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A Bad Faith Filing

IN RE NATIONAL RIFLE ASSOCIATION OF AMERICA AND SEA GIRT, LLC

628 B.R. 262 (BANKR. N.D. TEX. 2021)

Background on the NRA

The National Rifle Association of America (the “NRA”) is a 150-year-old organization with approximately five million members that is dedicated to the rights of Americans to own and safely use firearms for their personal protection and recreational use. The mission and function of the NRA is focused on gun safety, and the NRA asserts it is “the nation's foremost defender” of the Second Amendment of the United States Constitution. In recent years, however, it has become apparent that the NRA was suffering from inadequate governance and internal controls.

In re Nat'l Rifle Ass'n of Am., 628 B.R. 262, 263–64 (Bankr. N.D. Tex. 2021).

“The question the Court is faced with is whether the existential threat facing the NRA is the type of threat the Bankruptcy Code is meant to protect against.”

- U.S. BANKRUPTCY JUDGE HARLIN D. HALE
IN RE NAT'L RIFLE ASS'N OF AM., 628 B.R. AT 264.

The Threat: NY AG Complaint Seeking Dissolution

The NRA filed this case seeking the protection of the Bankruptcy Code **to preserve itself as a going concern in the face of litigation** Debtors commonly file bankruptcy when faced with a judgment that has, or will, render them insolvent, but the threat against the NRA differs from the classic scenario in that **dissolution** would not be a collateral effect of litigation but rather **the intended relief sought** in a state’s regulatory action. *In re Nat'l Rifle Ass'n of Am.*, 628 B.R. 262, 264 (Bankr. N.D. Tex. 2021).

NRA Formation -> NYAG Investigation & Complaint -> Bankruptcy Filing & Dismissal

| | |
|--------------------------|---|
| ▪ November 17, 1891 | New York grants the NRA a charter |
| ▪ Mid-2017 | New York AG's office informs NRA Board Member its office was opening investigations against NRA |
| ▪ 15-month investigation | NRA engages in "course correction," during which it also files a complaint against the governor of New York alleging interference with First and Second Amendment rights |
| ▪ August 6, 2020 | AG Letitia James files complaint in New York against NRA and 4 individual defendants seeking, inter alia, the dissolution of the NRA. |
| ▪ Late summer 2020 | NRA sets up entity Sea Girt, LLC in Texas. |
| ▪ January 7, 2021 | NRA closed door board meeting approved an employment agreement of Wayne LaPierre that included restructuring powers for purposes of cost minimization, regulatory compliance or otherwise. No mention of potential bankruptcy filing or Sea Girt formation at meeting. |
| ▪ 8 days later | NRA and Sea Girt, LLC file chapter 11 cases in Texas (later, jointly administered) |
| ▪ 12-day trial | Multiple motions to dismiss, and also to appoint a trustee and/or appoint an examiner. NRA opposed all motions but eventually consented to appointment of a chief restructuring officer. 16 states signed on to an amicus brief, and Texas filed its own brief in support of the NRA. |
| ▪ May 11, 2021 | U.S. Bankruptcy Court enters 38-page written order dismissing bankruptcy case |

The Proposed Solution Avoid New York, Relocate to Texas

"The Debtors filed these bankruptcy cases not to gain a tactical litigation advantage, but to implement a strategy *to survive* in the event of a potential adverse ruling in the NYAG Action. As described below, there could not be a more fundamental and proper use of the federal bankruptcy laws than preservation of and as a going concern."
In re Nat'l Rifle Ass'n of Am., 628 B.R. at 273 quoting the Official Committee of Unsecured Creditors' Omnibus Response.

NRA set out three goals in opening: "First, avoid the death penalty. Avoid dissolution. Two, avoid a receiver in a New York state court that would deny us the ability to file. And third, we wholly embrace our third goal. Our third goal is to [. . .] remove ourselves from New York and relocate ourselves to Texas." *In re Nat'l Rifle Ass'n of Am.*, 628 B.R. at 274.

Gamesmanship or Prudent Liability Management ?

Dismissal for Cause Under 11 U.S.C. § 1112(b)

“Determining whether the debtor’s filing for relief is in good faith depends largely upon the bankruptcy court’s on-the-spot evaluation of the debtor’s financial condition, motives, and the local financial realities. Findings of lack of good faith in proceedings based on §§ 362(d) or 1112(b) have been predicated on certain recurring but non-exclusive patterns, and they are based on a conglomerate of factors rather than on any single datum.” *In re Nat’l Rifle Ass’n of Am.*, 628 B.R. at 280 quoting *In re Little Creek Dev. Co.*, 779 F.2d 1068, 1072 (5th Cir. 1986).

“Courts have consistently held that a bankruptcy case filed for the purpose of obtaining an unfair litigation advantage is not filed in good faith and should be dismissed.” *In re Nat’l Rifle Ass’n of Am.*, 628 B.R. at 281 citing *Antelope Techs., Inc. v. Lowe (In re Antelope Techs, Inc.)*, 431 F. App’x. 272 (5th Cir. 2011).

Excerpts from Analysis

- “A dissolution that requires this showing is not the type of dissolution that the Bankruptcy Code is meant to protect against. The Court is not in any way saying it believes the NYAG can or cannot make the required showing to obtain dissolution of the NRA, but the Court is saying that the Bankruptcy Code does not provide sanctuary from this kind of a threat.” *In re Nat’l Rifle Ass’n of Am.*, 628 B.R. at 281.
 - “The purpose of this bankruptcy filing may not have been to end the NYAG Enforcement Action immediately, but it was to deprive the NYAG of the remedy of dissolution, which is a distinct litigation advantage.” *In re Nat’l Rifle Ass’n of Am.*, 628 B.R. at 281.
 - “Reincorporating in Texas could be accomplished outside of bankruptcy pursuant to applicable regulations for New York not-for-profit organizations, which begs the question of what the Bankruptcy Code is being used for. If the goal is moving to Texas, the purpose of the bankruptcy would still appear to be avoidance of the regulatory scheme in New York that would be required for such a transition outside of bankruptcy, or at least avoidance of the New York regulators.” *In re Nat’l Rifle Ass’n of Am.*, 628 B.R. at 282.
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*“The Court finds there is cause to dismiss this bankruptcy case as not having been filed in good faith both because **it was filed to gain an unfair litigation advantage** and because **it was filed to avoid a state regulatory scheme.**”*

HOLDING



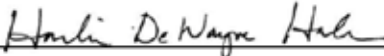
CLERK, U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS

ENTERED

THE DATE OF ENTRY IS ON
THE COURT'S DOCKET

The following constitutes the ruling of the court and has the force and effect therein described.

Signed May 11, 2021


United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

| | | |
|---------------------------------------|---|-------------------------|
| In re: | § | Chapter 11 |
| | § | |
| National Rifle Association of America | § | Case No. 21-30085 (HDH) |
| and Sea Girt LLC, | § | |
| | § | (Jointly Administered) |
| Debtors. | § | |

ORDER GRANTING MOTIONS TO DISMISS

The National Rifle Association of America (the “NRA”) is a 150-year-old organization with approximately five million members that is dedicated to the rights of Americans to own and safely use firearms for their personal protection and recreational use. The mission and function of the NRA is focused on gun safety, and the NRA asserts it is “the nation’s foremost defender” of the Second Amendment of the United States Constitution. In recent years, however, it has become apparent that the NRA was suffering from inadequate governance and internal controls.

The attorney general for the state of New York conducted a fifteen-month-long investigation of the NRA that revealed, the New York attorney general claims, widespread misuse of assets by the NRA’s executive vice president and his circle of insiders for their personal benefit. Nine months ago, the New York attorney general filed a lawsuit seeking dissolution of the NRA

based on allegations that (1) the NRA has exceeded the authority conferred upon it by New York law and has conducted its business in a persistently illegal manner and abused its powers contrary to the public policy of the state of New York by operating without effective oversight or control by its officers and directors, and (2) the directors or members in control of the NRA have looted or wasted the corporate assets, have perpetuated the corporation solely for their personal benefit, or have otherwise acted in an illegal, oppressive, or fraudulent manner.

The NRA filed this case seeking the protection of the Bankruptcy Code to preserve itself as a going concern in the face of litigation that, it argues, poses an existential threat. Debtors commonly file bankruptcy when faced with a judgment that has, or will, render them insolvent, but the threat against the NRA differs from the classic scenario in that dissolution would not be a collateral effect of litigation but rather the intended relief sought in a state's regulatory action. And in this instance, dissolution could only occur after judicial consideration of whether dissolution is in the best interest of the public.

The question the Court is faced with is whether the existential threat facing the NRA is the type of threat that the Bankruptcy Code is meant to protect against. The Court believes it is not. For the reasons stated herein, the Court finds there is cause to dismiss this bankruptcy case as not having been filed in good faith both because it was filed to gain an unfair litigation advantage and because it was filed to avoid a state regulatory scheme. The Court further finds the appointment of a trustee or examiner would, at this time, not be in the best interests of creditors and the estate.

I. Jurisdiction and Venue

This Court has jurisdiction to consider this matter under 28 U.S.C. §§ 157 and 1334. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A). Venue is proper in this District under 28 U.S.C. §§ 1408 and 1409.

II. Relevant Background

The NRA is a charitable not-for-profit corporation chartered by special act of the New York State Legislature on November 17, 1871. The NRA has approximately five million members, almost 500 employees, and annual revenue of approximately \$300 million. The NRA is primarily supported by dues from members and private contributions from donors.

Around the middle of 2017, NRA Board Member Tom King received a phone call from Eric Schneiderman, who at the time was the New York attorney general.¹ According to Mr. King, Mr. Schneiderman told him that investigations into the NRA were being opened and they should “prepare for the worst.”² Mr. King shared this message with Wayne LaPierre,³ the NRA’s executive vice president.⁴ In response to this warning, Mr. LaPierre testified that he decided the “NRA ought to take a look at everything, a 360-degree look to make sure we were in total compliance with New York State not-for-profit law, and if we weren’t, we needed to fix things.”⁵ This was the beginning of what the NRA now refers to as its course correction.⁶

As part of its course correction, the NRA hired the law firm Morgan, Lewis & Bockius LLP to provide advice regarding tax and nonprofit governance matters.⁷ The NRA also hired Brewer, Attorneys & Counselors (the “Brewer Firm”) in early 2018 to aid with the course

¹ *Transcript of Hearing Held April 21, 2021* [Docket No. 670] at 79:3-80:7; *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 62:12-16.

² *Transcript of Hearing Held April 21, 2021* [Docket No. 670] at 79:18-80:1.

³ *Transcript of Hearing Held April 21, 2021* [Docket No. 670] at 80:19-81:2.

⁴ In the NRA’s organizational structure, the executive vice president is the functional equivalent of a chief executive officer. *See* Ackerman Exhibit 10 (NRA Bylaws, Article V, section 2(c)).

⁵ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 41:25-42:14.

⁶ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 62:8-11.

⁷ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 43:17-44:1; *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 62:19-63:12.

correction process and potential upcoming litigation.⁸ Since that time, in addition to becoming the NRA’s primary litigation counsel, the Brewer Firm appears to have become involved in many aspects of the NRA.

In March 2018, the NRA hired Craig Spray as its new chief financial officer.⁹ Before joining the NRA, Mr. Spray served as the chief financial officer for two different companies, one of which was a publicly traded company valued at over \$1 billion.

On April 19, 2018, the New York Department of Financial Services sent letters to insurers and financial institutions encouraging them to review their relationships with the NRA and consider whether such relationships harm their corporate reputations and jeopardize public safety (the “NY DFS Letter”). Less than a month later, the NRA, with the assistance of the Brewer Firm, filed a complaint in federal court in the Northern District of New York against the governor of New York and the New York Department of Financial Services regarding their alleged attempts “to deprive the NRA and its constituents of their First Amendment rights to speak freely about gun-related issues and defend their Second Amendment freedoms against encroachment.”¹⁰

In July 2018, several whistleblowers came forward with the encouragement of Mr. Spray and presented a memo to the NRA Audit Committee regarding their top concerns (the “Whistleblower Memo”).¹¹ That list included concerns related to (1) financial conflicts of interest of senior management and board members, (2) senior management override of internal controls relating to, among other things, accounts payable procedures, travel and expense reporting, and procurement/contracts policy, (3) management making decisions in the best interests of vendors

⁸ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 67:13-16; *Transcript of Hearing Held April 21, 2021* [Docket No. 670] at 81:3-9; *Transcript of Hearing Held April 23, 2021* [Docket No. 697] at 148:16-19.

⁹ The board of directors also elected Mr. Spray as the treasurer of the NRA in September 2018.

¹⁰ NRA Exhibit 663.

¹¹ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 95:1-21; NYAG Exhibit 72.

instead of the NRA, (4) vague and deceptive billing practices of vendors, (5) improper reimbursement for apartments and living expenses of certain employees, and (6) lack of control over vehicle leases obtained by senior management.¹²

Following the presentation of the Whistleblower Memo to the Audit Committee, the NRA took several actions, including examining related party transactions and reviewing vendor contracts.¹³ As a result of this review process, the NRA required the inclusion of specific metrics in all contracts¹⁴ and improved documentation and recordkeeping.¹⁵ One of the more significant actions taken in response to the Whistleblower Memo was to send letters to the NRA's vendors notifying them of the rules regarding proper invoicing.¹⁶ While most vendors complied with these new measures, some did not.¹⁷ As a result, some contracts with vendors were re-negotiated, and some were terminated.¹⁸

This process caused a rift between the NRA and one of its most significant vendors, Ackerman McQueen, Inc. ("Ackerman"). Ackerman had very close ties with the NRA and had been the NRA's marketing and public relations firm for decades, but several of the concerns expressed in the Whistleblower Memo related to the NRA's relationship with Ackerman.¹⁹ The disagreements that came from discussions regarding billing practices and their business

¹² NYAG Exhibit 72.

¹³ *Transcript of Hearing Held April 23, 2021* [Docket No. 697] at 90:4-19.

¹⁴ *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 69:22-70:2.

¹⁵ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 24:24-25:9; *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 157:6-20.

¹⁶ *Transcript of Hearing Held April 23, 2021* [Docket No. 697] at 90:4-19; *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 25:10-25; *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 91:8-17.

¹⁷ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 91:8-92:4.

¹⁸ *Transcript of Hearing Held April 23, 2021* [Docket No. 697] at 91:2-9.

¹⁹ NYAG Exhibit 72.

relationship escalated and have spawned four overlapping lawsuits—three in Virginia state court and one in federal court in the Northern District of Texas.

On August 6, 2020, following a fifteen-month investigation, the New York attorney general (the “NYAG”) filed a complaint in New York state court against the NRA seeking, among other relief, dissolution of the NRA (the “NYAG Complaint” commencing the “NYAG Enforcement Action”).²⁰ The NYAG Complaint also named four individual defendants: (1) Mr. LaPierre; (2) John Frazer, the NRA’s general counsel; (3) the NRA’s former treasurer and chief financial officer; and (4) the NRA’s former chief of staff. The allegations in the 163-page NYAG Complaint are extensive but, in very general terms, accuse Mr. LaPierre of (i) exploiting the NRA for his financial benefit and the benefit of a close circle of NRA staff, board members, and vendors, (ii) intimidating, punishing, and expelling anyone at a senior level who raised concerns about his conduct, (iii) hiring and retaining individuals in senior positions at the NRA, or as NRA contractors, whom he believed would aid and enable him to control the organization, regardless of their skills, experience, integrity, or contribution to the charitable mission, and (iv) entering into post-employment agreements with departing officers and employees that provided excessive payments in exchange for little, if any, services and non-disclosure/non-disparagement agreements. Other of the individual defendants were accused of (i) ignoring, overriding, or otherwise violating the bylaws and internal policies and procedures they were charged with enforcing, resulting in charitable assets being diverted to benefit NRA insiders and favored vendors, (ii) instituting a practice whereby millions of dollars in entertainment and travel expenses incurred by NRA executives were billed to the NRA as disbursements by the NRA’s largest vendor, and (iii) circumventing internal controls, condoning or partaking in expenditures that were

²⁰ NYAG Exhibit 107.

an inappropriate and wasteful use of charitable assets, and concealing or misreporting relevant information, rendering the NRA's annual reports filed with the NYAG materially false and misleading. The NYAG Complaint, in addition to dissolution of the NRA, seeks (i) restitution of certain funds paid to current and former officers, which would be returned to the NRA, (ii) a ban on certain former and current officers, including Mr. LaPierre and Mr. Frazer, from serving as fiduciaries of any New York charity, and (iii) voiding of certain transactions.²¹

On September 10, 2020, Carolyn Meadows (the NRA's President) created a Special Litigation Committee to oversee (i) the NYAG Enforcement Action, (ii) a lawsuit filed against the NRA and the NRA Foundation by the District of Columbia attorney general, (iii) the NRA's pending lawsuit against the NYAG, and (iv) any future proceedings that arise out of or relate to the previously-identified matters. In an e-mail sent to the board of directors, Ms. Meadows explained that the creation of the Special Litigation Committee was done on the advice of counsel to avoid the appearance of any conflict because Mr. LaPierre and Mr. Frazer were named as individual defendants in the NYAG Enforcement Action.²² The Special Litigation Committee's members were Ms. Meadows, Charles Cotton (the NRA's First Vice President), and Colonel Willes Lee (the NRA's Second Vice President).

On November 18, 2020, the NRA filed its IRS Form 990 signed by Mr. LaPierre.²³ This form is an annual informational tax return filed by a nonprofit to justify maintaining its tax-exempt status. In the Form 990, the NRA disclosed several excess benefit transactions entered into by individuals at the NRA, including Mr. LaPierre.

²¹ *Id.*

²² NYAG Exhibit 1.

²³ NYAG Exhibit 8.

On November 23, 2020, the NRA hired the Neligan Law Firm to advise on bankruptcy and restructuring options.²⁴ The next day, Sea Girt, LLC was formed as a transition vehicle to facilitate the NRA's relocation to Texas.²⁵

On January 7, 2021, the NRA held a board meeting. At this meeting, the board of directors adopted a resolution formalizing the Special Litigation Committee.²⁶ The board of directors also passed a resolution approving an employment agreement for Mr. LaPierre.²⁷ Significantly, Mr. LaPierre's employment agreement contained language permitting Mr. LaPierre to "exercise corporate authority in furtherance of the mission and interests of the NRA, including without limitation to reorganize or restructure the affairs of the Association for the purposes of cost-minimization, regulatory compliance or otherwise."²⁸ Throughout the entirety of the board meeting, both in the general and executive sessions, no discussion of bankruptcy, Chapter 11, or the possible reorganization of the NRA occurred.²⁹ The board of directors was not informed that the language cited above could authorize Mr. LaPierre to unilaterally authorize a petition for bankruptcy relief for the NRA. In fact, the board of directors was not informed that the NRA was considering filing for bankruptcy at all.³⁰

On January 15, 2021, the NRA and Sea Girt, LLC filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. The cases are being jointly administered.³¹ On February 8,

²⁴ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 98:9-99:25; NYAG Exhibit 298.

²⁵ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 89:3-10; NYAG Exhibit 347.

²⁶ NYAG Exhibits 2, 3.

²⁷ NYAG Exhibit 3.

²⁸ NYAG Exhibit 50.

²⁹ *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 92:1-93:10; *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 76:15-21; *Transcript of Hearing Held April 8, 2021* [Docket No. 544] at 92:24-93:4.

³⁰ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 118:8-16; *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 47:7-10; *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 85:24-86:16.

³¹ *Order Granting Debtors' Emergency Motion for Joint Administration of Chapter 11 Cases* [Docket No. 36].

2021, Judge Phillip Journey,³² a longtime member, donor, and director of the NRA, filed a motion seeking the appointment of an examiner with special duties and powers under section 1104(c) of the Bankruptcy Code to investigate the governance of the NRA and the actions of its management (the “Examiner Motion”).³³ The Examiner Motion was originally set for hearing on March 9, 2021.³⁴

On February 10, 2021, Ackerman, now a former vendor and current litigation adversary of the NRA, filed a motion to dismiss the Chapter 11 case or, in the alternative, appoint a Chapter 11 trustee pursuant to section 1104(a) of the Bankruptcy Code.³⁵ The motion to dismiss filed by Ackerman was quickly followed by similar motions filed by the NYAG³⁶ and the District of Columbia attorney general³⁷ (the “Motions to Dismiss”) and a joinder filed by Christopher W. Cox, a former executive director of the NRA Institute for Legislative Action.³⁸ Because of the overlapping facts and interrelated relief being requested in the Examiner Motion and the Motions to Dismiss, the Court chose to set them for trial together after a brief period of time for expedited discovery.

³² Judge Phillip Journey currently serves as the Division 1 Judge of the 18th Judicial District Court of Kansas.

³³ *Motion for Appointment of Examiner* [Docket No. 114].

³⁴ *See Notice of Hearing* [Docket No. 130].

³⁵ *Ackerman McQueen, Inc.’s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, and Brief in Support* [Docket No. 131].

³⁶ *The State of New York’s Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee* [Docket No. 155]; *The State of New York’s Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee* [Docket No. 163].

³⁷ *The District of Columbia’s Motion in Support in the State of New York’s Motion to Appoint Chapter 11 Trustee* [Docket No. 214]; *The District of Columbia’s Motion in Support in the State of New York’s Motion to Dismiss* [Docket No. 429].

³⁸ *Christopher W. Cox’s Joinder to (I) the Motions to Dismiss or, in the Alternative, to Appoint a Chapter 11 Trustee Filed by Ackerman McQueen, Inc. and the State of New York, or (II) the Motion of Phillip Journey for Appointment of an Examiner* [Docket No. 172].

In the following weeks, the many parties involved in this case—each with different interests, perspectives, and goals—engaged in discovery and began to take positions on the motions filed and the various relief requested therein. Judge Journey filed an objection to the Motions to Dismiss but amended his previous request for an examiner to include an expanded role for the proposed examiner.³⁹ The Official Committee of Unsecured Creditors (the “Committee”) took the position that while the NRA is in need of major changes to its governance, current management should not be displaced by a Chapter 11 trustee, but if a trustee is appointed, they should have limited powers. The Committee also took the position that the NRA should retain a chief restructuring officer and that the appointment of an examiner was not necessary because the Committee was already fulfilling that role.⁴⁰

The NRA opposed all of the motions but did eventually consent to the appointment of a chief restructuring officer.⁴¹

David Dell’Aquila, a member of the Committee and the plaintiff in a purported class action against the NRA, filed a partial joinder opposing dismissal but supporting the appointment of a Chapter 11 trustee with limited authority.⁴²

³⁹ *Limited Objection to the Motions to Dismiss or the Appointment of Trustee* [Docket No. 306].

