . . .").

[276] *See id.* § 702(a)(3).

[277] *See id.* § 1129(a)(10).

It may be argued the concept should be more strictly applied when the issue concerns a pre-bankruptcy transaction and the creditor stands to be deprived of a benefit it has received, and less strictly applied where the issue concerns prophylactic protection against possible conflicts of interest in a pending case. It is no surprise that, except for *Lakeridge*, the cases in which the circuit courts have adopted the conjunctive test all involved an alleged insider preference or other avoidable pre-bankruptcy transactions. The requirement that the subject transaction was not arm's length operates to limit the reach of the provision. The fact that the antecedents of the Bankruptcy Code definition in the 1973 Bankruptcy Commission Report, from which the term apparently was derived, were exclusively concerned with pre-bankruptcy transactions may suggest it does not map perfectly to the in-case provisions to which the drafters extended it. Yet, given that a term must have the same meaning wherever it is employed, at least in theory, the test must be applied consistently across both categories.

VI. WHAT WILL BE THE STANDARD OF REVIEW ON A COMPARATIVE TEST?

The Supreme Court in *Lakeridge* unanimously held the Ninth Circuit properly applied the clearly erroneous standard of appellate review with respect to the second prong of the conjunctive test—whether the relevant transaction was conducted at arm's length.[278] The Court reasoned the issue was a mixed question of law and fact—whether the historical facts satisfied the legal standard.[279] The legal standard, which the Court took as a given, was clearly a question of law subject to *de novo* review, while the findings of historical facts were clearly questions of fact subject to clearly erroneous review.[280] The central "query," the Court stated, was: "What is the nature of the mixed question here and which kind of court (bankruptcy or appellate) is better suited to resolve it?"[281] The outcome of this query depends on whether the mixed question "require[s] courts to expound on the law, particularly by amplifying or elaborating on a broad legal standard:"

> [This] involves developing auxiliary legal principles of use in other cases [or whether it] immerse[s] courts in case-specific factual issues—compelling them to marshal and weigh evidence, make credibility judgments, and otherwise address what we have (emphatically if a tad redundantly) called "multifarious, fleeting, special, narrow facts that utterly resist generalization."[282]

[278] U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC, 138 S. Ct. 960, 969 (2018). "[W]hat an [appellate court] may *not* do," the Court stated, "is review independently a garden-variety decision, as here, that the various facts found amount to an arm's length (or a non-arm's length) transaction and so do not (or do) confer insider status." *Id.* at 968 n.7.
[279] *Id.* at 966.
[280] *See id.*
[281] *Id.*
[282] *Id.* at 967 (quoting Pierce v. Underwood, 487 U.S. 552, 561–62 (1988)).

The Court readily concluded the question in *Lakeridge*, which could be reduced to whether the transaction between Rabkin and MBP was "conducted as though the two parties were strangers," fell clearly on the latter side of the divide.[283]

The Court specifically did not consider the standard of review on the first prong of the Ninth Circuit's test for non-statutory insider status, "the closeness of [the alleged insider's] relationship with the debtor is comparable to that of the enumerated insider classifications."[284] "A bankruptcy court applying the Ninth Circuit's test might, in another case, reach its separate, non-transactional prong," the Court stated, however, "[w]e express no opinion on how an appellate court should review a bankruptcy court's application of that differently framed standard to a set of established facts."[285]

If the correct test is a comparative test, without any requirement of an actual non-arm's-length transaction, as it surely is, the scant available precedent that is directly on point suggests the correct standard is *de novo*. There are two circuit level decisions in which the courts applied, or apparently applied, a solely comparative approach to whether a creditor was a non-statutory insider and, in doing so, considered the proper standard of appellate review. In both cases, the courts applied the *de novo* standard.[286] However, the courts gave only cursory consideration to the question.[287]

Upon a more detailed examination in light of the Supreme Court's decision in *Lakeridge*, the question appears to be a close one. As discussed above,[288] the key to determining non-statutory insider status using a comparative test is whether the person or entity has a fiduciary or fiduciary-like relationship with the debtor. This inquiry appears to be very similar to that framed by the Court in *Lakeridge*: whether the parties do not deal with each other at arm's length.[289] This describes a fiduciary relationship.[290] In *Lakeridge*, the majority focused on whether an actual transaction was conducted at arm's length as opposed to whether Rabkin and MBP had an arm's-length relationship,[291] but the basic inquiry arguably is much the same. As the Court explained it in *Lakeridge*:

> [T]he mixed question becomes: Given all the basic facts found, was Rabkin's purchase of Rabkin's purchase of MBP's claim conducted

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[283] *See id.* at 967–68.

[284] *Id.* at 965 (quoting U.S. Bank N.A. *ex rel.* CWCapital Asset Mgmt. v. Vill. at Lakeridge, LLC (*In re* The Vill. at Lakeridge, LLC), 814 F.3d 993, 1001 (9th Cir. 2016)).