⁴⁰ *The Official Committee of Unsecured Creditors’ Objection to the Motion for Appointment of an Examiner* [Docket No. 354]; *The Official Committee of Unsecured Creditors’ Omnibus Response to (I) Ackerman McQueen, Inc.’s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, and Brief in Support, (II) the State of New York’s Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee, and (II) the District of Columbia’s Motion in Support in the State of New York’s Motion to Appoint Chapter 11 Trustee* [Docket No. 368].

⁴¹ *Omnibus Opposition to (1) Ackerman McQueen, Inc.’s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, (2) the State of New York’s Motion to Dismiss or, in the Alternative, to Appoint Chapter 11 Trustee, and (3) the District of Columbia’s Motion to Appoint Chapter 11 Trustee* [Docket No. 307]; *Debtor’s Response in Opposition to the Motion for Appointment of an Examiner Filed by Phillip Journey* [Docket No. 358].

⁴² *David Dell’Aquila’s Partial Joinder to (I) Ackerman McQueen, Inc.’s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, and Brief in Support, (II) the State of New York’s Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee, (III) the District of Columbia’s Motion in Support in the State of New York’s Motion to Appoint Chapter 11 Trustee, and (IV) the Official Committee of Unsecured Creditors Motion in Response to (I), (II), and (III)* [Docket No. 415].

The United States Trustee did not initially express an opinion regarding the underlying motions but did express views on several of the options the parties had discussed.⁴³ Specifically, the United States Trustee took the position that there is no such entity as a limited purpose trustee under the Bankruptcy Code, and if the Court orders the appointment of a Chapter 11 trustee, the trustee must have full statutory powers. The United States Trustee also took the position that while an examiner may be granted expanded powers, the Bankruptcy Code does not permit a chief restructuring officer to usurp the powers of a Chapter 11 trustee.⁴⁴

Sixteen states, as *amici curiae*, filed a brief in support of the NRA,⁴⁵ and the state of Texas submitted its own brief in support of the NRA.⁴⁶

Trial commenced on April 5, 2021 and continued over twelve days with twenty-three witnesses. On April 7, 2021, the NRA filed an application to employ a chief restructuring officer,⁴⁷ which the Court heard concurrently with the ongoing trial. Closing arguments took place on May 3, 2021, after which the Court took the matters under advisement.

⁴³ In closing arguments following trial, the United States Trustee took the position that the evidence supports dismissal, the appointment of a trustee, or the appointment of an examiner.

⁴⁴ *United States Trustee's Statement Regarding Motions Seeking Appointment of Examiner, Trustee, or Case Dismissal* [Docket No. 405].

⁴⁵ *Brief of the States of Arkansas, Alabama, Alaska, Georgia, Idaho, Kentucky, Louisiana, Mississippi, Missouri, Montana, Ohio, Oklahoma, South Carolina, South Dakota, Utah, and West Virginia as Amici Curiae in Support of Debtors; and in Opposition to the State of New York's Motion to Dismiss, or in the Alternative to Appoint a Chapter 11 Trustee* [Docket No. 445].

⁴⁶ *Brief of the State of Texas as Amicus Curiae in Support of Debtors; and in Opposition to the State of New York's Motion to Dismiss, or in the Alternative to Appoint a Chapter 11 Trustee* [Docket No. 465].

⁴⁷ *Application of the Debtors for an Order Authorizing the Retention and Employment of Ankura Consulting Group, LLC and Appointment of Louis E. Robichaux IV as the Debtors' Chief Restructuring Officer* [Docket No. 519] (the "CRO Motion").

III. Applicable Legal Standard

The movants generally seek three forms of relief: dismissal of the bankruptcy cases, the appointment of a Chapter 11 trustee, or the appointment of an examiner. Pursuant to section 1112(b) of the Bankruptcy Code, the court shall dismiss a case under this chapter for cause unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.⁴⁸ Section 1112(b)(4) contains a non-exclusive list of what constitutes “cause” for purposes of dismissal, but the Fifth Circuit Court of Appeals has held that the term “cause” affords flexibility to the bankruptcy courts and can include a finding that the debtor’s filing for relief is not in good faith. *In re Little Creek Dev. Co.*, 779 F.2d 1068, 1072-73 (5th Cir. 1986); *In re Humble Place Joint Venture*, 936 F.2d 814, 816-17 (5th Cir. 1991).

After the movant satisfies the initial burden of making a prima facie showing of a lack of good faith in filing, the burden shifts to the debtor to demonstrate good faith. *In re Mirant Corp.*, 2005 Bankr. LEXIS 1686, at *27 n.20 (Bankr. N.D. Tex. Jan. 26, 2005) (noting that some courts hold that the burden of showing good faith is on the debtor while other courts hold that the movant has an initial burden to present a prima facie case of a lack of good faith before the burden shifts to the debtor to show good faith); *In re Sherwood Enters., Inc.*, 112 B.R. 165, 170-71 (Bankr. S.D. Tex. 1989). Furthermore, courts have held that a Chapter 11 petition is not filed in good faith unless it serves a valid bankruptcy purpose. *Off. Comm. of Unsecured Creditors v. Nucor Corp. (In re SGL Carbon Corp.)*, 200 F.3d 154, 165 (3d Cir. 1999).

If a court finds cause for dismissal, it must dismiss the case unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of

⁴⁸ Section 1112(b) also requires consideration of whether conversion to a case under chapter 7 would be in the best interests of creditors and the estate, but pursuant to section 1112(c), in cases where the debtor is a nonprofit, the court may not convert a case under chapter 11 to a case under chapter 7 unless the debtor requests such a conversion. The NRA has not requested such a conversion, so the Court need not consider it in this case.

creditors and the estate. Pursuant to section 1104(a), at any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States Trustee, and after notice and a hearing, the court shall order the appointment of a trustee (1) for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause, but not including the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor; or (2) if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate, without regard to the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor.

Pursuant to section 1104(c), if the court does not order the appointment of a trustee, then at any time before the confirmation of a plan, on request of a party in interest or the United States Trustee, and after notice and a hearing, the court shall order the appointment of an examiner to conduct such an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor, if (1) such appointment is in the interests of creditors, any equity security holders, and other interests of the estate or (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.

IV. Discussion

Because of the structure of the relevant provisions of the Bankruptcy Code, the Court will first determine whether there is cause for dismissal and, specifically, whether the NRA filed for bankruptcy in good faith.

The NRA's Stated Reasons for Filing Bankruptcy

At various times in this case, the NRA has provided the Court with several—and at times slightly different—reasons for why this bankruptcy case was filed.⁴⁹ In an informational brief filed on January 20, 2021, the NRA explained that it “instituted this chapter 11 reorganization proceeding to establish a centralized, neutral forum in which it can streamline, resolve, and address all outstanding claims and preserve its ability to pursue its constitutionally protected mission as a going concern” and that it “intends to restructure through a plan of reorganization that provides for the reorganized NRA to emerge from these chapter 11 cases as a Texas nonprofit entity.”⁵⁰ The NRA went on to explain that “separate and apart from the on-going disputes with the NYAG, the NRA seeks to avail itself of the protections of the Bankruptcy Code in order to continue its efforts to reduce operating costs and to address the ever-increasing litigation being filed against the NRA” and that “[c]ontrary to the NYAG’s press releases, the NRA is not seeking to evade regulatory oversight; rather it seeks, and is entitled, to being treated fairly by regulators providing that oversight.”⁵¹ Finally, the NRA announced its intention to propose a plan of reorganization that will (1) pay all of the allowed claims of the NRA’s creditors in full, (2) provide a mechanism for adjudicating and/or resolving the claims of the NYAG and any other creditor with contingent,

⁴⁹ In its discussion, the Court will focus on the NRA rather than Sea Girt, LLC. Sea Girt, LLC has no employees or operations and was formed to accomplish a shared bankruptcy purpose with the NRA.

⁵⁰ *Debtors’ Informational Brief in Connection with Voluntary Chapter 11 Petitions* [Docket No. 31] at ¶¶ 3, 6.

⁵¹ *Id.* at ¶ 26.

unliquidated, and disputed claims, and (3) allow the NRA to exit Chapter 11 as a Texas nonprofit organization.⁵²

Counsel for the NRA reiterated these reasons at the hearing held on January 20, 2021, with a particular emphasis on (1) the cost of ongoing litigation and the time and effort of the NRA management team being spent on litigation, (2) the need for a breathing spell and an opportunity to centralize litigation, and (3) the NRA's desire to emerge from bankruptcy as a company domiciled in Texas.⁵³ Counsel for the NRA went so far as to say that "absent being able to streamline discovery and have all of this litigation, or much of it, handled in a centralized forum, the NRA was indeed facing the adage, death by a thousand cuts."⁵⁴

In the Examiner Motion and the Motions to Dismiss, the other parties offered different opinions on the true purpose of the NRA's bankruptcy. Judge Journey took the position that if the NRA was able to successfully terminate its corporate existence in New York and reconstitute the organization under Texas law, the NRA wishes to "avoid the ongoing challenges to its corporate charter brought by the State of New York and other ongoing litigation."⁵⁵ Ackerman accused the NRA of primarily using the bankruptcy filing to escape civil prosecution and avoid regulatory oversight from the NYAG, but also to stall litigation.⁵⁶ The NYAG agreed with Ackerman that the NRA's purpose in filing bankruptcy was to evade regulatory oversight.⁵⁷

⁵² *Id.* at ¶ 27.

⁵³ *Transcript of Hearing Held January 20, 2021* [Docket No. 55] at 11:8-17, 12:1-14:9, 15:2-6.

⁵⁴ *Id.* at 12:19-23.

⁵⁵ *Motion for Appointment of Examiner* [Docket No. 114] at 2.

⁵⁶ *Ackerman McQueen, Inc.'s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, and Brief in Support* [Docket No. 131] at ¶¶ 2, 29-31.

⁵⁷ *The State of New York's Memorandum of Law and Brief in Support of Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee* [Docket No. 156] at ¶¶ 3, 20, 24.

In its brief in opposition to the Examiner Motion and the Motions to Dismiss, the NRA again summarized its reasons for filing bankruptcy, but in a slightly more expansive way:

On January 15, 2021, the Debtors filed their chapter 11 petitions with a series of goals:

- a. The Debtors seek to streamline the barrage of litigation they are facing. Although the Debtors expect to ultimately prevail on the merits in many pending cases, the disruption and expense of such litigation creates significant burdens for the NRA.
- b. The organizational structure of the NRA is based on a 150-year-old charter that has not been updated in over a century. Given the size and impact that the NRA now has, the organization would benefit from the modernization to ensure its continued existence as a going concern for the benefit of the NRA's creditors and members.
- c. While this case is certainly unique, ultimately, the NRA is not unlike a typical chapter 11 debtor grappling with the typical operational strains with which chapter 11 is designed to assist. The NRA seeks to reduce operating expenses, address burdensome executory contracts and unexpired leases, maintain its employees and operations, and institute and effectuate a streamlined claims process to address the multitude of claims and repayment through a confirmed plan of reorganization.
- d. The NRA seeks to move its corporate domicile and its principal place of business to Texas which, as has been widely reported, welcomes the NRA with open arms.⁵⁸

Later in the brief, the NRA acknowledged that there is no judgment against it and no impending trial but expressed the belief that it faces existential threats:

The NRA filed for protection under chapter 11 in good faith, not to circumvent judgments in other courts (in fact, no judgments have been rendered), nor to escape an impending trial (because there is none), but because it is in a situation where it must be able to continue its operations in the face of existential threats, in order to maximize the value of its estate and to protect the interests of its members, employees, vendors, and legitimate creditors.⁵⁹

⁵⁸ *Omnibus Opposition to (1) Ackerman McQueen, Inc.'s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, (2) the State of New York's Motion to Dismiss or, in the Alternative, to Appoint Chapter 11 Trustee, and (3) the District of Columbia's Motion to Appoint Chapter 11 Trustee* [Docket No. 307] at p. 13, ¶ 40.

⁵⁹ *Id.* at p. 25, ¶ 38.

In its briefing, the Committee seemed to agree that the NRA's primary goal was to avoid dissolution in the NYAG Enforcement Action but did not find this to be an improper motive and also saw other benefits for the NRA in bankruptcy:

In seeking the dismissal of these Chapter 11 Cases, the Moving Parties conflate the concept of litigation gamesmanship with prudent liability management. The Debtors filed these bankruptcy cases not to gain a tactical litigation advantage, but to implement a strategy *to survive* in the event of a potential adverse ruling in the NYAG Action. As described below, there could not be a more fundamental and proper use of the federal bankruptcy laws than preservation of and as a going-concern.

....

In addition to protecting the NRA from dissolution, these Chapter 11 Cases also offer the NRA an opportunity to implement corporate governance changes that will promote transparency and increase public confidence in the way the NRA handles its finances, conducts business with vendors and customers, and safeguards against future mismanagement.⁶⁰

In the NRA's opening statement at trial, the stated reasons for filing bankruptcy were significantly narrower than in the NRA's briefing and appeared to focus heavily on the NYAG Enforcement Action:

The exclusive testimony as to good faith will be we had three goals in mind. First, avoid the death penalty. Avoid dissolution. Two, avoid a receiver in a New York state court that would deny us the ability to file. And third, we wholly embrace our third goal. Our third goal is to [. . .] remove ourselves from New York and relocate ourselves to Texas.⁶¹

It is against this backdrop that the Court evaluates the evidence presented at trial regarding the NRA's reasons for filing bankruptcy.

⁶⁰ *The Official Committee of Unsecured Creditors' Omnibus Response to (I) Ackerman McQueen, Inc.'s Motion to Dismiss the Chapter 11 Bankruptcy Petition, or, in the Alternative, Motion for the Appointment of a Chapter 11 Trustee, and Brief in Support, (II) the State of New York's Motion to Dismiss, or, in the Alternative, to Appoint a Chapter 11 Trustee, and (III) the District of Columbia's Motion in Support in the State of New York's Motion to Appoint Chapter 11 Trustee* [Docket No. 368] at ¶¶ 24, 31 (emphasis in original).

⁶¹ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 40:25-41:7.

Evidence of the NRA's Reasons for Filing Bankruptcy

The parties elicited testimony from several witnesses regarding the NRA's reasons for filing bankruptcy, but the way in which the Court has weighed that evidence is based on the somewhat unusual way in which this case was filed. There was no vote on whether the NRA should file for bankruptcy, and therefore there is no need to resolve inconsistent or conflicting reasoning and motivations of individuals who all had an equal say in the decision. Rather, the ultimate decision to file for bankruptcy was made solely by Mr. LaPierre.⁶² As a result, Mr. LaPierre's testimony is the most direct, and, since the Court finds it credible on this topic, the most compelling evidence for why the NRA filed for bankruptcy, but it is not the only evidence to consider.⁶³ Mr. LaPierre consulted the three members of the Special Litigation Committee about the decision to file bankruptcy before it was made,⁶⁴ so their knowledge of the decision-making process is also relevant. The only other person within the NRA who appears to have known about the decision to file bankruptcy prior to the actual filing was the NRA spokesman,⁶⁵ but he did not testify. Neither the NRA's treasurer and then-CFO nor the NRA's current acting CFO were consulted about the decision to file bankruptcy, and they only learned of the decision after bankruptcy was filed.⁶⁶ Nevertheless, they were both able to offer helpful testimony regarding

⁶² *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 84:8-19; *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 68:1-8, 70:12-72:23.

⁶³ See *Elmwood Dev. Co. v. Gen. Elec. Pension Tr. (In re Elmwood Dev. Co.)*, 964 F.2d 508, 512 (5th Cir. 1992) ("Because the good faith standard is an objective one, the court was not constrained to entertain and give dispositive weight to testimony of the subjective state of mind of [the debtor's] manager."); *In re Little Creek Dev. Co.*, 779 F.2d 1068, 1072-73 (5th Cir. 1986) (stating that in determining whether a debtor's filing for relief is in good faith, courts must consider a conglomerate of factors, including motives).

⁶⁴ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 84:8-85:11; *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 36:18-23; NYAG Exhibit 4 at 5-10.

⁶⁵ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 72:11-23.

⁶⁶ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 70:12-17; *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 119:23-120:1; *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 49:7-11; *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 54:12-21; *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 85:19-22.

potential reasons for the bankruptcy, including the cost of litigation and the financial condition of the NRA. The NRA's general counsel also offered testimony regarding reasons for the NRA to file for bankruptcy, but he did not participate in the actual decision-making process and did not know about the decision to file bankruptcy until bankruptcy had already been filed.⁶⁷

There was a general consensus among the witnesses that, as the NRA has consistently represented to the Court and to its members, the NRA is in its strongest financial condition in years⁶⁸ and intends to pay creditors all allowed claims in full.⁶⁹ The CFO at the time of the bankruptcy filing, Mr. Spray, testified that there was no financial reason for the NRA to file bankruptcy,⁷⁰ but he later qualified that testimony by noting that he did not have any information about potential litigation outcomes.⁷¹ The current acting CFO, Ms. Rowling, gave supporting testimony regarding the financial strength of the NRA and its ongoing ability to pay its creditors⁷² and testified that the NRA has sufficient funds to prosecute and defend its current litigation.⁷³ Ms. Rowling also testified, however, that it was her opinion that the NRA was in bankruptcy because of potential litigation losses that could severely impact the organization's financial position.⁷⁴

⁶⁷ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 118:17-119:21; *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 43:19-44:8.

⁶⁸ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 78:16-81:2; *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 32:24-33:2; *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 160:24-161:2; *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 33:12-14, 34:13-21; *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 51:21-53:13; NYAG Exhibit 151.

⁶⁹ *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 32:9-17; *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 52:22-53:5.

⁷⁰ *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 53:11-13, 129:17-130:20, 132:22-133:4.

⁷¹ *Transcript of Hearing Held April 16, 2021* [Docket No. 620] at 19:10-16.

⁷² *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 33:12-14, 34:13-21, 36:17-38:14.

⁷³ *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 39:17-23.

⁷⁴ *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 34:22-35:1.

The testimony of the NRA’s general counsel, Mr. Frazer, on the reasons for filing bankruptcy was, in some respects, a bit difficult to reconcile. Despite not being involved in the decision to file for bankruptcy and not knowing about the decision until after bankruptcy was filed,⁷⁵ Mr. Frazer was designated as the corporate representative of the NRA as to the reasons, both financial and non-financial, for the NRA seeking protection under Chapter 11 of the Bankruptcy Code.⁷⁶ During his deposition, the only reasons for filing bankruptcy that Mr. Frazer identified were to streamline litigation, consolidate the claims against the NRA, and reorganize in Texas.⁷⁷ Mr. Frazer did not identify avoiding dissolution or avoiding receivership as reasons for the NRA filing bankruptcy at that time.⁷⁸ Nevertheless, Mr. Frazer testified at trial that he agreed the bankruptcy filing allowed the NRA to seek protection from regulators in New York.⁷⁹

With regard to the threats of dissolution or a receiver being appointed, it is clear that the NYAG was seeking dissolution of the NRA.⁸⁰ Nevertheless, Mr. Frazer was not sure if a trial date is currently set in the NYAG Enforcement Action but anticipated a trial early next year and acknowledged that dissolution is not imminent.⁸¹ Mr. Frazer also acknowledged having no personal knowledge of an imminent threat of a receiver being appointed over the NRA.⁸² With regard to streamlining litigation, Mr. Frazer reaffirmed that it is one of the NRA’s reasons for filing

⁷⁵ *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 43:19-44:8, 109:22-24.

⁷⁶ *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 17:5-14.

⁷⁷ *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 17:15-20, 57:8-25.

⁷⁸ *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 20:20-21:1.

⁷⁹ *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 107:22-108:6; *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 21:12-19.

⁸⁰ See NYAG Exhibit 107 (NYAG Complaint in which the first two causes of action are labeled “Dissolution of the NRA”).

⁸¹ *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 29:10-30:6, 30:19-22.

⁸² *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 33:18-34:11.

bankruptcy⁸³ but acknowledged that he has not conducted an analysis, and was not aware of anyone else conducting an analysis, of the cost of proceeding with litigation outside of bankruptcy versus the cost of the bankruptcy and proceeding with the litigation in the bankruptcy case.⁸⁴ Mr. Frazer also testified that the NRA previously filed a motion for centralization of four pending actions that was denied by the United States Judicial Panel on Multidistrict Litigation on the basis that they were not persuaded that centralization was necessary for the convenience of the parties and witnesses or to further the just and efficient conduct of the litigation.⁸⁵

The Court received testimony from all three members of the Special Litigation Committee, but their testimony did not explore the reasons for filing bankruptcy in much depth. The parties offered excerpts of the deposition of Ms. Meadows, but those excerpts did not include a discussion of why the NRA filed for bankruptcy. Colonel Lee testified that he understood the NYAG had sought the appointment of a receiver to seize the NRA's assets and that if a receiver were appointed over the NRA, it would be disastrous.⁸⁶ Mr. Cotton testified that he believed there was a risk that the NYAG could attempt to put the NRA into receivership because the first cause of action in the NYAG Complaint was for dissolution.⁸⁷ Mr. Cotton further testified that dissolution in the NYAG Enforcement Action was a legitimate risk that the NRA was concerned about.⁸⁸

During trial, Mr. LaPierre was questioned several times regarding why the NRA filed for bankruptcy. In response to a question of whether the NRA filed bankruptcy to leave New York, Mr. LaPierre testified that the NRA filed bankruptcy to look for a fair legal playing field where

⁸³ *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 109:2-11.

⁸⁴ *Transcript of Hearing Held April 6, 2021* [Docket No. 692] at 112:19-113:1.

⁸⁵ *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 36:20-38:12; Ackerman Exhibit 121.

⁸⁶ *Transcript of Hearing Held April 21, 2021* [Docket No. 673] at 45:10-46:2.

⁸⁷ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 37:3-7.

⁸⁸ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 38:15-39:10.

the NRA could prosper and grow in a fair legal environment⁸⁹ and later testified that the NRA needs the approval of a federal court to move to a new state.⁹⁰ At one point, Mr. LaPierre was presented with a series of communications informing the NRA's members, the NRA's board of directors, and the general public that the NRA had filed for bankruptcy and asked if the contents of those communications were accurate, which Mr. LaPierre testified they were.⁹¹ The communications, which were prepared by the NRA's Managing Director of Public Affairs working with a member of the Brewer Firm,⁹² described a variety of reasons for why the NRA filed bankruptcy, including leaving New York and reincorporating in Texas, seeking protection from New York officials, streamlining legal and financial affairs, organizing pending litigation in a coordinated and structured manner, and realizing other financial and strategic advantages. In one of the communications, a question and answer page posted on the NRA's website, the NRA states: "This action is necessitated primarily by one thing: the unhinged and political attack against the NRA by the New York Attorney General."⁹³ With regard to the risk of a receiver being appointed, Mr. LaPierre testified that the NRA has not been put on notice that the NYAG intends to seek a receivership and he does not have any facts to suggest that there is an imminent threat of a receiver being appointed.⁹⁴

The most helpful testimony from Mr. LaPierre came during an exchange when counsel for one of the movants was attempting to discern which of the many reasons for filing for bankruptcy

⁸⁹ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 66:11-23.

⁹⁰ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 42:23-43:4.

⁹¹ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 67:14-25 (affirming the accuracy of NYAG Exhibit 153); *id.* at 86:18-21 (affirming the accuracy of NYAG Exhibit 55); *id.* at 87:5-18 (affirming the accuracy of NYAG Exhibit 151); *id.* at 87:22-88:8 (affirming the accuracy of NYAG Exhibit 208).

⁹² *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 88:1-4.

⁹³ NYAG Exhibit 208.

⁹⁴ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 21:8-22:1.

that have been discussed was the real driving force behind Mr. LaPierre's decision. A few very valuable pieces of information came from that exchange. After establishing that the bankruptcy filing was not related to the NRA's financial condition,⁹⁵ Mr. LaPierre acknowledged that although the cost of defending the NYAG Enforcement Action was significant, the cost of bankruptcy is high as well.⁹⁶ Mr. LaPierre then confirmed that if the NRA's bankruptcy case is dismissed, the NRA would be able to pay its debts in full and meet its obligations.⁹⁷ The exchange continued:

Q: Okay. So it comes down to the reason you filed Chapter 11 is because you have this New York attorney general enforcement action which is asking for dissolution of the NRA; is that correct?

[Counsel for the NRA]: Objection; misstates his testimony.

[Counsel for the Movant]: Well --

THE COURT: Well, I'm going to go ahead and let him answer that. Try to give an answer to that, Mr. LaPierre.

THE WITNESS: Yes, Your Honor. Yes, we filed the Chapter 11 to -- because the New York State attorney general is seeking dissolution of the NRA and [seizure of] its assets, and we believe it's not a fair, level playing field.

....

Q: So really what we're down to is that it's -- the New York attorney general action is the reason you believe you need to be in bankruptcy, and, really, solvency and all your other litigation, those are not issues that would require you to be in bankruptcy; is that correct?

A: That's correct.

Transcript of Hearing Held April 8, 2021 [Docket No. 654] at 33:19-34:20.

⁹⁵ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 32:9-20.

⁹⁶ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 32:15-23.

⁹⁷ *Transcript of Hearing Held April 8, 2021* [Docket No. 654] at 32:24-33:2.

The Court's Determination of the NRA's Primary Reason for Filing Bankruptcy

The evidence does not support a finding that the purpose of the NRA's bankruptcy filing was to reduce operating costs, to address burdensome executory contracts and unexpired leases, to modernize the NRA's charter and organization structure, or to obtain a breathing spell. While some of these could be added benefits of going through a bankruptcy process, they do not appear to have been significant considerations for the NRA.

There was some evidence that the NRA wants to streamline litigation and control litigation costs, but this does not appear to have been the real purpose behind filing for bankruptcy. Ms. Rowling testified that she believes the NRA is in bankruptcy because of potential litigation losses, but this concern did not appear to be shared by Mr. LaPierre or supported by other evidence. The testimony regarding the ongoing cost of litigation was that the NRA is currently able to afford to pay its legal fees and that there has not been an analysis of the cost of proceeding with litigation outside of bankruptcy versus the cost of the bankruptcy and proceeding with the litigation in the bankruptcy case. Furthermore, Mr. LaPierre testified that but for the NYAG Enforcement Action, it would not have been necessary to file for bankruptcy.

Whether the NRA's desire to leave New York and reincorporate in Texas was a true reason for filing bankruptcy is a closer call, but the evidence weighs in favor of a finding that it was not the real purpose for filing for bankruptcy. Several witnesses testified that New York is a hostile environment for the NRA,⁹⁸ but the testimony was that individuals within the organization had been interested in leaving New York and reincorporating in Texas for a long time.⁹⁹ The choice

⁹⁸ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 16:23-25; *Transcript of Hearing Held April 21, 2021* [Docket No. 670] at 7:25-8:12; *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 37:14-38:9; *Transcript of Hearing Held April 13, 2021* [Docket No. 584] at 146:1-8; *Transcript of Hearing Held April 7, 2021* [Docket No. 559] at 22:10-13; *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 66:11-20.

⁹⁹ *Transcript of Hearing Held April 6, 2021* [Docket No. 499] at 37:8-38:14.

to attempt to do so now—and to do so through a bankruptcy reorganization—appears to have been a means of achieving the more specific purpose of avoiding dissolution in the NYAG Enforcement Action.

In closing arguments at the conclusion of trial, there was a suggestion that part of the desire to move to Texas, and therefore part of the reason for filing bankruptcy, was due to the NRA having increasing difficulty with its relationships with financial institutions because of the NY DFS Letter.¹⁰⁰ The specific evidence on this topic came from Mr. Spray, who testified that he “didn’t know exactly what the catalyst was for their angst,” but that the NRA’s relationships with banks when Mr. Spray joined the NRA were tenuous and he had to find more enthusiastic banking support.¹⁰¹ Mr. Spray also testified that it was becoming difficult to get insurance when he joined the NRA and that problem has only gotten worse.¹⁰² Counsel for the NRA characterized this as an existential threat that the NRA was facing before the NYAG Enforcement Action was pending and a reason for filing bankruptcy to move to Texas. There are a few reasons the Court is skeptical of this argument. The first is one of timing. The NY DFS Letter was sent in April 2018, and the NRA filed its lawsuit over alleged interference with its banking and insurance relationships in May 2018. The speed with which the NRA sought relief by filing a complaint in the Northern District of New York and the delay in filing bankruptcy, over two years later, suggests the purpose of the bankruptcy was related to something else. Moreover, the general testimony was that financial reasons did not drive the bankruptcy filing. The Court understands how this might not fall into the category of current financial health when asking most people at the NRA, but even Mr. Spray, who was fully aware of the banking and insurance relationships, testified that he was not aware of any

¹⁰⁰ The NY DFS Letter is attached to NRA Exhibit 663.

¹⁰¹ *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 153:18-154:20.

¹⁰² *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 154:21-155:9.

reasons to file for bankruptcy. If the deterioration of banking and insurance relationships is an existential threat and an important reason for filing bankruptcy, one would think Mr. Spray would have been consulted, but he was not consulted on—or even informed of—the decision to file for bankruptcy.

With regard to receivership, there was no evidence to suggest that it was an imminent threat, and the witnesses only appear to have been concerned about receivership in the context of dissolution being granted. In other words, the witnesses appeared to be conflating the appointment of a receiver and dissolution when dissolution was the real concern. As far as the Court can tell, the appointment of a receiver was never requested by the NYAG in the NYAG Complaint or elsewhere. There was a statement in a press conference held by the NYAG that she may attempt to freeze assets,¹⁰³ but this comment appeared to relate to finding hidden assets and, in any event, none of the witnesses testified that this caused them concern that a receiver would be appointed. It is possible that if the NYAG had become aware that the NRA was preparing to file for bankruptcy, the NYAG could have attempted to have a receiver appointed on an expedited basis, but that would only be a reason for the NRA to go to extreme lengths to avoid leaks about its intention to file bankruptcy and not a reason for the bankruptcy filing itself.

Though articulated slightly differently, the remaining reasons for filing bankruptcy, such as preserving the NRA as a going concern, can be grouped under the general reason of avoiding dissolution in the NYAG Enforcement Action. Based on the statements of counsel and the evidence in the record, the Court finds that the primary purpose of the bankruptcy filing was to avoid potential dissolution in the NYAG Enforcement Action.

¹⁰³ NRA Exhibit 675.

Analysis of Whether the NRA Filed Bankruptcy to Achieve a Valid Bankruptcy Purpose

Having identified the purpose of the NRA’s bankruptcy filing, the Court must now decide whether it was a valid purpose for bankruptcy such that the bankruptcy was filed in good faith. The Fifth Circuit Court of Appeals has offered guidance on how courts should approach the good faith inquiry:

Determining whether the debtor’s filing for relief is in good faith depends largely upon the bankruptcy court’s on-the-spot evaluation of the debtor’s financial condition, motives, and the local financial realities. Findings of lack of good faith in proceedings based on §§ 362(d) or 1112(b) have been predicated on certain recurring but non-exclusive patterns, and they are based on a conglomerate of factors rather than on any single datum.

In re Little Creek Dev. Co., 779 F.2d 1068, 1072 (5th Cir. 1986).¹⁰⁴ The Third Circuit Court of Appeals has stated that almost every federal Court of Appeals follows some variation of this “totality of the circumstances” approach to the good faith filing requirement for Chapter 11 petitions. *In re 15375 Mem’l Corp.*, 589 F.3d 605, 618 n.7 (3d Cir. 2009). In that same case, the Third Circuit went on to note that they focus on two inquiries that are particularly relevant to the question of good faith: (1) whether the petition serves a valid bankruptcy purpose and (2) whether the petition is filed merely to obtain a tactical litigation advantage. *Id.* at 618.

The Court has great concern about this case because its purpose is to avoid dissolution that is being sought as a remedy in a state regulatory action. It has been asserted that this case is about preserving the NRA as a going concern, which is a very common good faith reason for filing bankruptcy. There is a difference, however, between a lawsuit in which a party seeks a monetary judgment that would pose an existential threat to a debtor and one where the attorney general of a

¹⁰⁴ The Fifth Circuit also identified several conditions that usually exist in filings that are not made in good faith. *Id.* at 1072-73. Because of the unusual circumstances of this case, the Court considered the *Little Creek* factors but did not structure its discussion around them.

state is specifically seeking dissolution of a debtor under the state's laws and therefore required to satisfy standards and requirements that specifically justify dissolution.

The New York Legislature constructed a regulatory system under which charities would be dissolved under certain circumstances. In this situation, the NRA is financially healthy, and the only way that the NRA will be dissolved is if it is determined in the New York court system that the requirements in Article 11 of the New York Not-For-Profit Corporation Law have been met. The NYAG has requested dissolution of the NRA under two different statutory provisions and acknowledged the high burden that it must meet:

But New York law does not allow the NYAG to summarily dissolve a charity, but rather place[s] a burden upon the NYAG to prove to a court that dissolution is called for under the law in a given circumstance.

With respect to N-PCL § 1101, the Attorney General must show a regulated entity's misconduct "has produced, or tends to produce, injury to the public. The transgression must not be merely formal or incidental, but material and serious, and such as to harm or menace the public welfare." *People v. Oliver Schools, Inc.*, 206 A.D.2d 143, 145 (4th Dep't 1994) (interpreting BCL § 1101, from which N-PCL § 1101 is derived) (quoting *People v. North River Sugar Refining Co.*, 121 N.Y. 582, 609 (1890)). . . .

With respect to Dissolution under N-PCL § 1102, the Attorney General stands in the shoes of the NRA's members and, as relevant here, must prove that the "directors or members in control of [the NRA] have looted or wasted the corporate assets, have perpetuated the corporation solely for their personal benefit, or have otherwise acted in an illegal, oppressive or fraudulent manner." N-PCL § 1102(a)(2)(D); 112(a)(7).

The State of New York's Omnibus Reply to Debtors' Opposition and the Committee's Response to Motion to Dismiss or Appoint a Trustee [Docket No. 459] at ¶ 17. A dissolution that requires this showing is not the type of dissolution that the Bankruptcy Code is meant to protect against. The Court is not in any way saying it believes the NYAG can or cannot make the required showing to obtain dissolution of the NRA, but the Court is saying that the Bankruptcy Code does not provide sanctuary from this kind of a threat.

For this reason, the Court believes the NRA’s purpose in filing bankruptcy is less like a traditional bankruptcy case in which a debtor is faced with financial difficulties or a judgment that it cannot satisfy and more like cases in which courts have found bankruptcy was filed to gain an unfair advantage in litigation or to avoid a regulatory scheme. The purpose of this bankruptcy filing may not have been to end the NYAG Enforcement Action immediately, but it was to deprive the NYAG of the remedy of dissolution, which is a distinct litigation advantage. This differs materially from the prescribed parallel proceedings structure for regulatory actions where regulators can obtain monetary judgments in one forum and then are required to have any claims treated through a bankruptcy process in that it is the NRA’s goal to avoid dissolution and subvert the remedy provided for under New York law entirely through this Chapter 11 case. The Court does not know what specific mechanism the NRA plans to use,¹⁰⁵ but its intention is clearly to “take dissolution off the table.”¹⁰⁶

Courts have consistently held that a bankruptcy case filed for the purpose of obtaining an unfair litigation advantage is not filed in good faith and should be dismissed. *See Antelope Techs., Inc. v. Lowe (In re Antelope Techs, Inc.)*, 431 F. App’x. 272 (5th Cir. 2011) (affirming dismissal for cause based on finding that “the purpose of the petition was not primarily to reorganize or respond to financial crisis but instead was to gain unfair advantage in the shareholder derivative action”); *Investors Group, LLC v. Pottorff*, 518 B.R. 380, 383-84 (N.D. Tex. 2014) (affirming dismissal of a bankruptcy case for being filed in bad faith based on a finding that the primary

¹⁰⁵ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 41:22-42:5 (Counsel for the NRA describing different ways in which a plan could be structured to achieve the NRA’s goal in this case).

¹⁰⁶ *Transcript of Hearing Held April 5, 2021* [Docket No. 497] at 49:23-25 (Counsel for the NRA: “We filed, again, for three reasons that constitute good faith. We needed to take dissolution, the equivalent of foreclosure, off the table. . . .”).

purpose for filing the bankruptcy petition was to gain an advantage in pending litigation); *In re Alexandra Trust*, 526 B.R. 668, 679-680 (Bankr. N.D. Tex. 2015) (citing cases).

Using the bankruptcy process to avoid dissolution in the NYAG Enforcement Action is also problematic because it deprives the state of New York of the ability to regulate not-for-profit corporations in accordance with its laws. There is a regulatory scheme for evaluating whether a New York charity should continue in existence under Article 11 of the New York Not-For-Profit Corporation Law. While bankruptcy courts can, in some circumstances, apply state regulatory law,¹⁰⁷ a bankruptcy case filed for the purpose of avoiding a regulatory scheme is not filed in good faith and should be dismissed. *See In re First Plus Fin. Enters., Inc.*, 99 B.R. 751, 755-56 (Bankr. W.D. Tex. 1989) (finding cause for dismissal under section 1112(b) because the case was filed in bad faith where “the obvious purpose in this case is to use the Chapter 11 filing as a litigation strategy and leverage in order to defeat the Texas regulatory scheme for the receivership and conservatorship of insolvent life insurance companies”); *In re Forest Hill Funeral Home & Mem’l Park-East, LLC*, 364 B.R. 808, 822-23 (Bankr. E.D. Okla. 2007) (finding cause for dismissal under section 1112(b) because the case was not filed in good faith for several reasons, including that it was filed to evade the regulatory authority of the state of Tennessee); *cf. Halo Wireless, Inc. v. Alenco Commc’ns Inc. (In re Halo Wireless, Inc.)*, 684 F.3d 581, 587-88 (5th Cir. 2012) (noting that section 362(a)(4) assists with the goal of discouraging debtors from submitting bankruptcy petitions either primarily or solely for the purpose of evading impending governmental efforts to invoke the governmental police powers to enjoin or deter ongoing debtor conduct that would seriously threaten the public safety and welfare).

¹⁰⁷ *See, e.g., In re HHH Choices Health Plan, LLC*, 554 B.R. 697 (Bankr. S.D.N.Y. 2016).

The Court would also like to discuss some of the NRA’s other stated reasons for filing bankruptcy. The Court understands that the NRA wants to leave New York for a variety of reasons, not least of which being what it perceives to be a generally hostile environment. While the Court does not find that reincorporating in Texas was the true purpose of the bankruptcy filing, the Court would have concerns even if it were. Reincorporating in Texas could be accomplished outside of bankruptcy pursuant to applicable regulations for New York not-for-profit organizations,¹⁰⁸ which begs the question of what the Bankruptcy Code is being used for. If the goal is moving to Texas, the purpose of the bankruptcy would still appear to be avoidance of the regulatory scheme in New York that would be required for such a transition outside of bankruptcy, or at least avoidance of the New York regulators.

While the Court also does not find potential adverse judgments in litigation other than the NYAG Enforcement Action to have been a purpose for filing bankruptcy, the Court notes that based on the evidence, the NRA is financially healthy and potentially adverse litigation outcomes are too attenuated to justify a good faith bankruptcy filing. *See Off. Comm. of Unsecured Creditors v. Nucor Corp. (In re SGL Carbon Corp.)*, 200 F.3d 154, 163 (3d Cir. 1999) (holding that dismissal was appropriate where bankruptcy filing was based on litigation because the record was replete with evidence of the debtor’s financial strength, there was no evidence that a judgment was imminent, and an assessment that pending litigation might result in a judgment causing financial and operational ruin was premature).

In closing arguments, counsel for the NRA raised several additional arguments that the Court would like to address. One of those arguments was that if avoiding dissolution is found to

¹⁰⁸ See Article 9 of the New York Not-For-Profit Corporation Law (governing merger or consolidation); Article 10 of the New York Not-For-Profit Corporation Law (governing non-judicial dissolution).

be an inappropriate bankruptcy purpose, this would allow a state to block a debtor's right to file for bankruptcy simply by filing an action seeking dissolution, and this would be tantamount to allowing a state to preempt federal law. This argument is based on the misconception that the state of New York has blocked access to bankruptcy relief just by filing a complaint with the word dissolution in it. The Court has not announced a *per se* rule that a pending dissolution action renders an entity ineligible for bankruptcy. Rather, the Court is evaluating the debtor's good faith or lack thereof in filing bankruptcy based on the totality of the circumstances of this specific case. The NRA is a solvent and growing organization using this bankruptcy as a tool to win its dissolution lawsuit, and that is not an appropriate use of bankruptcy.

Counsel for the NRA also, as the Court understands it, made the following argument. Section 1129(d) of the Bankruptcy Code states that the court may not confirm a plan over the objection of a governmental unit if the principal purpose of the plan is the avoidance of the application of section 5 of the Securities Act of 1933. Section 5 of the Securities Act of 1933 is an exercise of police power. Therefore, counsel argues, Congress has implicitly instructed that it is acceptable to file a bankruptcy petition for the purpose of avoiding any exercise of police power other than section 5 of the Securities Act of 1933. The Court does not understand this provision of the Bankruptcy Code to make such a sweeping endorsement of using bankruptcy for the principal purpose of avoiding the exercise of police power. Just because Congress has provided a guard rail for confirmation does not relieve the Court of its duty to conduct a fact-intensive inquiry to determine where a particular petition for bankruptcy relief falls along the spectrum ranging from the clearly acceptable to the patently abusive. *See In re 15375 Mem'l Corp.*, 589 F.3d 605, 618 (3d Cir. 2009) (discussing the duties of courts in examining whether bankruptcy petitions are filed in good faith).

Finally, the Court notes that even if it agreed with one or more of the NRA's arguments regarding eligibility or confirmation standards, the Fifth Circuit Court of Appeals has already given clear instruction to examine cases to determine whether they were filed in good faith and to dismiss those that were not. *See In re Humble Place Joint Venture*, 936 F.2d 814, 817 (5th Cir. 1991) ("Because *Little Creek* explicitly treated the question of good faith dismissals under § 1112, the case settles any statutory or constitutional question about that procedure.").

The Court finds, based on the totality of the circumstances, that the NRA's bankruptcy petition was not filed in good faith but instead was filed as an effort to gain an unfair litigation advantage in the NYAG Enforcement Action and as an effort to avoid a regulatory scheme. This constitutes cause for dismissal under section 1112(b)(1) of the Bankruptcy Code.

Consideration of the Appointment of a Trustee or Examiner

Having found cause for dismissal, section 1112(b)(1) requires that the Court now consider whether appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate. The appointment of a Chapter 11 trustee is an extraordinary remedy that requires a movant to meet their burden of proof by clear and convincing evidence. *In re Patman Drilling Int'l, Inc.*, 2008 Bankr. LEXIS 715, at *15-16 (Bankr. N.D. Tex. Mar. 14, 2008). As mentioned previously, there is nothing approaching a consensus from the parties on what should be done.

As counsel for the NRA acknowledged on the record, there were cringeworthy facts during this trial. The movants have presented evidence of the NRA's past misconduct. Some facts regarding the NRA's past conduct were not available to this Court because the NRA's former treasurer asserted his rights under the Fifth Amendment during large swaths of his deposition.

Some of the conduct that gives the Court concern is still ongoing. The NRA appears to have very recently violated its approval procedures for contracts in excess of \$100,000. Mr. LaPierre is still making additional financial disclosures. There are also lingering issues of secrecy and a lack of transparency. For example, even after hearing testimony from several witnesses, it is still very unclear why Mr. Spray, an officer everyone seemed to hold in high regard for his talent and integrity, parted ways with the NRA two weeks into this bankruptcy case. What is clear is that Mr. Spray's departure was precipitated by a call from Mr. LaPierre without involvement of the board of directors.

What concerns the Court most though is the surreptitious manner in which Mr. LaPierre obtained and exercised authority to file bankruptcy for the NRA. Excluding so many people from the process of deciding to file for bankruptcy, including the vast majority of the board of directors, the chief financial officer, and the general counsel, is nothing less than shocking.

The determination of whether appointment of a trustee or an examiner is in the best interests of creditors and the estate in this case, however, is complicated for a variety of reasons. The NRA has a mission that is, at times, political and polarizing. The NRA does not sell goods or services, and it would not be easy to find a suitable individual to serve in the role of trustee or examiner with expanded powers.¹⁰⁹

In an odd twist for a bankruptcy case, the NRA is financially healthy, and undisputed creditors are likely to be paid sooner in the ordinary course outside of bankruptcy than they would if they must wait for confirmation of a plan of reorganization. On the other hand, if a trustee or an

¹⁰⁹ The examiner that has been requested is one with expanded powers, including the power to “independently examine, and the extent necessary, remove management for cause.”

examiner with expanded powers were appointed, the Court believes the members and other donors who provide financial support to the NRA may not continue to support the organization.