[285] *Id.* at 967 n.5.

[286] *See In re* Longview Aluminum, LLC, 657 F.3d 507, 509 (7th Cir. 2011) (applying the comparative approach question of whether the LLC member was an insider); Schubert v. Lucent Techs., Inc. (*In re* Winstar Commc'ns, Inc.), 554 F.3d 382, 396–400 (3d Cir. 2009) (stating a comparative rule, but arguably applying the conjunctive test).

[287] *See In re* Longview Aluminum, 657 F.3d at 511; *see also In re* Winstar Commc'ns, 554 F.3d at 396.

[288] *See supra* notes 250–58 and accompanying text.

[289] *See Lakeridge*, 138 S. Ct. at 968.

[290] *See supra* notes 141–45 and accompanying text.

[291] *See Lakeridge*, 138 S. Ct. at 967–68.

> as if the two were strangers to each other? . . . The court takes a raft of case-specific historical facts, considers them as a whole, balances them one against another—all to make a determination [whether] two particular persons . . . were (or were not) acting like strangers. Just to describe that inquiry is to indicate where it (primarily) belongs: in the court that has presided over the presentation of evidence, that has heard all the witnesses, and that has both the closest and the deepest understanding of the record—*i.e.*, the bankruptcy court.[292]

On the other hand, deciding whether a *relationship* is arm's-length as opposed to whether a particular *transaction* was conducted at arm's length arguably entails "amplifying or elaborating on a broad legal standard."[293] Whether a person or entity has a fiduciary or comparable relationship with the debtor depends on two primary factors: whether there is "trust and reliance on one side, and a corresponding opportunity to abuse that trust for personal gain on the other."[294] These factors in turn are informed by such conditions as closeness, control, and inside knowledge.[295] Put this way, the inquiry does not involve a single conclusion to be drawn from "a raft of case-specific historical facts" the trial court "considers . . . as a whole [and] balances . . . one against another," as was the case with determining whether a transaction was conducted at arm's length in *Lakeridge*.[296] Rather, it entails developing norms and criteria of use in other cases. Further, unlike *Lakeridge*, intent and motivations, which are especially fact-specific inquiries, are not relevant considerations.[297]

In her concurring opinion joined by three other justices from across the ideological spectrum of the Court, Justice Sotomayor seemed to suggest the correct standard of review on a comparative test would be *de novo*. In hypothetically applying both a comparative test that "focus[es] solely on a comparison of the characteristics of the alleged non-statutory insider and the enumerated insiders" and a test that also would take account of circumstances surrounding any relevant transaction to the facts of *Lakeridge,* she "assum[ed], *arguendo*," each test would

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[292] *Id.* at 968 (footnote omitted).

[293] *Id.* at 967.

[294] *In re* Estate of Scott, 316 A.2d 883, 885 (Pa. 1974).

[295] *See id.* at 885–86 (assessing the closeness and degree of control of the parties' relationship); *see also* Chmieleski v. City Prods. Corp., 660 S.W.2d 275, 294 (Mo. Ct. App. 1983) ("[C]ertain basic elements necessary to the establishment of a fiduciary relationship . . . are: (1) as between the parties, one must be subservient to the dominant mind and will of the other as a result of age, state of health, illiteracy, mental disability, or ignorance; (2) things of value such as land, monies, a business, or other things of value which are the property of the subservient person must be possessed or managed by the dominant party; (3) there must be a surrender of independence by the subservient party to the dominant party; (4) there must be an automatic or habitual manipulation of the actions of the subservient party by the dominant party; and (5) there must be a showing that the subservient party places a trust and confidence in the dominant party.").

[296] 138 S.Ct. at 968.

[297] *Cf.* Pullman-Standard v. Swint, 456 U.S. 273, 288 (1982) ("Treating issues of intent as factual matters for the trier of fact is commonplace.").

"involve more legal than factual work thus resulting in *de novo* review."[298] Further, during oral argument of the case, there appeared to be a widely shared assumption among the justices that the standard of review on a purely comparative test would be *de novo*.[299] A comparative test would normally involve somewhat less factual work than a test that "focus[es] on a broader comparison that includes consideration of the circumstances surrounding any relevant transaction" and, therefore, would be somewhat more likely to be subject to *de novo* review.[300]

In other contexts involving whether a fiduciary relationship existed, appellate courts have held the question is one of law, subject to the *de novo* standard of review. For example, as to whether fiduciary status exists under ERISA, the courts of appeals have held the question is a mixed question of law and fact, and that where the facts are not disputed, the question is purely legal, subject to a *de novo* standard of review.[301]

Similarly, federal courts of appeals have consistently applied a *de novo* review standard to bankruptcy court determinations, based on factual findings that are not clearly erroneous, whether the debtor was acting in a fiduciary capacity for purposes of section 523(a)(4), which bars the discharge of debts "for fraud or defalcation while acting in a fiduciary capacity."[302]

Finally, it may be argued, as an institutional matter, appellate courts are "better positioned" to make determinations regarding non-statutory insider status because of a pro-reorganization bias on the part of bankruptcy judges.[303] At oral argument in

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[298] 138 S. Ct. at 971–72 (Sotomayor, J., concurring).