While there is evidence of the NRA's past and present misconduct, the NRA has made progress since 2017 with its course correction. Whether it is yet complete or not, there has been more disclosure and self-reporting since 2017. Both Ms. Rowling and Mr. Erstling, the NRA's Director of Budget and Financial Analysis, testified that the concerns they expressed in the 2017 Whistleblower Memo are no longer concerns.¹¹⁰ Mr. Frazer testified regarding the compliance training program that the NRA now has for employees.¹¹¹ Mr. Spray testified credibly that the change that has occurred within the NRA over the past few years could not have occurred without the active support of Mr. LaPierre.¹¹² It is also an encouraging fact that Ms. Rowling has risen in the ranks of the NRA to become the acting chief financial officer, both because of her former status as a whistleblower and because of the Court's impression of her from her testimony as a champion of compliance.

In short, the testimony of Ms. Rowling and several others suggests that the NRA now understands the importance of compliance. Outside of bankruptcy, the NRA can pay its creditors, continue to fulfill its mission, continue to improve its governance and internal controls, contest dissolution in the NYAG Enforcement Action, and pursue the legal steps necessary to leave New York. While the Court appreciates the way in which some of the parties have presented the appointment of an examiner as a compromise that could provide some benefits without taking too much control from the NRA, the Court finds that the reasons discussed above weigh against keeping this case in bankruptcy with the appointment of a trustee or an examiner. For these

¹¹⁰ *Transcript of Hearing Held April 23, 2021* [Docket No. 697] at 94:24-95:4.

¹¹¹ *Transcript of Hearing Held April 7, 2021* [Docket No. 700] at 26:15-28:1.

¹¹² *Transcript of Hearing Held April 13, 2021* [Docket No. 578] at 156:17-157:5.

reasons, the Court finds appointment of a trustee or an examiner would not be in the best interests of creditors and the estate.

Analysis of the Unusual Circumstances Exception Under Section 1112(b)(2)

The NRA did not allege unusual circumstances under section 1112(b)(2) of the Bankruptcy Code in their briefing but did discuss them during closing arguments at the conclusion of trial.

Section 1112(b)(2) states:

The court may not convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter if the court finds and specifically identifies unusual circumstances establishing that converting or dismissing the case is not in the best interests of creditors and the estate, and the debtor or any other party in interest establishes that—

(A) there is a reasonable likelihood that a plan will be confirmed within the timeframes established in sections 1121(e) and 1129(e) of this title, or if such sections do not apply, within a reasonable period of time; and

(B) the grounds for converting or dismissing the case include an act or omission of the debtor other than under paragraph (4)(A)—

(i) for which there exists a reasonable justification for the act or omission; and

(ii) that will be cured within a reasonable period of time fixed by the court.

While there are certainly unusual circumstances in this case, the Court does not find that they establish that dismissing the case is not in the best interests of creditors and the estate. This is true for many of the reasons discussed above. In addition, no party has established the requirement of section 1112(b)(2)(A). At trial, the Court was aware that the NRA intended to file a plan that would pay creditors in full, but the plan was not filed before the close of evidence. It was also clear from the evidence that the NRA could face substantial challenges in confirming a plan depending on how the NRA would be willing to structure it. The Court is aware that the NRA has now filed a plan of reorganization, but that plan was not offered into evidence and is not properly before the Court.

V. Conclusion

There are several aspects of this case that still trouble the Court, including the manner and secrecy in which authority to file the case was obtained in the first place, the related lack of express disclosure of the intended Chapter 11 case to the board of directors and most of the elected officers, the ability of the debtor to pay its debts, and the primary legal problem of the debtor being a state regulatory action. The Court agrees with the NYAG that the NRA is using this bankruptcy case to address a regulatory enforcement problem, not a financial one.

The Court finds that the NRA did not file the bankruptcy petition in good faith because this filing was not for a purpose intended or sanctioned by the Bankruptcy Code. Therefore, cause exists under section 1112(b) to dismiss this case, which the Court finds is in the best interests of creditors and the estate.

The Court is not dismissing this case with prejudice,¹¹³ but should the NRA file a new bankruptcy case, this Court would immediately take up some of its concerns about disclosure, transparency, secrecy, conflicts of interest of officers and litigation counsel, and the unusual involvement of litigation counsel in the affairs of the NRA, which could cause the appointment of a trustee out of a concern that the NRA could not fulfill the fiduciary duty required by the Bankruptcy Code for a debtor in possession.

IT IS THEREFORE ORDERED that the Motions to Dismiss are **GRANTED** and the above-captioned cases are dismissed without prejudice;

IT IS FURTHER ORDERED that the Examiner Motion is **DENIED** as moot; and

IT IS FURTHER ORDERED that the CRO Motion is **DENIED** as moot.

¹¹³ The movants did not request a prejudice period in their original Motions to Dismiss. While the NYAG did request dismissal with prejudice in a reply brief, it was not discussed in the body of the reply, and the NRA did not have an opportunity to provide responsive briefing to that request.

AMERICAN BANKRUPTCY INSTITUTE

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###End of Order###



“Fraud Is The Daughter Of Greed” PPP Fraud In Turbulent Times

Thomas J. Salerno, Esq.
STINSON LLP

“Fraud is the daughter of greed.”
John Gash
The Great California Game
(1992)



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Thomas J. Salerno is a partner at Stinson LLP in Phoenix, Arizona, and an experienced litigator with national and international experience in complex commercial cases. He regularly assists private and publicly-traded companies in a broad range of industries (including hotels, sports, tech, health care, manufacturing, airlines, and franchising) to continue operations as they negotiate restructuring plans; he also advises lenders, distressed companies, committees, and assets acquirers in bankruptcies and out-of-court settlements. Mr. Salerno, who holds a JD from Notre Dame School of Law and a BA from Rutgers University, is a frequent writer, lecturer and presenter, who also serves as an adjunct law professor teaching courses in bankruptcy law and litigation. He is active in leadership positions with the American Bankruptcy Institute and served as the past chair of the Bankruptcy Section of the State Bar of Arizona. He has also served as an expert witness on U.S. insolvency law in litigation in Germany and has advised numerous foreign governments on revamping insolvency laws. Mr. Salerno has published several articles on third-party litigation funding and is a co-author of the two-volume treatise *BANKRUPTCY LITIGATION AND PRACTICE*.



Little Bit Of Context....

- **Fall 2009: Lehman Bros. Market Meltdown**
 - **Government Response:** Troubled Asset Recovery Program (“TARP”)
 - **Stimulus Package: \$600 Billion (Wow! Does that much money even exist?)**
 - Overvalued real estate decimates investment/retirement portfolios worldwide.
 - ***Where did 35% of my 401K money go?***

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“COVID? What the heck is that?”

February/March 2020: Funny Sounding “Foreign Virus” Creeps Into U.S. Public Consciousness

- “Coronavirus” and “COVID-19”...
 - Did I miss COVID 1-18?
- How serious can this be...really?
 - 18 months In...

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How Is The COVID Economic Fallout Different From Lehman Bros.?

- Lehman Bros. was a **BALANCE SHEET CRISIS**

- COVID -19 is a **P&L CRISIS**
- The **Balance Sheet Crisis** is just about here....

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COVID BLUES? GOVERNMENT TO THE RESCUE!!!

- **Coronavirus Aid & Economic Security Act (“CARES Act I”) (March 27, 2020)**

- Total Stimulus Package: **\$2.2 TRILLION!** (Is that a “T”?)
 - Makes TARP look like chump change!

Introduces U.S. to Payroll Protection Program (“PPP”) (“PPP I Loans”)

- PPP Program Loan Allocation: **\$349 Billion**
- **Money runs out about 2 weeks!** (\$349 Billion just doesn’t go as far as it used to...)

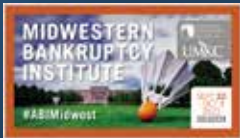
- **Payroll Protection Program & Health Care Enhancement Act (“CARES Act I 1/2”) (April 23, 2020)**

- PPP Loan Allocation: Another **\$310 Billion** (that should do it!)
 - “PPP 1 ½ Loans”
- CARES Act I ½ (and PPP 1 ½ Loan Program) expire August 8, 2020
- From August to December 27, 2020---no new CARES Act/PPP funds available....
 - **Ugly capitalism in all its glory!**

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CARES Act II



- Passed on December 23, 2020, signed by President December 27, 2020.
- Smorgasbord of stimulus monies/benefits—a veritable financial feast! **\$748 Billion*** in yet more stimulus monies.
 - Continuation of expanded unemployment benefits, direct stimulus checks, grants to states to implement vaccine distribution, aid to nursing homes...the list goes on! And...
- CARES Act II includes the Payroll Protection Program and Other Small Business Support Act— another **\$284.45 Billion!** (“PPP III Loans”)— combined total for all PPP Loan allocations is now about **\$943 Billion.**
- **PPP III Expired by its own terms end of May 2021—the party’s over (at least for now)!**
- But wait—there’s more! PPP Clarification of Tax Treatment of Forgiveness of Covered Loans—tax deductions and free money!
 - So you get free money, use it to pay business expenses, and then still get a tax write off for those payments!
 - This following a fairly major tax cut—but hey, that’s an issue for our kids/grandkids to worry about!
 - Not sold in any stores! Get yours while they last!

* A billion here, a billion there, and pretty soon you start having some real money!

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Back to Fraud--Come On! Is This Really An Issue?

- Where there is a crisis that money is thrown at, there is fraud!
- Recall the **9/11 Relief Fund Scams?**
 - The Eighth Circle of torment in *Dante's Inferno* is reserved for Fraud—perhaps too lenient?
- **First prosecution for PPP Fraud was in July 2020** (the PPP was all of 4 months old!)—involved a \$24 million scheme of submitting false PPP loan applications.
- And away we go!

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Arnold & Porter has its own tracker!

<https://www.arnoldporter.com/en/general/cares-act-fraud-tracker>



Last Updated September 8, 2021

| Date | Char. | Feder. | Program | Defendant | Charge | Amount | Summary |
|-----------|----------------|--|---------|---------------------------------|--|--------------|---|
| 5/14/2021 | DOJ/W.D. Wash. | FBI, DOJ-ORG, SSO-ORG, USSS, CSPOL, IRS-CI | PCA | Abiodun Rufai a./i's Sandy Tang | Conspiracy to commit wire fraud, wire fraud, aggravated identity theft: 18 U.S.C. 1, 1345. | \$24,000,000 | Abiodun Rufai, a Nigerian citizen, was charged with allegedly using the identities of more than 100 Washington residents to file fraudulent pandemic-related unemployment benefits. Rufai also allegedly filed fraudulent unemployment claims in Hawaii, Wyoming, Massachusetts, Montana, New York, and Pennsylvania. |
| 5/28/2021 | DOJ/W.D. | FBI IRS-CI | PPP | Adam D. Arena, Amanda J. Gloria | Conspiracy to commit bank fraud, conspiracy to engage in monetary transactions with criminally derived proceeds, engaging in monetary transactions with criminally derived proceeds: 18 U.S.C. §§ 1345, 1925(a), 1924(a)(1), 1967. | \$4,000,000 | Adam Arena and Amanda Gloria were charged with allegedly conspiring to fraudulently obtain and misuse nearly \$4 million in PPP loans. Arena and Gloria allegedly submitted a false loan application on behalf of a defunct business owned by Arena called ADA Auto Group LLC. The two allegedly used the loan proceeds on personal expenses, including the purchase of two cars. |



Brief Recap...

- As per the A&P Tracker, **between July 28, 2020 and May 14, 2021** (approx. 25 months), there have been...
 - **348** total PPP related criminal fraud prosecutions brought...
 - Involving about **\$1.1 billion** total allegedly fraudulently obtained PPP and related funds.

Compare with 9/11 scams:

Prepare for the coronavirus scams: Learning from post-9/11 fraud

The 9/11 scams were largely stopped or deterred before massive damage could be done to relief efforts. But government agencies, legitimate charities, law enforcement and, above all, individuals will have to be vigilant in order to prevent fraud from succeeding. Organizations will want to train their personnel in fraud detection. And government agencies should consider beefing up public education campaigns.

By DANIEL R. ALONSO and LEROY FRAZER JR.
NEW YORK DAILY NEWS | APR 08, 2020 AT 5:00 AM



By any metric, that's a pretty prevalent issue!

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And Fraud Cases Do Make For Some Catchy Headlines!



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L.A. Man Admits Fraudulently Obtaining \$9 Million in COVID-19 Loans

A Los Angeles man has pleaded guilty to fraudulently obtaining \$9 million in loans from COVID-relief programs, some of which he transferred to his stock trading accounts and used for gambling trips to Las Vegas, federal prosecutors said, the Associated Press reported. Andrew Marnell pleaded guilty Tuesday to one count of bank fraud and one count of money laundering, the U.S. Attorney's Office said in a statement. The 41-year-old faces up to 40 years in prison when he's sentenced in February. **Marnell admitted using a series of corporations he controlled to fraudulently obtain loans under the federal Paycheck Protection Program.** Prosecutors said his loan applications made numerous false and misleading statements about the companies' business operations and payroll expenses. Marnell, often using aliases, submitted fake and altered documents, including bogus federal tax filings and employee payroll records, investigators said. As part of a plea agreement, Marnell agreed to forfeit items related to the pilfered loan funds, including \$319,298 in cash recovered from his residence, numerous electronic devices, a **Rolux Oyster watch**, a **Range Rover** and a **Ducati motorcycle**. Thursday, September 16, 2021

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'Unprecedented' fraud penetrated rollout of COVID-19 small business loans, watchdog warns

The SBA inspector general says "inherent guardrails" left the program vulnerable.

By Leslie Bruggeman
August 5, 2021, 1:00 AM • 11 min read



At the dawn of the COVID-19 pandemic, when offices and restaurants began shuttering, the federal government scrambled to keep small businesses afloat -- ultimately spending over a trillion dollars to help protect the American Dream for millions of workers and business owners.

But even before the first checks went out, alarm bells went off.

The person ringing those bells the loudest was Hannibal "Mike" Ware, the inspector general of the **Small Business Administration**. The veteran internal watchdog says he participated in a series of meetings with Trump administration officials and SBA program analysts that were laced with "testy exchanges" about how to expeditiously dispense funds without leaving them vulnerable to fraudulent claims.

"In terms of the monetary value, the amount of fraud in these COVID relief programs is going to be larger than any government program that came before it," Ware said.



The New York Times

15% of Paycheck Protection Program Loans Could Be Fraudulent, Study Shows

Some \$76 billion of the program's \$800 billion in loans may have been taken improperly, a new paper concludes.

Aug. 17, 2021

When the Paycheck Protection Program began last year to help small businesses that were struggling during the pandemic, the federal government was determined to get the relief money out fast — so it waived much of the vetting lenders traditionally do on business loans.

The absence of those safeguards meant that fraud was highly likely. But just how much of the program's \$800 billion was taken illicitly?

A new academic working paper released on Tuesday contains an estimate: **Around 1.8 million of the program's 11.8 million loans — more than 15 percent — totaling \$76 billion had at least one indication of potential fraud, the researchers concluded.**

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United States Department of Justice

THE UNITED STATES ATTORNEY'S OFFICE
DISTRICT OF KANSAS

FOR IMMEDIATE RELEASE

Thursday, September 9, 2021

Wichita Businessman Faces 19 Counts of COVID Relief Fraud

WICHITA, KAN. — A federal grand jury in Wichita indicted a Kansas man on charges he defrauded federal, state, and local agencies of more than \$450,000 in COVID-19 business recovery funds.

According to court documents, Michael Capps, 43, of Wichita is the owner and/or majority owner of Midwest Business Groups, LLC and Krivacy, LLC. Court documents also indicate he is a member of the Fourth and Long Foundation. Capps is accused of submitting false and fraudulent documents on behalf of the companies to the Small Business Administration (SBA) for Economic Injury Disaster Loans (EIDL), as well as to the Kansas Department of Commerce for Small Business Working Capital grants, and to Sedgwick County for a Sedgwick County Cares grant.

Capps also allegedly sent false and fraudulent documents to Emprise Bank to receive a Payroll Protection Program (PPP) loan.

The indictment filed against Capps charges him with:

- one count of making false statement to a bank for a PPP loan,
- one count of bank fraud in connection with a PPP loan,
- three counts of false statement to the SBA for EIDL loans,
- three counts of wire fraud in connection with EIDL loans from the SBA,
- two counts of wire fraud in connection with grants from the Kansas Department of Commerce,
- one count of wire fraud in connection with a grant from Sedgwick County, and
- eight counts of money laundering.



POLITICS

Covid-19 Fraud Charges Levelled Across the Country

Justice Department targets a dozen people for submitting allegedly fraudulent bills totaling \$143 million

By Aruna Viswanatha
Updated May 27, 2021 6:33 pm ET

Mr. Taylor is one of around a dozen people charged by federal prosecutors in the past week with participating in fraud schemes related to the pandemic, as the Justice Department ramps up investigations into misconduct tied to Covid-19 and **the trillions of dollars in government relief funds** provided since last year. The new cases collectively account for around \$143 million in allegedly fraudulent bills to government healthcare programs, the agency said.

Several of the alleged schemes appear to have started in the years before the pandemic, escalating as the federal government loosened healthcare billing restrictions in early 2020 in an effort to speed care to patients around the country and avoid overwhelming healthcare systems.

Last week, Attorney General Merrick Garland announced a new task force specifically targeting Covid-19 fraud, noting that some 600 people across the country had already been charged in the past year with related crimes involving more than \$600 million. In the early days of the pandemic, the Justice Department under the Trump administration focused on price gouging and hoarding of crucial supplies. It also targeted **fraud in the Paycheck Protection Program** and other federal loan programs, including defendants who allegedly submitted an application for fake businesses named after characters in "Game of Thrones," and others who spent loan proceeds on cars, boats and jewelry.

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Two Men Charged in Scheme to Obtain Fraudulent SBA Loans

Federal authorities announced yesterday that men from Massachusetts and New Hampshire have been charged in connection with their alleged roles in a scheme that used stolen identities to fraudulently obtain more than **\$450,000** in disaster loans from the Small Business Administration, the Associated Press reported. About \$250,000 of that money was used to purchase iPhones that were then resold, according to a statement from the U.S. attorney's office in Boston. Edwin Acevedo of Acton, Mass., and Hector Garcia of Manchester, N.H. were arrested last week and charged with conspiracy to commit wire fraud. Garcia was also charged with aggravated identity theft. Acevedo is being held pending a detention hearing. Garcia is scheduled to make an initial court appearance on Sept. 3. Garcia used the **stolen identity of a U.S. citizen to open a fraudulent bank account**, which was linked to other fraudulent bank accounts set up to receive the loans, prosecutors alleged. Acevedo then distributed debit cards associated with those accounts to other alleged accomplices, which were used to **launder the loans through the purchase of iPhones for resale**, prosecutors said. Garcia also **wired a portion of the funds to the Dominican Republic**, according to authorities.

Tuesday, August 24, 2021

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PPP loan fraud schemes ran wild as government doled out billions; at least 120 charged

First PPP fraud case closed last week

By Fred Lucas | Fox News

The Justice Department has charged more than [120 defendants](#) with fraud related to PPP loans. Some cases are substantial. For example, in March, a [Texas man](#) pleaded guilty to a scheme applying for 15 different PPP loans using 11 different companies to get \$24.8 million. In a pending case in California, federal prosecutors charged eight defendants with seeking more than 100 loans totaling almost [\\$22 million](#) using stolen identities and fake companies.

The Justice Department has charged more than [120 defendants](#) with fraud related to PPP loans. Some cases are substantial. For example, in March, a [Texas man](#) pleaded guilty to a scheme applying for 15 different PPP loans using 11 different companies to get \$24.8 million. In a pending case in California, federal prosecutors charged eight defendants with seeking more than 100 loans totaling almost [\\$22 million](#) using stolen identities and fake companies.

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Investors In Bankrupt Hotel Co. Ordered To Return \$2.4M

By Vince Sullivan

Law360 (September 15, 2021, 3:24 PM EDT) -- Two investors of bankrupt hotel owner Eagle Hospitality Group must return \$2.4 million to the debtor after a Delaware judge said the investors obtained the money through a fraudulent transfer of assets from the debtor after improperly applying for a loan under the federal Paycheck Protection Program.

According to the adversary complaint filed by Eagle subsidiary and co-debtor Urban Commons Queensway LLC, Wu and Woods fraudulently represented that they were authorized to seek a PPP loan on behalf of Urban Commons and when the loan was approved, transferred the \$2,473,500 in loan proceeds away from the debtor entities to businesses they controlled. This transfer puts the debtors at risk of having to repay the loans.

U.S. Bankruptcy Judge Christopher S. Sontchi granted Eagle's motion for summary judgment Tuesday in a Chapter 11 adversary proceeding against investors Taylor Woods and Howard Wu, saying there were no material facts in dispute surrounding the allegations that the investors engaged in a fraudulent transfer, fraud and unjust enrichment.

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New Twist—Let’s Get Someone to Drop A Dime on Fraudsters!



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Fraudulent Claims Act and Qui Tam Laws

- Essentially “deputizes” the public to report on fraud.
- Fraudulent Claims Act in certain cases imposes treble damages!
- Also provide for a “bounty” of usually between 25-30% of amount recovered...
 - Save the taxpayer some money and be rewarded for your efforts!

Applicable in PPP Fraud Cases? Yup!

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DOJ Continues to Use the False Claims Act to Protect PPP Funds

Sep 7, 2021

GOVERNMENT PROGRAM FRAUD, FALSE CLAIMS ACT & QUI TAM LITIGATION PLAYBOOK

KEY TAKEAWAYS:

- **The government continues to use the FCA as a tool to recover COVID-19 relief funds.** The Bernstein settlement is just the most recent example of the DOJ using the FCA as a significant tool for detecting PPP abuses in an effort to protect the integrity of the program and harks back to comments made by Acting Assistant Attorney General Brian Boynton at this year's annual Federal Bar Association Qui Tam Conference. In his remarks, Boynton stated that the "[FCA] will play a significant role in the coming years as the government grapples with the consequences of [the COVID-19 pandemic]."¹⁶ Boynton stressed that while the "circumstances of the current pandemic may be novel . . . the inevitable fraud schemes it will produce," such as "misuse of program funds and false certifications pertaining to loan forgiveness," "will in many cases resemble misconduct that the [FCA] has long been used to address."¹⁷
- **SBA's \$2 million "safe harbor" threshold will not deter government agency enforcement.** SBA's \$2 million "safe harbor" threshold¹⁸ does not mean that PPP loans of under \$2 million will escape scrutiny entirely. Rather, PPP loans under \$2 million can still give rise to FCA liability where—as here—there is evidence that the defendant knowingly submitted a false loan application and misappropriated PPP loan funds. Thus, this case further demonstrates the importance of ensuring that all PPP requirements are met regardless of the size of the loan.
- **Whistleblowers continue to be vital to the DOJ's pursuit of FCA cases.** This settlement emphasizes that whistleblowers will continue to be crucial to the government's efforts to recover misappropriated funds. For their efforts, whistleblowers may be awarded a portion of the recovery. Indeed, the whistleblower here received \$57,411, plus attorney's fees and costs.



Does Crime Pay?

Take from the White-Collar Criminal Defense Trenches

False Claims Act and PPP Fraud: When Will the Other Shoe Drop?

By Brian K. Starkevocher & Norman Blum on September 8, 2021

The rapid rollout of the PPP coupled with shifting federal guidelines and reduced underwriting requirements made PPP loans ripe for fraud. One expected avenue that the government and private whistleblowers will use to combat that fraud is the False Claims Act (FCA) (see [here](#)). But to date, there have been few publicly announced FCA cases brought for PPP fraud. It was not until January 2021 when the government announced its **first settlement** in a FCA case for PPP fraud. **There, the defendant failed to disclose that it was in bankruptcy proceedings at the time of the loan application.** There were no criminal charges. While that settlement was notable for being the first, **the alleged fraud involved only \$350,000 of PPP funds**—PPP loans, however, were made in sums as large as \$10 million.

Indeed, recent reporting suggests that the focus of investigations into FCA violations for the PPP is expanding beyond the recipients of PPP loans to the financial institutions, i.e., banks and fintech companies, that processed the borrowers' PPP applications and disbursed the loans. Whether there can be a viable FCA claim made out against these financial institutions is unclear—there are several strong defenses to FCA liability based on materiality and intent these entities likely could assert. But this reporting indicates that FCA cases based on PPP fraud are likely to increase substantially in the coming months and years.

So, it is not a question of if the other shoe will drop for PPP FCA cases, but when.



Impact on Bankruptcy World?

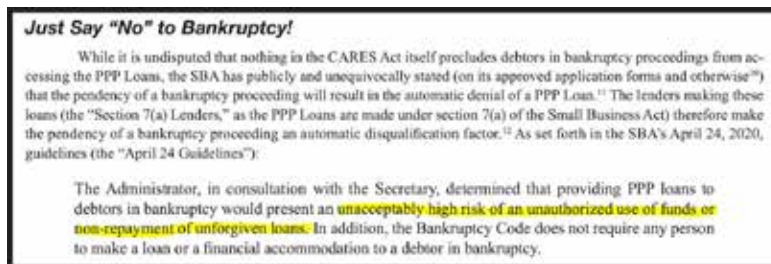
- Discharge related litigation?
 - Failure to disclose on the PPP loan application of a pending bankruptcy as **fraud under 523(a)(2)?**
- Plan objection issues?
 - If PPP money was obtained without disclosure of a pending bankruptcy, can a plan be objected to on the basis of being **violative of public policy under 1129(a)(1)(2) and/or (3)?**
 - Likely other issues—like why didn't the debtor get authority to borrow under 364?
- **"No harm no foul?"** If didn't disclose the pending bankruptcy or use the money as intended, **doesn't CARES Act provide the "penalty"?** You have to pay it back over 5 years at a low interest rate!
 - Good luck with that one in bankruptcy. Bankruptcy Courts are, after all, Courts of equity.
 - But still, isn't this like a liquidated damages clause? CARES Act has a "built in" penalty!

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Parting Shot--And the SBA Was Concerned About *Debtor* Dishonesty?

- As we all now know, since the CARES Act was enacted the SBA has dogmatically taken the position that **PPP loans should not be made available to debtors in bankruptcy.**



See Salerno, Weidner, Ebner & Simpson, "This DIP Loan *Should* Be Brought To You By Someone Who CARES! (Or "You Can't Get There from Here"): A Plea for Rationality, Part Two", *ABI Commentary* (April 28, 2020) (cited in "Emerging Trends From Bankruptcy Rulings On PPP Access", *Law360* (May 8, 2020).

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Despite the Change in Administrations and Congressional Invitation To Allow PPP Loans In Bankruptcy, the SBA Refused To Budge!

- Salerno, "SBA Consent To PPP Debtor Loan Provisions Under CARES Act II: Just Do It Already!!!!", *ABI Headlines* (March 4, 2021), available at https://abi-org.s3.amazonaws.com/Covid19/LegalUpdates/ABI_Just_Do_It_Article_March_4_2021.pdf
- Salerno, "The 'New and Improved' PPP Loan Package! Part 3", *American Bankruptcy Institute Journal* (February 2021)
- Salerno, "The Gift that Keeps On Giving: 'New And Improved' PPP Loan Package—Part 2!", *ABI Headlines* (December 31, 2020), available at https://abi-news.s3.amazonaws.com/The_New_and_Improved_PPP_Loan_Package.pdf
- Salerno, "The 'New and Improved' PPP Loan Package!", *ABI Headlines* (December 30, 2020), available at https://abi-news.s3.amazonaws.com/The_New_and_Improved_PPP_Loan_Package.pdf
- Salerno, "Update On Proposed Extension Of The PPP Loan Program—Gotta Read The Fine Print!", *ABI Headlines* (November 24, 2020) available at https://abi-org.s3.amazonaws.com/Newsroom/ABI_Brief/Update_on_Proposed_Extension_of_PPP.pdf
- Salerno, "COVID-19: Challenges In Distressed Debt And Liability Management", *Financier Worldwide* (October 2020)
- Salerno, "Proposed Extension Of The PPP Loan Program: A Nice First Step..." *American Bankruptcy Institute Journal* (September 2020) available at <https://abi.org/covid19>
- Salerno, "Reports Of A 'Debtor Bar' for PPP Loans Have Been 'Exaggerated'", *ABI News And Analysis* (July 2, 2020) available at https://abi-org.s3.amazonaws.com/Newsroom/ABI_Brief/SBAIangoArticle.pdf
- See Salerno & Simpson, "This DIP Loan *Should* Be Brought To You By Someone Who CARES! (Or "You Can't Get There from Here"): A Plea for Rationality, Part Two 1/2", *ABI Journal* (June 2020)

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So Debtors Obtaining PPP Loans In A Judicially Supervised Forum With Checks And Balances—This Creates The “Unacceptably High Risk” of Fraud?

- In what alternate universe, and given the rampant non-bankruptcy incidences of fraud related to PPP money, does this rationale make any sense at all?



But I digress....

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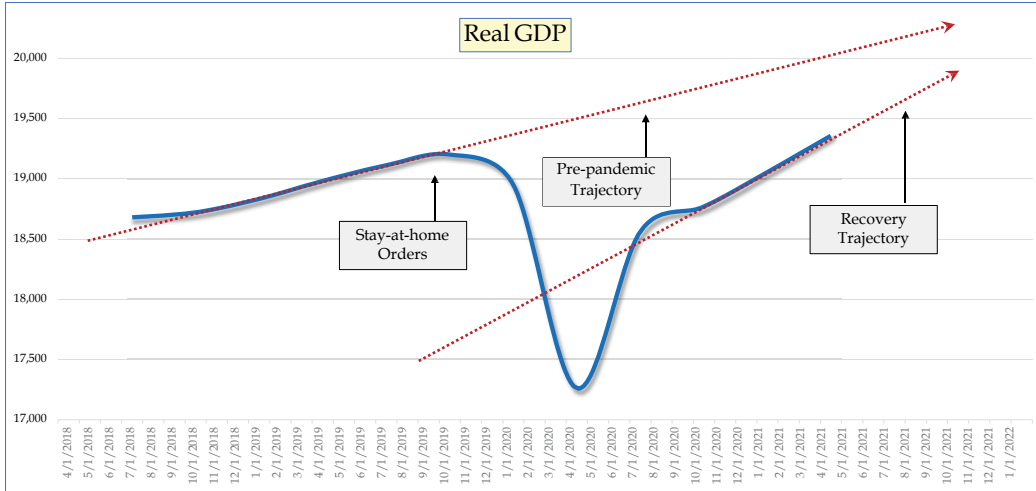


Thank You!!

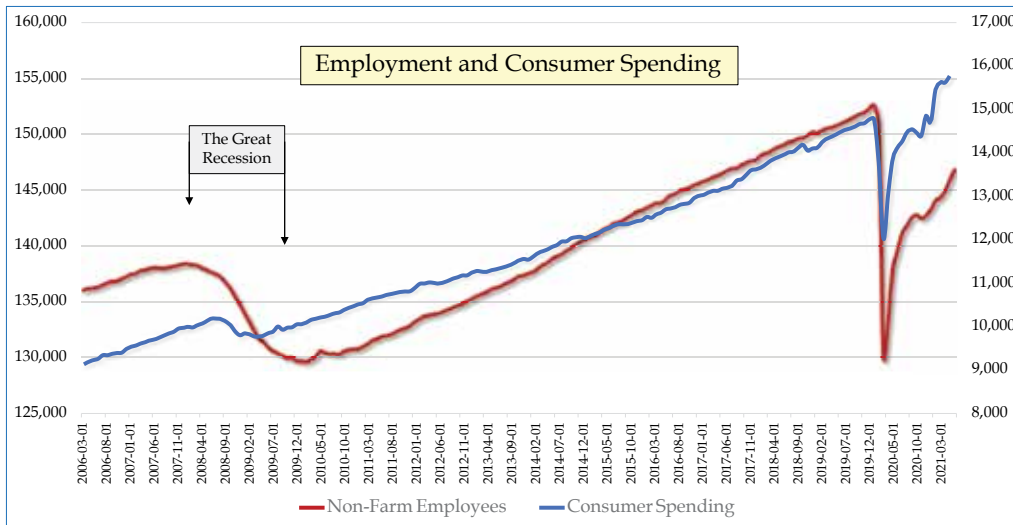


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GDP is recovering because of direct stimulus. It should return to normal in Q1 or Q2 2022, but, because direct stimulus is a thing of the past, GDP may not recover then unless employment and consumer confidence recover. That is unlikely to happen until the virus is contained.

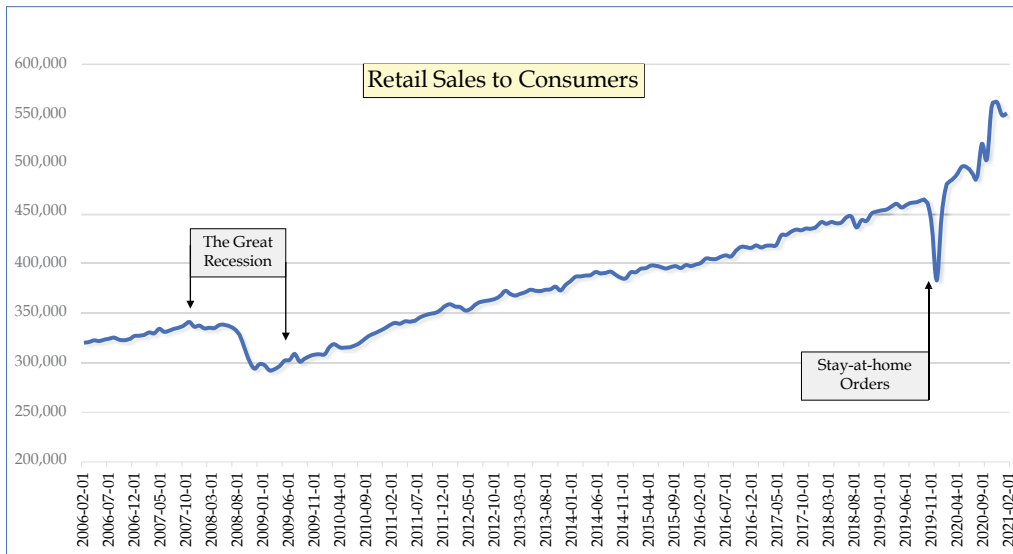


Before the pandemic, consumer spending and employment were at all-time highs. During the pandemic, spending recovered faster, because of stimulus. Employment continues to lag.



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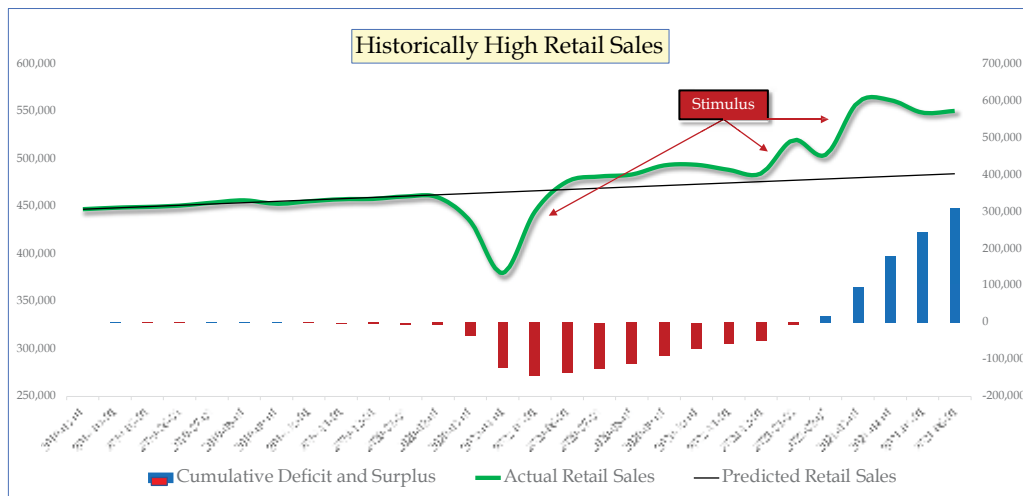
Retail sales in the pandemic recovered faster than in the great recession, because of stimulus.



[Advance Retail Sales: Retail Trade \(RSXFS\) | FRED | St. Louis Fed \(stlouisfed.org\)](#)

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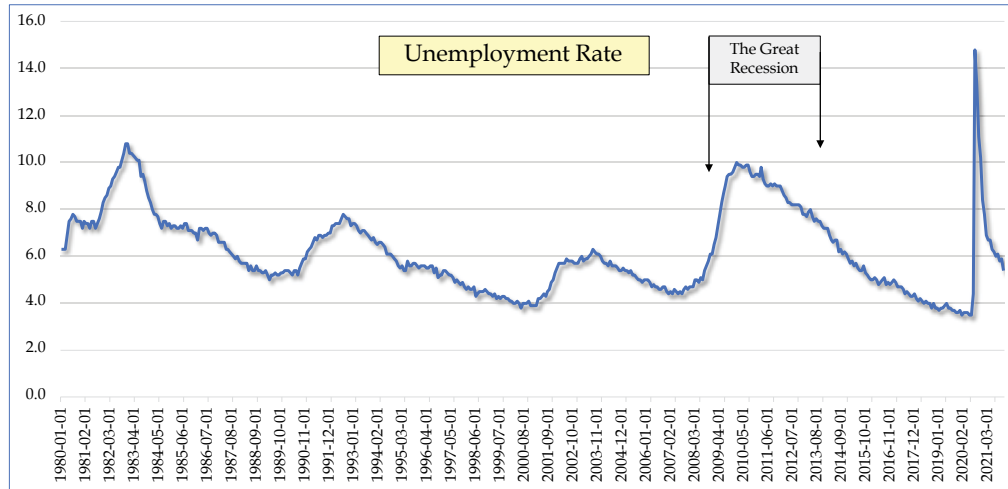
Retail sales plunged between February and June 2020, creating a backlog. Then those sales rose and fully recovered that deficit by February 2021. Since then, such sales have exceeded historic norms, because of stimulus.



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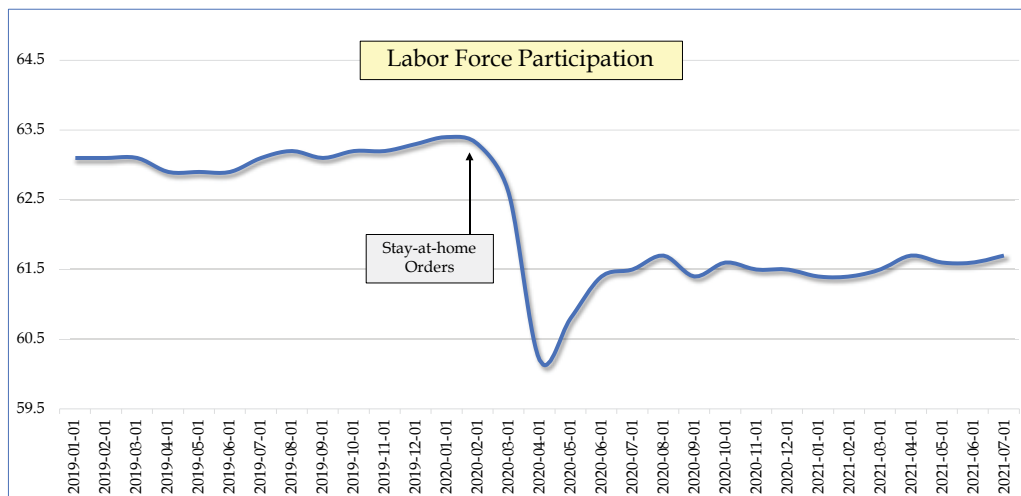
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Before the pandemic, the unemployment rate was at its lowest level since 1968. During the pandemic, unemployment briefly peaked at the highest rate since 1936 – during the great depression – but it has since recovered to 2014 levels, about 5.5% (9 million).



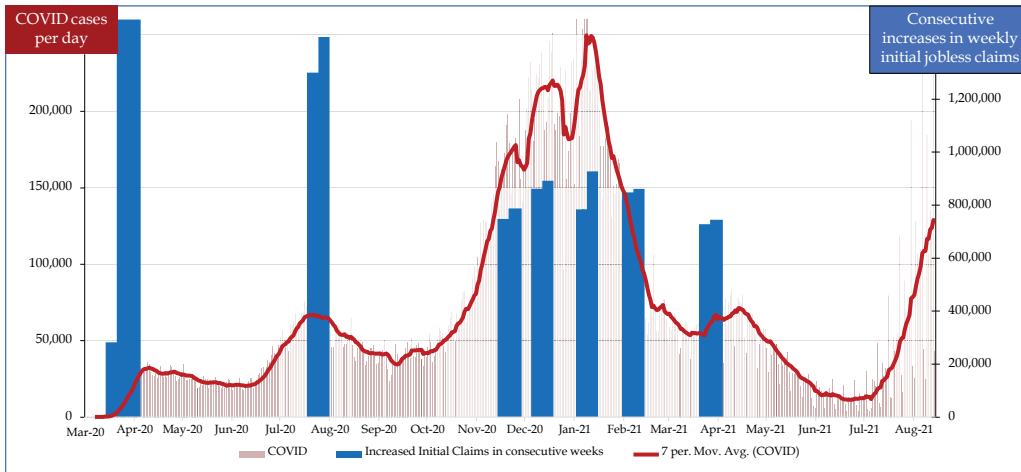
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Before the pandemic, workforce participation rates were at their highest levels since 2013. During the pandemic, they fell to the lowest rate since 1972, and they have since recovered less than half the loss. Nearly 2% of workers (3 million) have left the workplace and not returned.



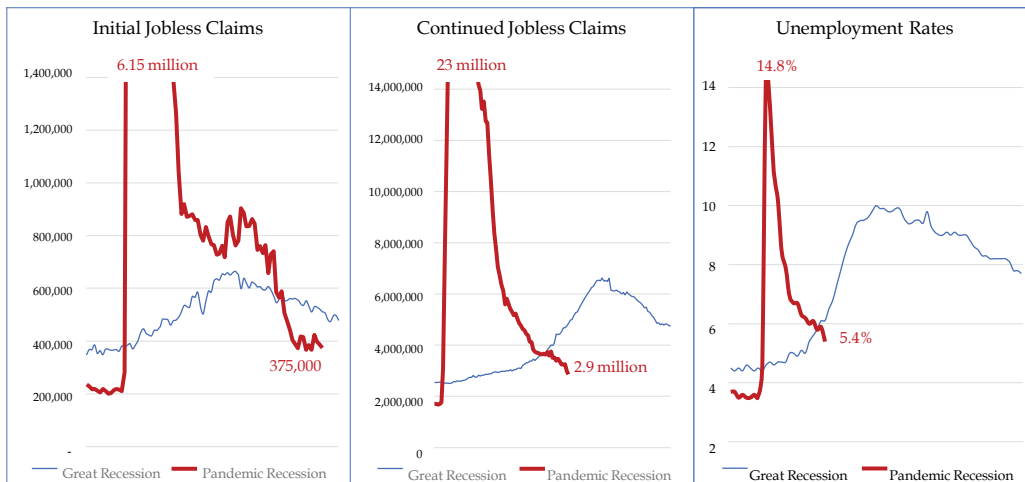
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Each COVID surge caused consecutive weeks of increases in initial jobless claims. After a horrid winter, COVID cases fell until mid-June, then began to rise again. Yet we haven't had any consecutive weeks of initial claims increases this summer.



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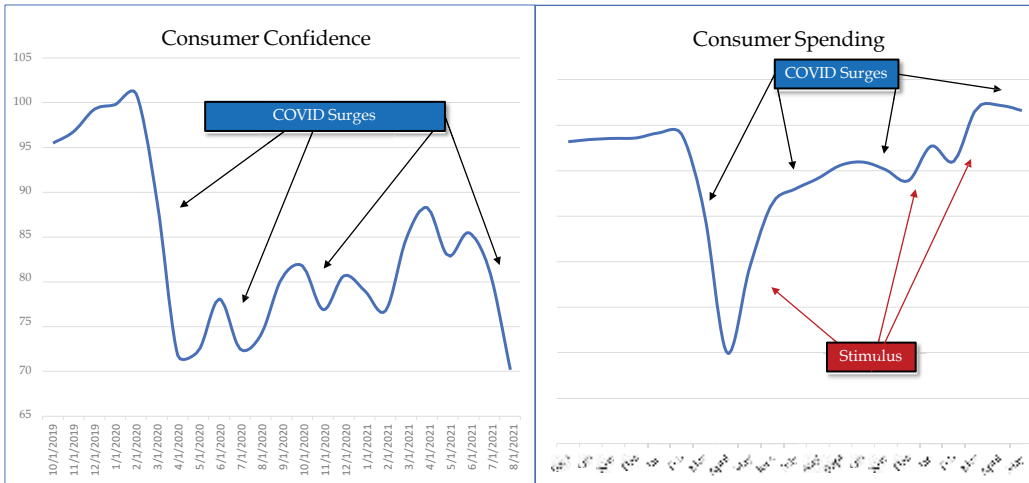
The pandemic recession began more brutally than the great recession and recovered faster, at first. After a rough churning winter, initial jobless claims fell in the spring, then stopped falling in the summer. Continued claims and the unemployment rate are dropping. Initial claims are not, which means that new workers are still cycling through the ranks of the unemployed.