[299] *See* Transcript of Oral Argument, *supra* note 109, at 18. USB counsel stated: "Certainly an appellate court is better positioned to say what relationship is comparable to 101(31). That is not a trial court decision." *Id.* Justice Alito responded: "I think you have a strong argument on that." *Id.* In questioning the debtor's attorney, Justice Kagan stated that "how any particular set of facts does or does not meet [the first, comparative] prong of the test does not seem much of a factual question. . . . That doesn't seem like any factual question [she had] ever heard of." *Id.* at 35–36. Justice Alito again suggested the proper standard of appellate review on a comparative test would be *de novo* because appellate courts are the judicial actor better positioned to decide the question where "bankruptcy judges have a very strong tendency to want to get plans confirmed." *Id.* at 38–39. In questioning counsel for the United States as amicus curiae, Justice Kagan stated it "seems easier" to say that whether a transaction is made at arm's length is a factual inquiry than to say that a relationship is sufficiently close to be comparable to a statutory insider, with which counsel agreed. *Id.* at 56–57. Justice Gorsuch said, "if [the test] depends upon status, that might be a legal-looking question. If it depends on arm's length, that might be a more factual-looking question." *Id.* at 65.

[300] *See Lakeridge*, 138 S. Ct. at 971–72.

[301] *See, e.g.*, Varity Corp. v. Howe, 516 U.S. 489, 492 (1996) (reviewing, independently, the district court's legal holding that the employer was acting as an ERISA fiduciary based on factual findings that were not clearly erroneous); Allen v. Credit Suisse Sec. (USA) LLC, 895 F.3d 214, 218 (2d Cir. 2018) (conducting a *de novo* review of the district court's imposition of "a novel contract-evidence requirement for identifying ERISA functional fiduciary status"); David P. Coldesina, D.D.S. v. Estate of Simper, 407 F.3d 1126, 1131 (10th Cir. 2005) ("[W]here the parties essentially agree on the underlying facts, . . . the only issue . . . is the district court's legal conclusions, which we review de novo."); LoPresti v. Terwilliger, 126 F.3d 34, 38–39 (2d Cir. 1997).

[302] 11 U.S.C. § 523(a)(4) (2018). *See, e.g.*, Ingram v. Womack (*In re* Womack), 122 F. App'x 400, 401 (10th Cir. 2005); Fowler Bros. v. Young (*In re* Young), 91 F.3d 1367, 1371 (10th Cir. 1996); Ragsdale v. Haller, 780 F.2d 794, 795 (9th Cir. 1986); Raso v. Fahey (*In re* Fahey), 482 B.R. 678, 687 (B.A.P. 1st Cir. 2012).

[303] *See Lakeridge*, 138 S. Ct. at 967 (citing Miller v. Fenton, 474 U.S. 104, 114 (1985)).

Lakeridge, USB's counsel stated, "[b]ankruptcy is an area where forum shopping is prevalent. My concern is if you don't provide uniformity here, we're going to have a race to the bottom" because bankruptcy judges have a strong tendency to want to get plans confirmed.[304] Justice Alito later echoed this point during Lakeridge's argument on whether the bankruptcy court or an appellate court is better situated to make the determination of non-statutory insider status.[305] If bias of this sort is common, this would support using the *de novo* standard of review for the comparative test of non-statutory insider status.

CONCLUSION

By virtue of their relationship of trust and confidence with the debtor, insiders are in a position to appropriate value for themselves at the expense of creditors. The Bankruptcy Code therefore includes special protections against insiders exploiting their positions. Whether a person or entity is a non-statutory insider is a key determination under a range of Bankruptcy Code provisions. A majority of circuit courts have applied a conjunctive test to determine non-statutory insider status, but the requirement of an actual non-arm's-length transaction is clearly incorrect. As suggested by Justice Sotomayor in *Lakeridge*, the proper test for determining non-statutory insider status should entail only a comparative analysis that focuses on whether the alleged insider's relationship with the debtor is comparable to those of the enumerated insiders. Further, the prototypical insider has a fiduciary relationship with the debtor, and the essence of insider status is a fiduciary or fiduciary-like relationship of trust and confidence with the debtor. This insight indicates a strict test for non-statutory insider status and provides courts with a clear theoretical framework for making the non-statutory insider determinations in a more consistent manner. It is a close question whether the standard of review on this test should be *de novo* or clearly erroneous, and if *Lakeridge* has any legacy, it may well be that it is the fount of arguments on either side of the question.

[304] Transcript of Oral Argument, *supra* note 109, at 27.
[305] *See id.* at 39.