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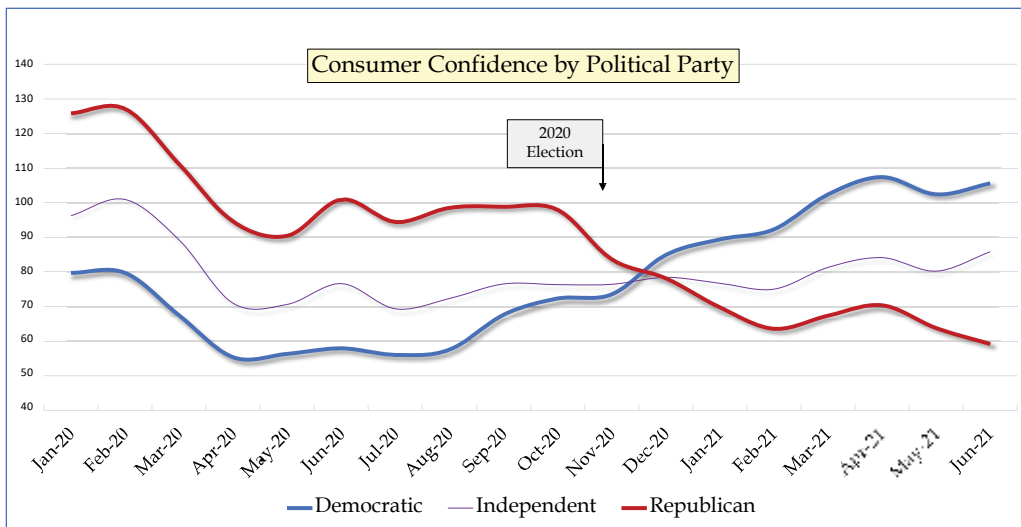
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Consumer confidence was also beaten down by COVID surges. That slowed the recovery of consumer spending between the April and January tranches of stimulus. The University of Michigan's consumer survey puts sentiment as of August 1 at its lowest level since 2011.



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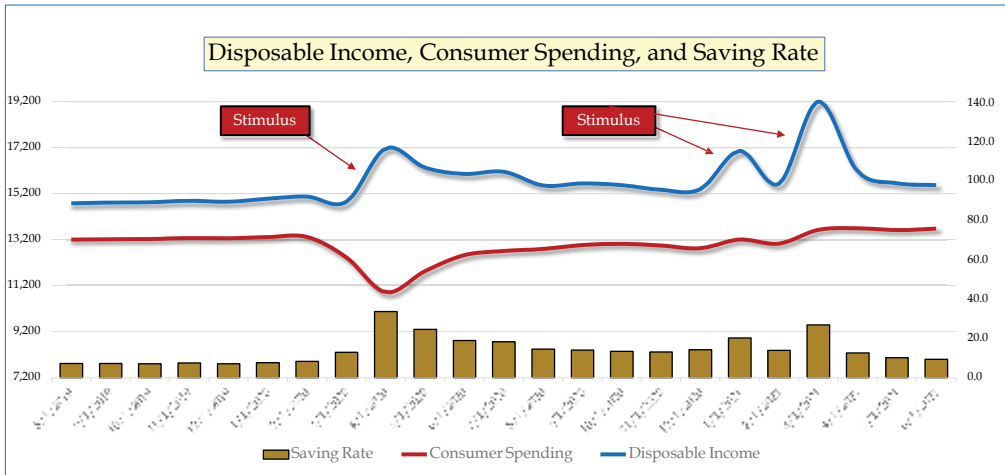
What can I say?



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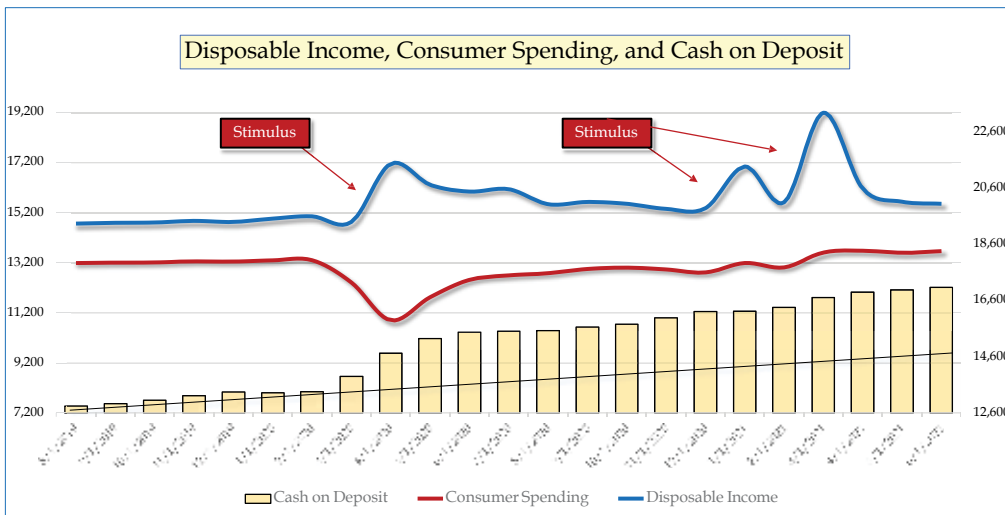
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During the pandemic, disposable income spiked three times with a total of \$5 trillion of stimulus injections in April 2020 (CARES Act), January 2021 (Budget Act), and March 2021 (America Recovery Act). This increased savings. Before the pandemic, the average saving rate was 7%. During the pandemic, it's been 17%. Consumers are spending more and saving more.



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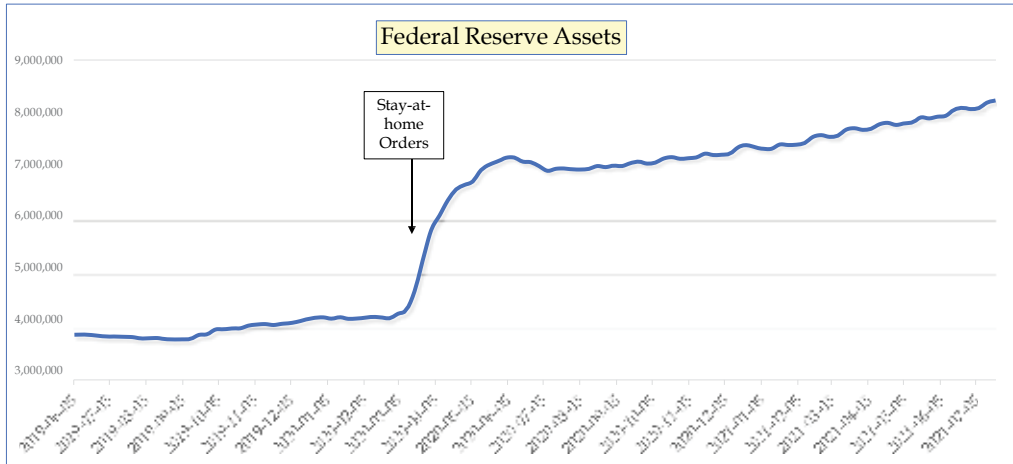
The higher saving rates contributed an additional \$3 trillion of cash on deposit at banks. That cash, to the extent it is spent, should accelerate a recovery.



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Early in the pandemic, the Fed bought a lot of debt paper, increasing the asset side of its balance sheet by \$3.5 billion. Its expenditures to purchase those assets did not go directly into consumer pockets. Rather, they maintained credit markets and kept interest rates low, both of which facilitated borrowing, sustaining liquidity.



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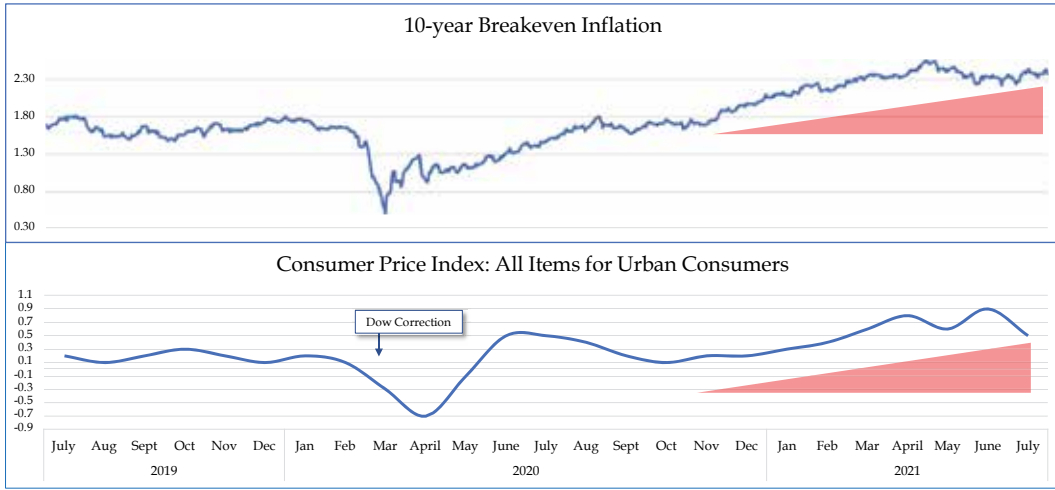
“Raw material prices are soaring! Businesses can’t find workers! It’s the 1970s all over again!” Chill out, everyone. Mostly we’re just experiencing the economic equivalent of a moment of wheelspin.

Paul Krugman, May 28, 2021

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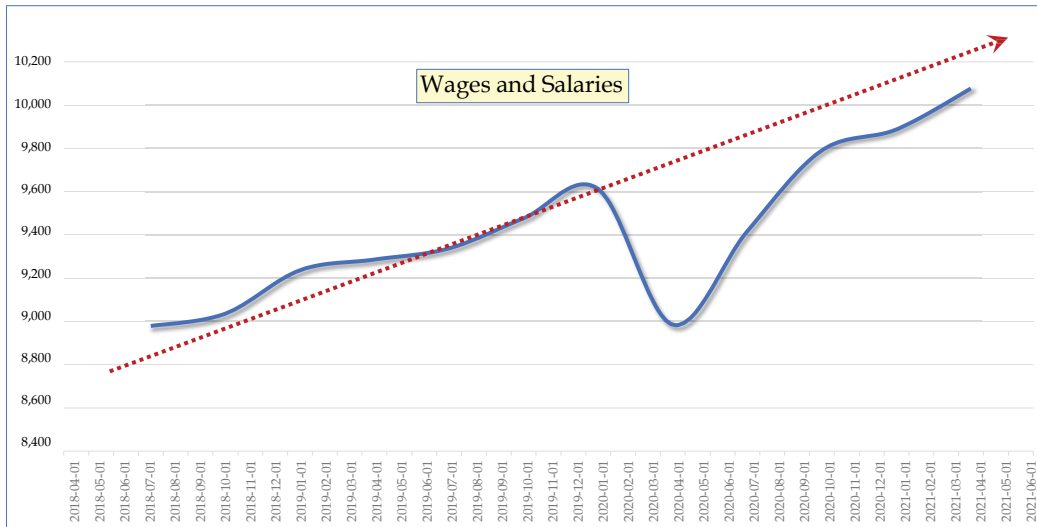
Between December 2020 and May 2021, the bond market signaled its expectation of modest inflation going forward. Since May 2021, it has signaled its concern that growth will slow, even as the CPI remains high. This suggests that current high prices are not yet systemic “inflation.”



Bureau of Labor Statistics Data ([bls.gov](https://www.bls.gov))

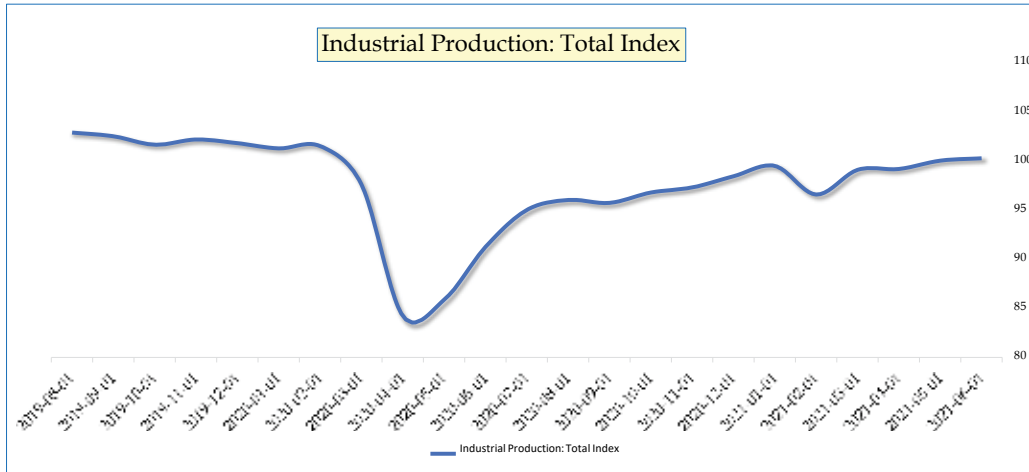
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Wages and salaries are returning to normal. But they lag the increases in spending and prices.



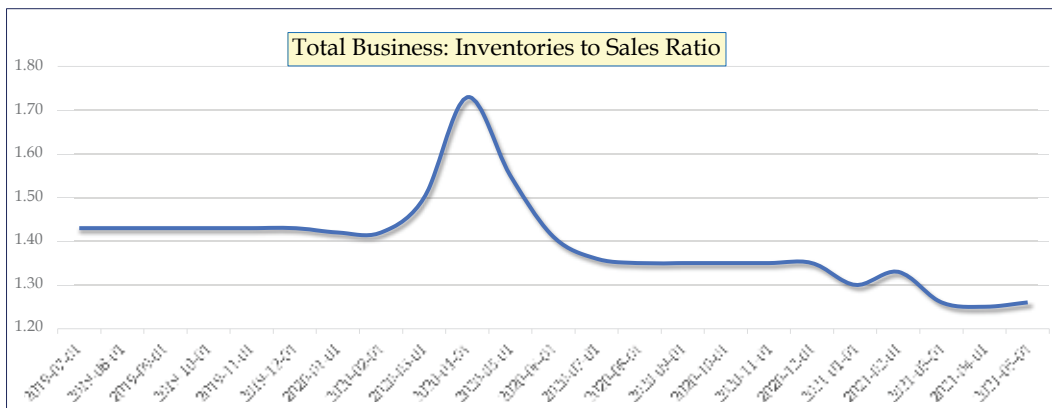
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Before the pandemic, production was humming. When the pandemic began, production fell. It's recovered, but not enough to make up for the pandemic shortfall, much less to replenish inventories.

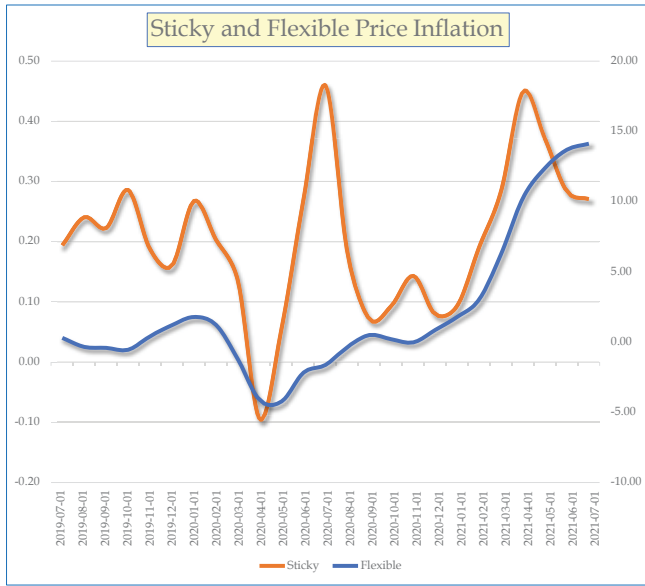


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Before the pandemic, inventories were efficiently thin. When the pandemic began, demand fell causing inventories to leap. That caused businesses to slow production. At the same time, the pandemic decreased productivity and disrupted supply chains. As demand returned, the business inventories to sales ratio then fell to its lowest level in decades. That and supply chain disruptions have caused prices to rise. That's not necessarily inflation.



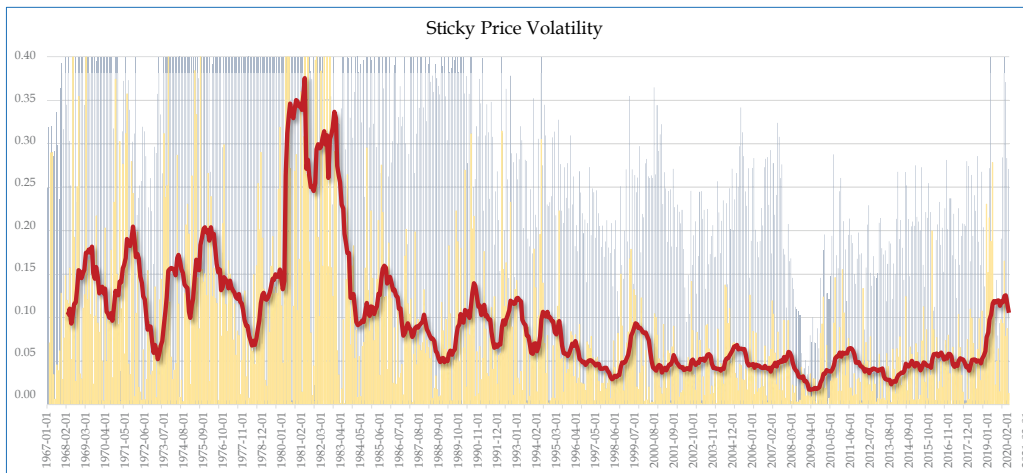
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Prices for goods and services that resist inflation (“sticky items”) rose in Q1 2021 and fell in Q2. Rates for those things that are sensitive to inflation (“flexible items”) started going up last fall. The rise in sticky prices reflected the structural effect of flooding the economy with cash. The rise in flexible prices is, in part, recapture of prior losses. It’s also the groaning sound made by a seriously-damaged and hastily-rebuilt machine (our economy), in which inventories are non-existent, which is just now being restarted, and which surely has some slack and gum in the works. “Wheelspin.” Note that, since May 2021, flexible prices went up while sticky prices went down.

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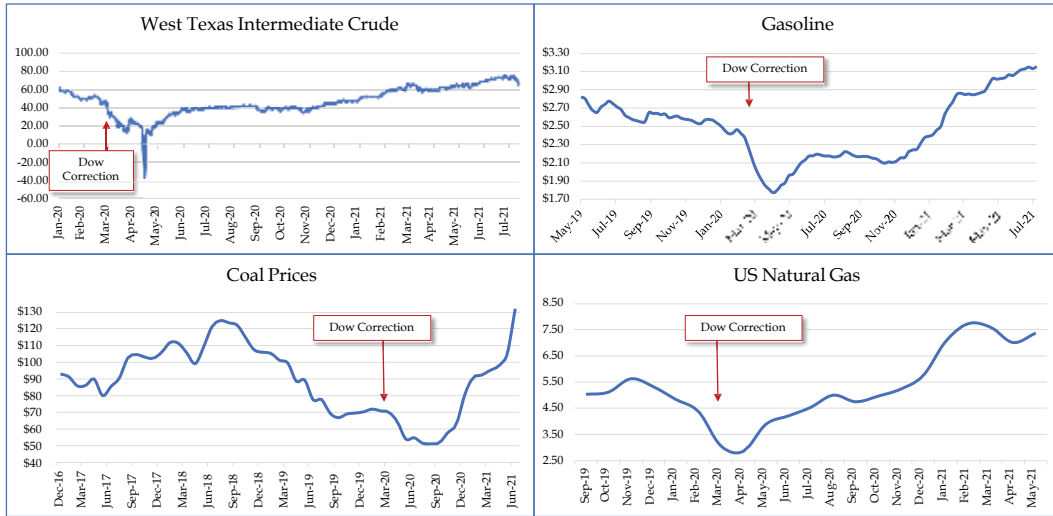
Whether inflation is structurally embedded in the economy is better predicted by sticky price increases than by flexible price increases. In 2021, sticky prices were more volatile than since the late 90s, but nothing like between 1970-1985.



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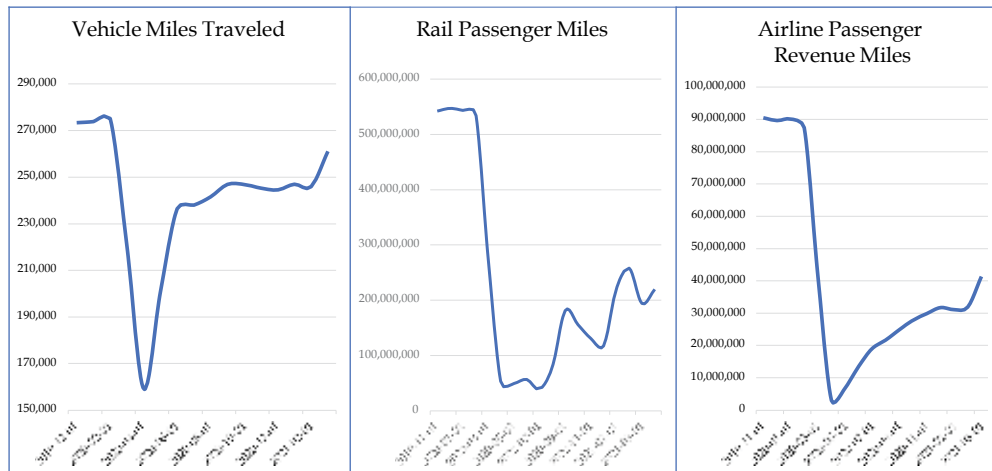
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Energy is the sector that currently leads price increases, but these prices are generally flattening, except for coal.



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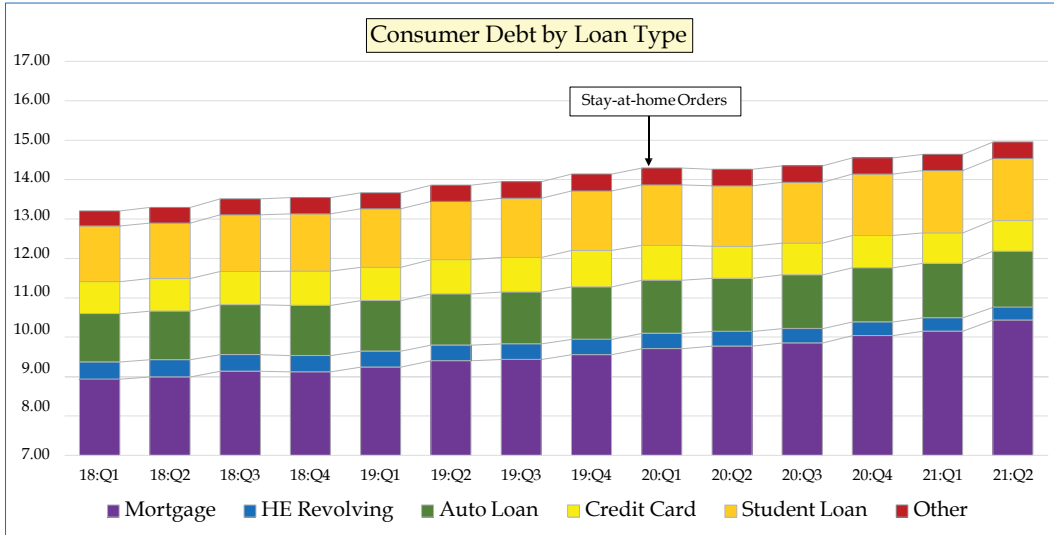
We're moving again on trains, planes, and automobiles. Vehicle and airline miles jumped in March. But rental cars cost more than space travel, and airlines are cutting back some routes because they don't have enough pilots.



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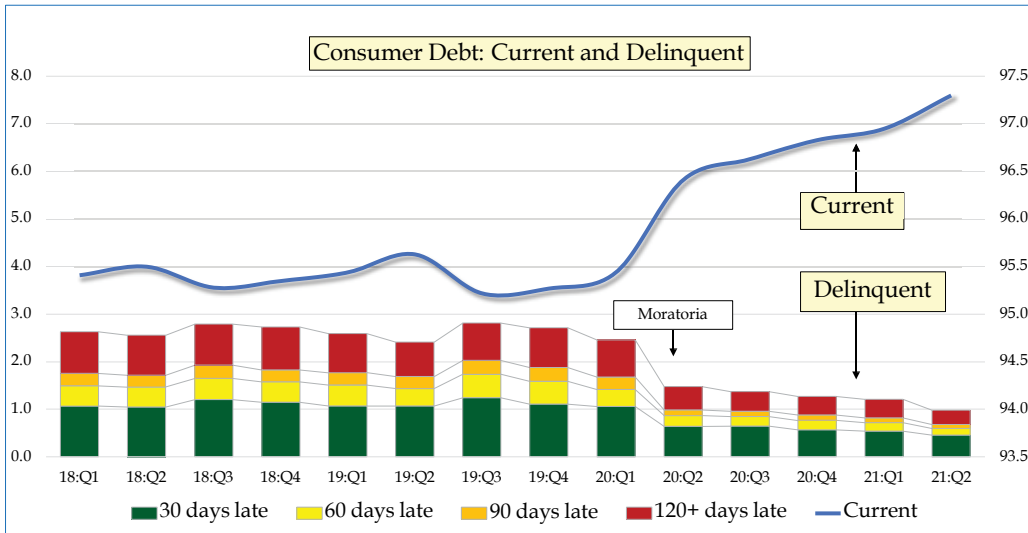
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The pandemic had little effect on consumer debt-incurring behavior. Q2 2021 had a bit of a jump, led by mortgage, auto, and credit card debt.



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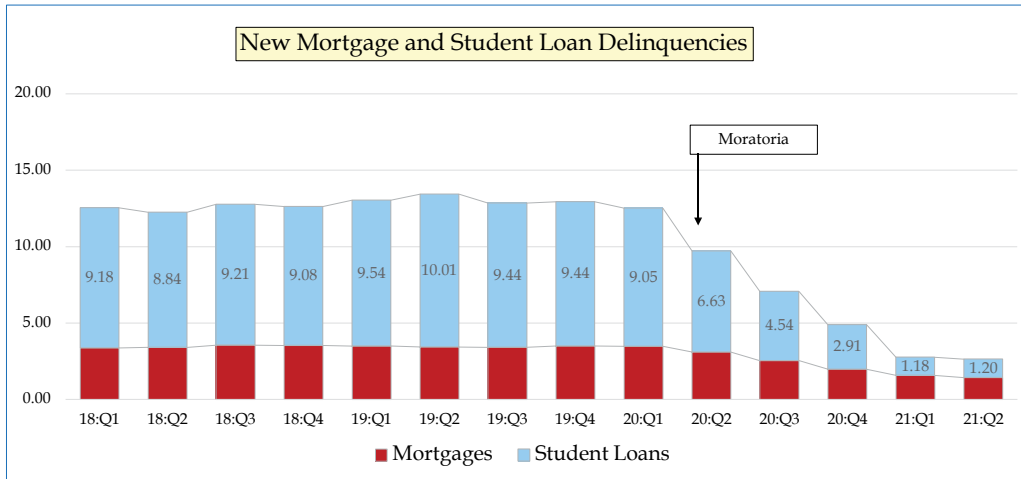
Consumer debt delinquency decreased during the pandemic, because of moratoria and forbearances. In Q2 2021, 60+ day delinquencies dropped about 20%.



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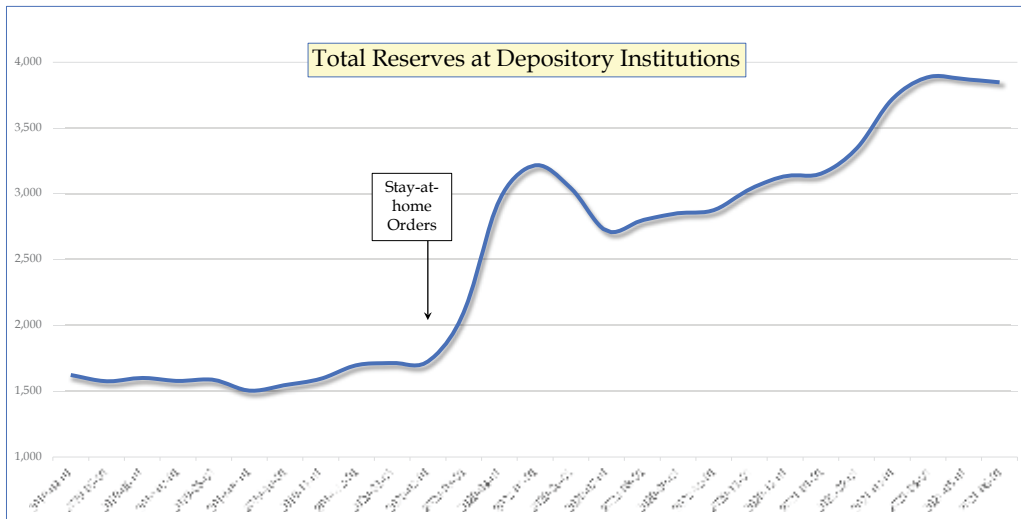
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Delinquency decreased because of moratoria relating to mortgages and student loans. The former is 70% of all consumer debt, the latter is 10%. Auto loan and credit card delinquencies also fell, but not as dramatically. It is uncertain what will happen when moratoria are lifted in and after August 2021.



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Delinquency rates have fallen because of stimulus and moratoria. But lenders are expecting them to rise in the future. Reserve account balances have increased 250% since the first stay-at-home orders.



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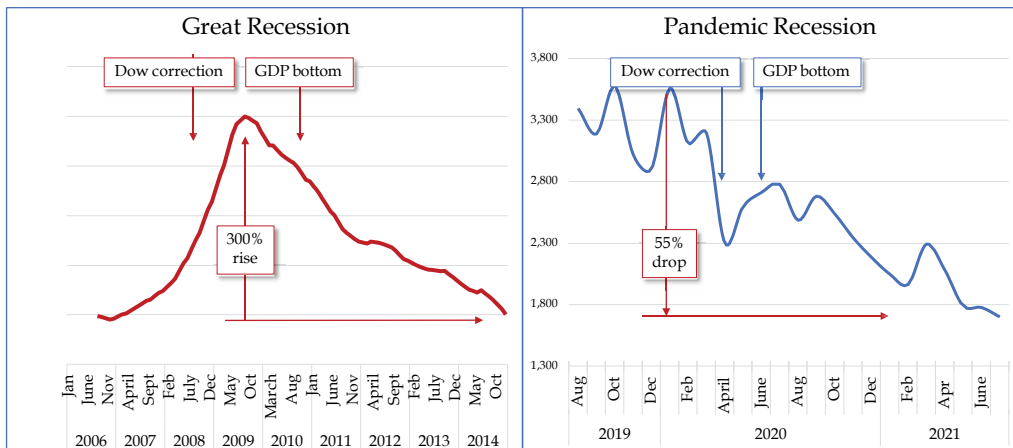
“How did you go bankrupt?” Bill asked.

“Two ways,” Mike said. “Gradually and then suddenly.”

-The Sun Also Rises

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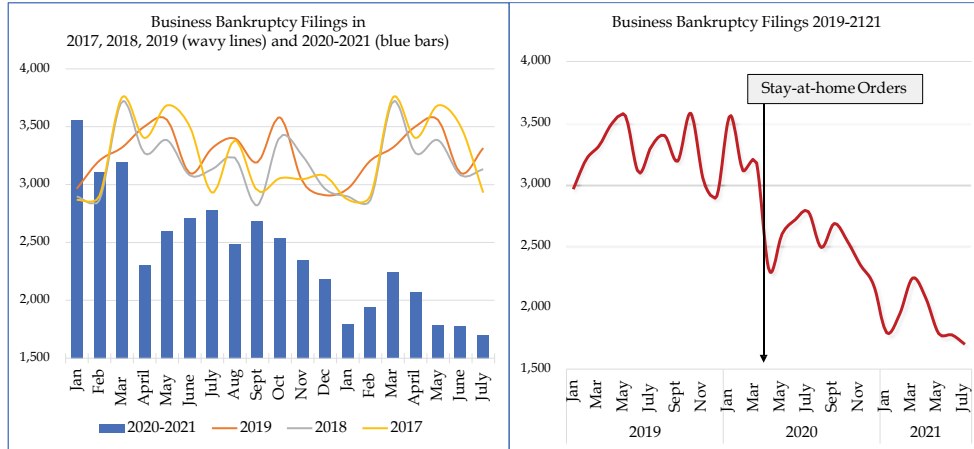
In the great recession, business bankruptcy filings peaked between the Dow correction and the GDP bottom. Conversely, in the pandemic recession, business bankruptcy filings plunged between the Dow correction and the GDP bottom, and then they fell to all-time lows during the third COVID surge. Between January 2020 and January 2021, business filings dropped by half. In July 2021, business filings were the lowest in more than a decade.



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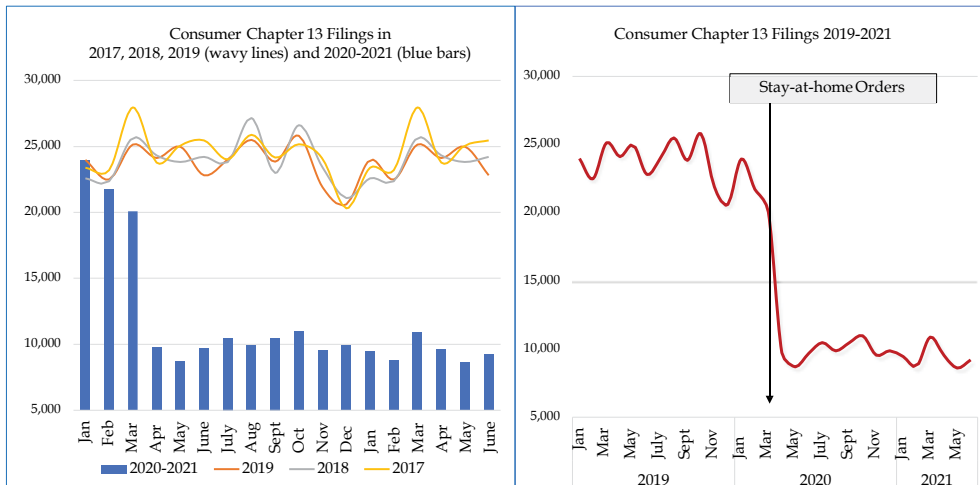
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During the pandemic, business bankruptcy filings fell substantially and have remained historically low since the first stay-at-home orders. (Business bankruptcies are chapter 7 and 11 filings by commercial entities and chapter 13s that include sole proprietorships.)



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During the pandemic, consumer bankruptcy filings fell precipitously and have remained historically low since the first stay-at-home orders. (Consumer bankruptcies are chapter 7, 11, and 13 filings by individuals.)

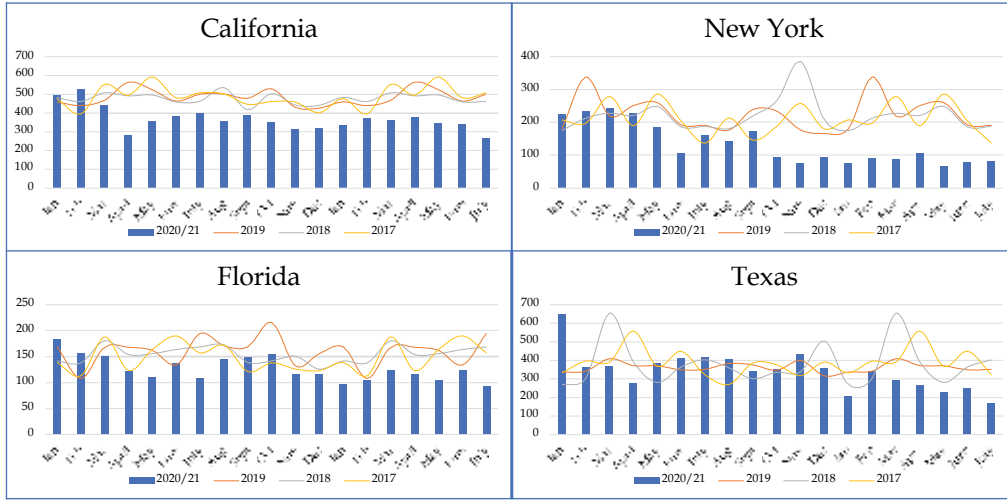


F-2 | United States Courts (uscourts.gov)

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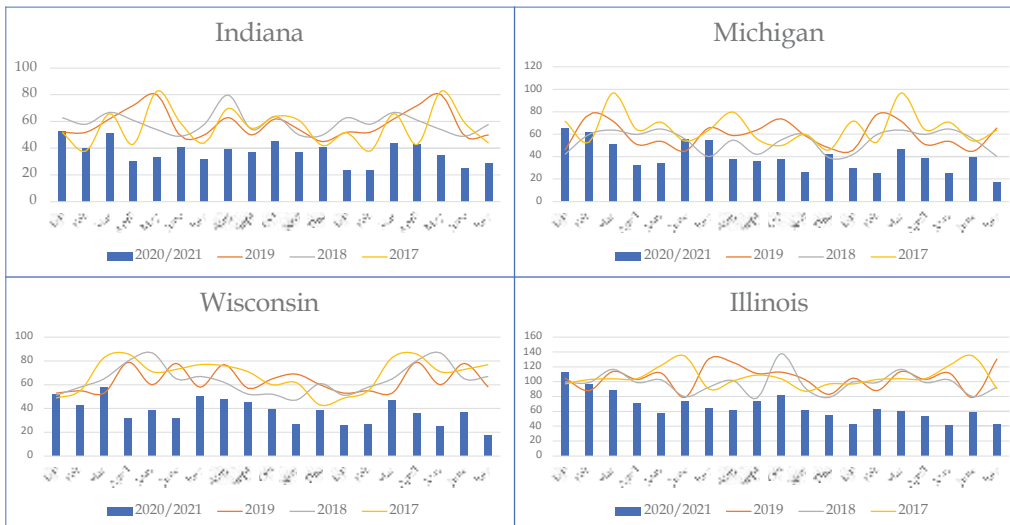
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Business bankruptcy filings in three of the four most populous U.S. states followed the national trend during the pandemic. Texas, one of the most business bankruptcy-active states in 2020, had merely a typical year. Even Texas is off-pace in 2021.



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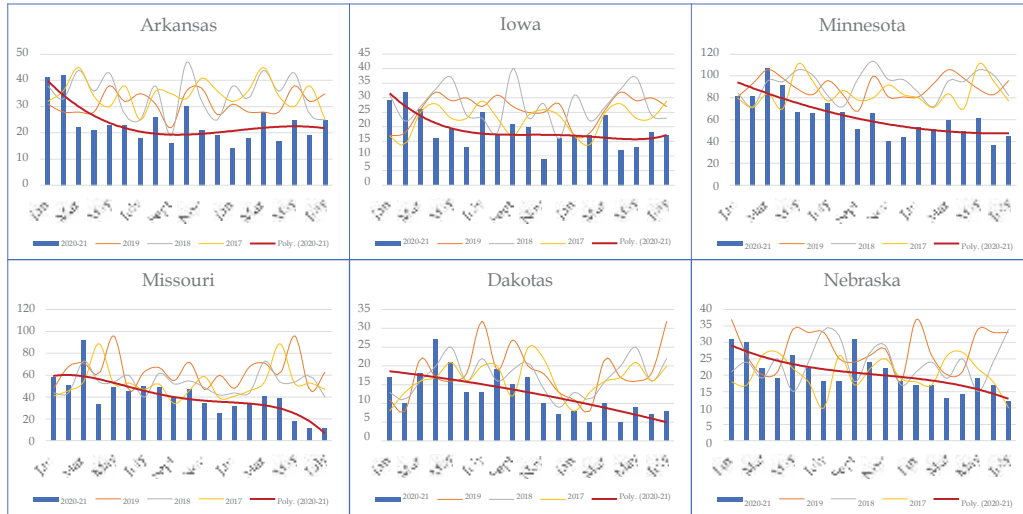
The most populous central states followed the national trend.



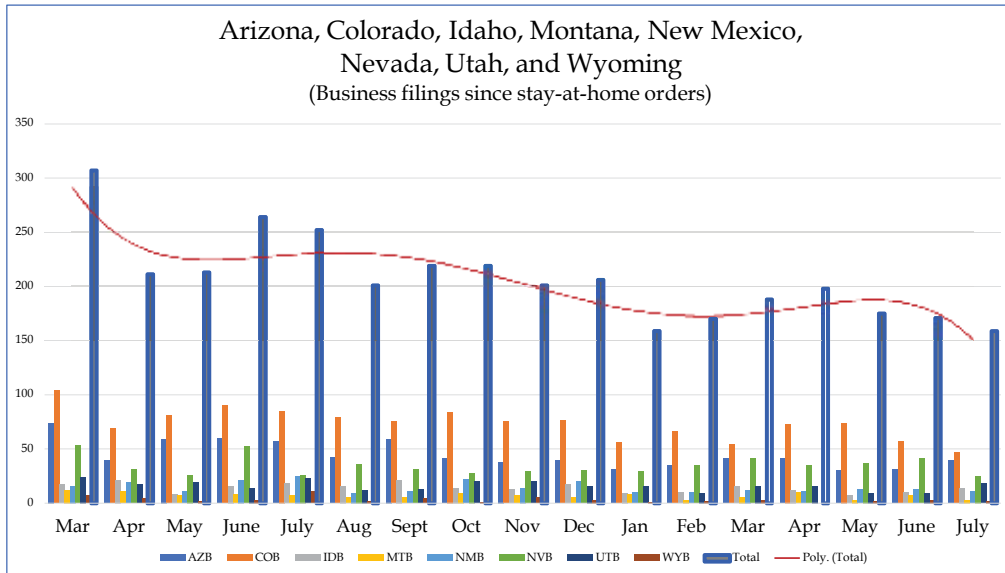
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The Eighth Circuit followed the national trend.

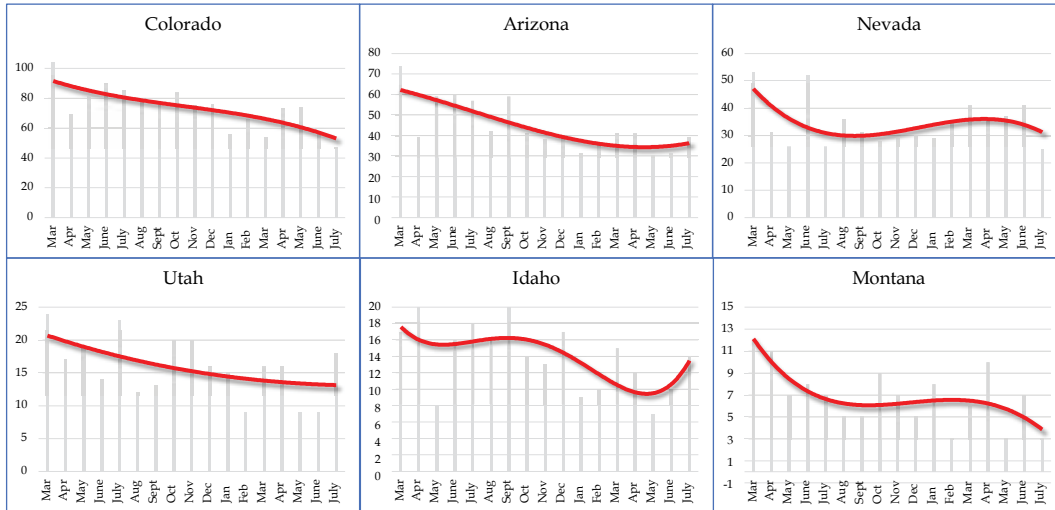


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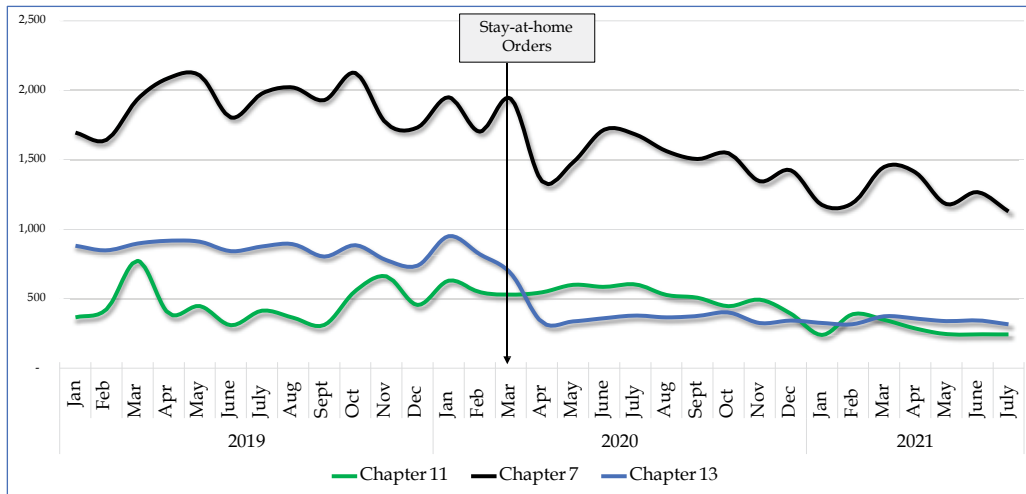
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Rocky Mountain Business Filings Since Stay-at-home Orders



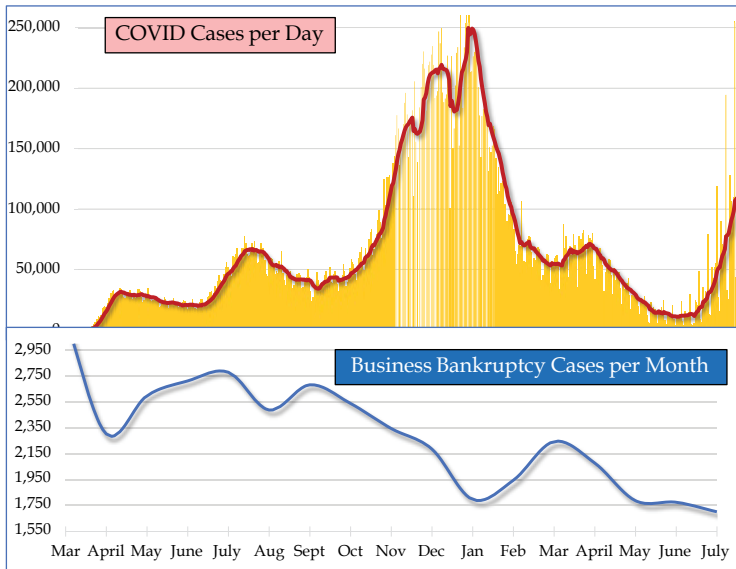
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Business chapter 11s nationally were less affected by the pandemic than business chapter 7s and chapter 13 sole proprietorships. Regardless, in July 2021, business chapter 11s and 7s all fell to all-time lows.



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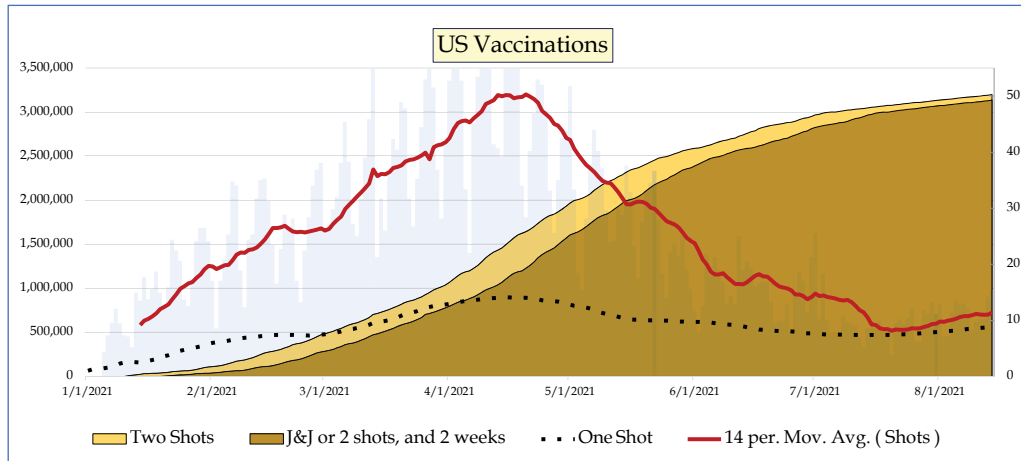
Throughout the pandemic (except for May 2021) there was an inverse correlation between COVID surges and business bankruptcy cases. When COVID cases went up, bankruptcy cases went down, and vice versa.

The correlation was indirect. Bankruptcy filings fell in April because of the chaos initially caused by COVID. They remained low thereafter because of stimulus payments and state and federal moratoriums. They fell after August when COVID surged again, and uncertainty fomented an attitude of “wait and see” and a wave of forbearances.

Bankruptcy filings should increase as uncertainty decreases when COVID decreases, workforce participation increases, prices fall as supply chains heal, and consumer confidence increases. Not yet.

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As of August 7, 2021, 50% of US residents were fully vaccinated (2 shots plus 2 weeks). The shot rate slowed dramatically in mid-April, then began to rise again in July, with the surge. Ten percent of US citizens are COVID survivors. If half of them are immune but unvaccinated, then the immunity rate is now about 55%.



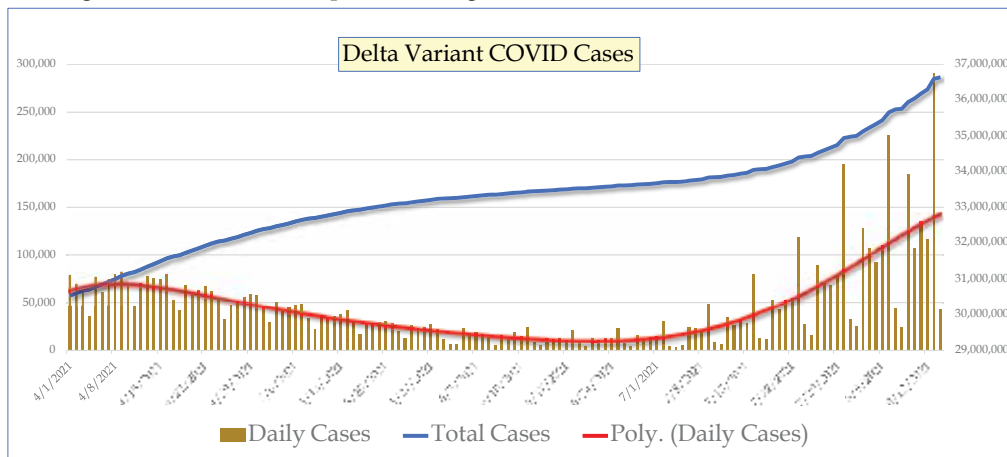
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“We are very concerned about the Delta variant and other variants that could emerge and threaten [economic] recovery. We are a connected global economy. What happens in any part of the world affects all other countries.”

- Treasury Secretary Janet Yellen, July 9, 2021

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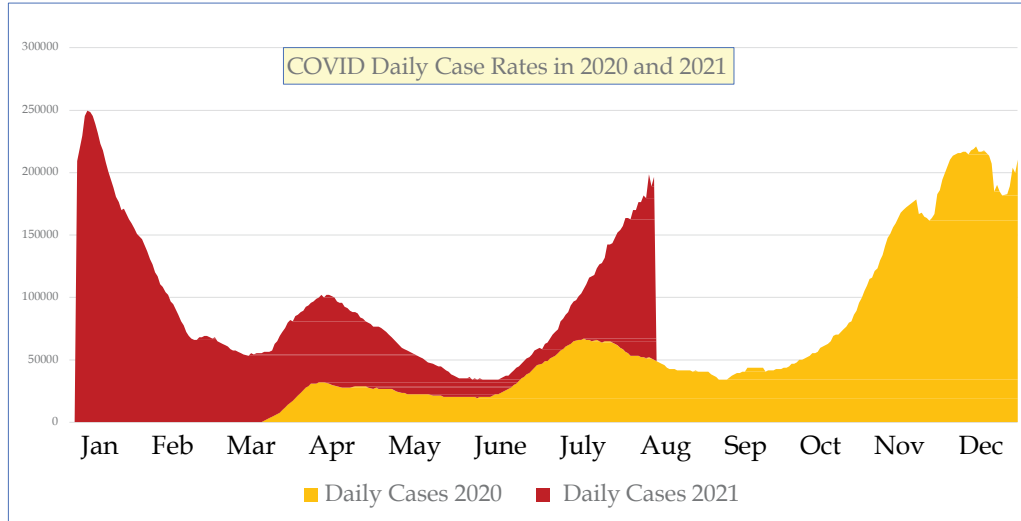
COVID cases began to rise again in mid-June because of falling vaccination rates and the rising incidence of the Delta variant. Daily cases are currently as high as the worst we’ve been through. Nearly 300,000 new cases were reported in the US on August 14, 2021. That was the third highest number since the pandemic began.



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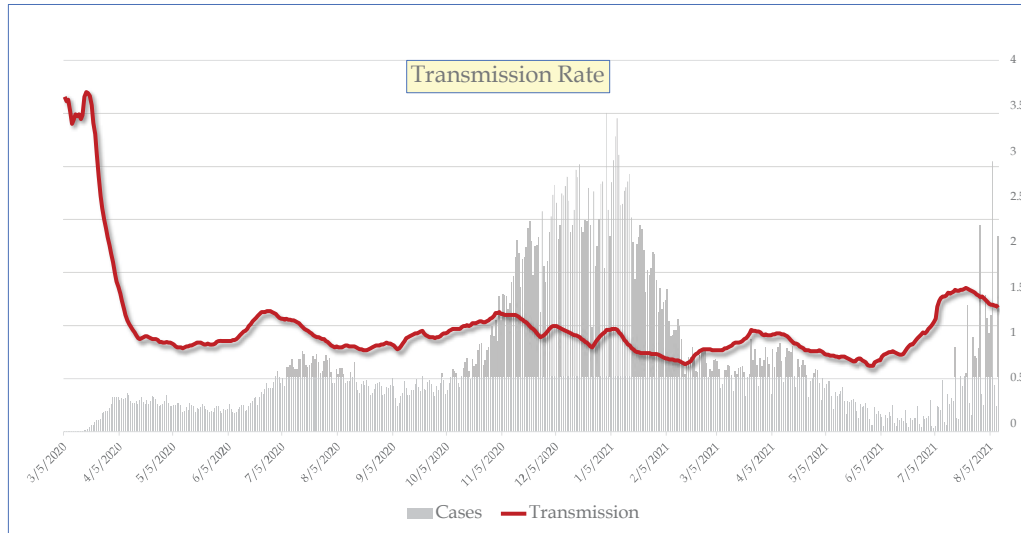
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Vaccinations have been available since January 2021. But COVID case rates since then have remained higher than in 2020.



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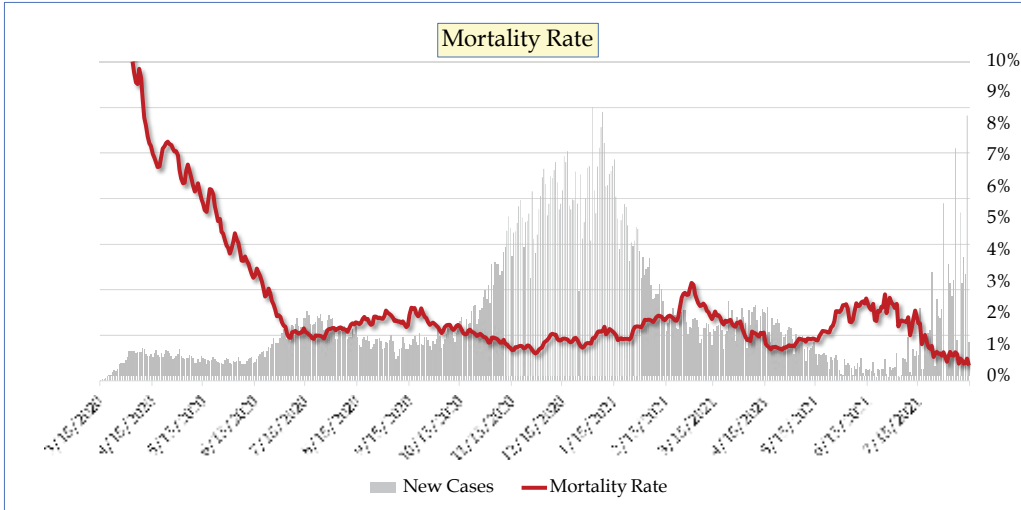
Currently, transmission rates are higher than since April 2020. That's the Delta variant.



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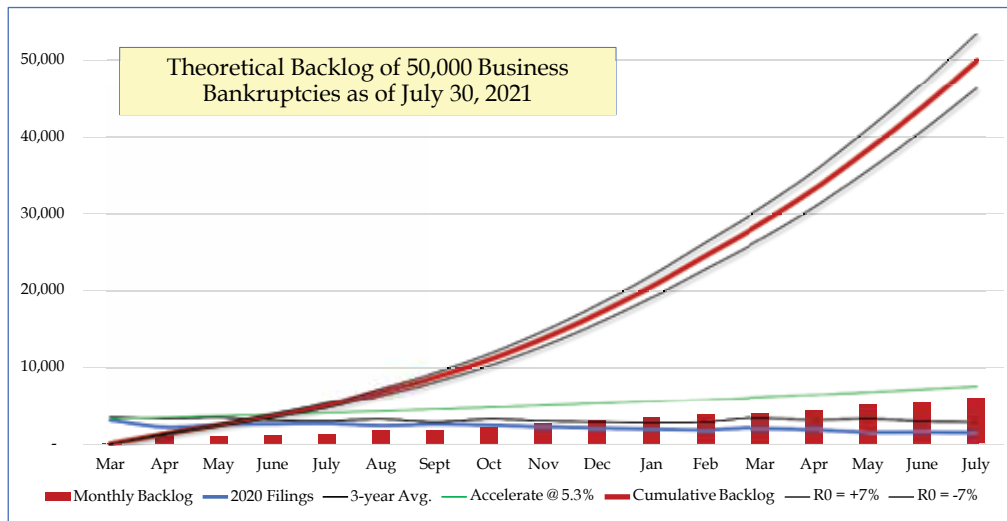
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Currently, the mortality rate is low. But case rates are high and hospitalization rates are increasing. The mortality rate will go up again.



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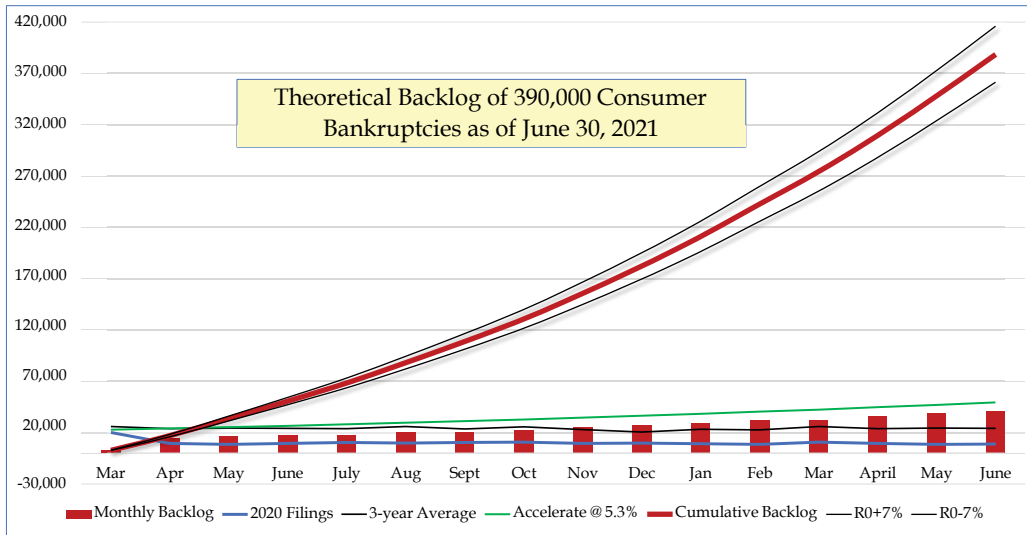
Business bankruptcy filing rates decelerated during the pandemic when we expected them to accelerate (as they did in the great recession), perhaps predicting a backlog.



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Consumer bankruptcy filing rates also decelerated during the pandemic when we expected them to accelerate (as they did in the great recession).



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“We’re recovering, but to a different economy.”

- Fed Chair Jerome Powell, November 10, 2020

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Faculty

J. Thomas Beckett is a shareholder with Parsons Behle & Latimer in Salt Lake City and heads the firm's bankruptcy practice group. He has represented a diverse roster of clients in chapter 11 cases, notably, in the Yellowstone Mountain Club bankruptcy, as lead counsel to the creditors' committee, for which he obtained the equitable subordination of a \$370 million secured loan to enable unsecured creditors to be paid first. Formerly an associate at Milbank in New York City, Mr. Beckett's work experience also includes a year on the staff of the U.S. Senate Judiciary Subcommittee on Constitutional Rights. He recently served as chairman of the board of directors of Clark Planetarium and currently serves on the Utah Supreme Court's Ethics and Discipline Committee. He has maintained a whitewater river guide's license and wilderness first responder certification for 40 years. Mr. Beckett received his B.A. from Brown University in 1979 and his M.B.A. in finance from New York University Stern School of Business Administration in 1986. He also was trained as a mediator at the Harvard Law School's Program on Negotiation.

Hon. Bianca M. Rucker was appointed U.S. Bankruptcy Judge for the Eastern and Western Districts of Arkansas in Fayetteville on April 26, 2021. Prior to her judicial appointment, she was a chapter 7 panel bankruptcy trustee and attorney representing creditors and debtors in consumer and business bankruptcy matters at Rucker Law PLLC, in Fayetteville. Before working as a trustee, Judge Rucker was a partner at Wright, Lindsey & Jennings, LLP (WLJ), where her practice focused on bankruptcy, commercial litigation and insurance defense. She also served as a staff attorney to Hon. Richard D. Taylor (2006-07) and Hon. Ben T. Barry (2007-11) of the U.S. Bankruptcy Court for the Eastern and Western Districts of Arkansas. Judge Rucker has served as president of the Northwest Arkansas Debtor and Creditor Bar Association, and she is an adjunct professor at the University of Arkansas School of Law. She received her B.A. in political science in 2003 from the University of Arkansas at Little Rock and her J.D. with honors in 2006 from the William H. Bowen School of Law.

Thomas J. Salerno is a partner in the Bankruptcy and Creditors' Rights practice at Stinson LLP in Phoenix, where he represents distressed companies, acquirers and creditors in financial restructurings and bankruptcy proceedings, pre- and post-bankruptcy workouts, and corporate recapitalizations. He works with clients from an array of industries, including casinos, resort hotels, sports teams, real estate, high-tech manufacturing, electricity generation, agribusiness, construction, health care, airlines and franchised fast-food operations. Mr. Salerno has represented parties in insolvency proceedings in 30 states and five countries. He has been involved in restructurings in the U.S., U.K., Germany, France, Switzerland, and the Czech and Slovak Republics. In addition, Mr. Salerno taught comparative international insolvency at the University of Salzburg and Gray's Inn School of Law in London, and is an adjunct professor at the Sandra Day O'Connor School of Law at Arizona State University, teaching bankruptcy litigation and advanced chapter 11 bankruptcy. He is also a regular guest lecturer at the Eller MBA Program for the University of Arizona. Mr. Salerno has served as an expert witness on U.S. insolvency law in litigation in Germany, and represented Coyote Hockey LLC, the owners of the Phoenix Coyotes of the National Hockey League (NHL), in historic bankruptcy proceedings that resulted in an unprecedented solution: the NHL purchasing one of its own teams for the first time in the league's 90-year history. He headed the U.S. delegation to the Czech Republic in advising the Czech Government in the historic revamping of its bankruptcy law, which

took effect in January 2008, and he has also advised on revamping insolvency laws in the Dominican Republic and Costa Rica. Mr. Salerno is a member of the UNCITRAL working group on its Insolvency Law Reform Project, completed in early 2007. He is a former ABI Board and Executive Committee member, a past director of the American Board of Certification, a Fellow of the American College of Bankruptcy, and a member of the Plan Issues Advisory Subcommittee for ABI's landmark Bankruptcy Review Commission. Mr. Salerno received his B.A. *summa cum laude* from Rutgers University and his J.D. *cum laude* from Notre Dame Law School, where he served as an editor of the *Notre Dame Law Review*.

Kristina M. Stanger is an attorney and shareholder with Nyemaster Goode, P.C. in Des Moines, Iowa, the state's largest firm, and focuses her practice on creditors' rights and bankruptcy. Her experience spans such industries as retail, grocery, agriculture, health care, construction, transportation and manufacturing, and her practice areas include construction and real estate litigation, creditor rights and bankruptcy litigation, banks and financial institution litigation, and business and commercial litigation. She appears in both federal and state courts for secured and unsecured creditors in a variety of contexts. In addition to her legal practice, Ms. Stanger is a combat-experienced Lieutenant Colonel in the Iowa Army National Guard and a 2017 AMEDD Iron Major. She served more than 20 years as an enlisted soldier, commander and planner for state, national and international operations, and now serves as one of the state of Iowa's highest-ranking females and is the Battalion Commander for the 109th Medical Battalion for the Iowa Army National Guard. Ms. Stanger has held a number of committee positions with the Iowa State Bar Association, is an author and speaker on bankruptcy and commercial law topics, and provides *pro bono* services on behalf of veterans and their families. She also was a member of the 2016 Next Generation Class for the National Conference of Bankruptcy Judges (NCBJ), is a 2018 ABI "40 Under 40" honoree, and chairs IWIRC's Midwest Network. Ms. Stanger is admitted to practice in all state, federal and bankruptcy courts in Iowa and the Eighth Circuit Court of Appeals. Following law school, she interned for Hon. Ronald E. Longstaff of the U.S. District Court for the Southern District of Iowa and clerked for the Iowa Academy of Trial Lawyers U.S. Army Command and General Staff College in 2014. Ms. Stanger graduated with distinguished honors from the 185th Military Regional Training Institute's Officer Candidate School in 2000, received her B.A. *magna cum laude* from Central College the same year, and received her J.D. with high honors from Drake University in 2006, where she was a member of the Order of the Coif, worked on the *Drake Law Review* and was active in its moot court program.