

# DEBTOR/CREDITOR

October 2018

## *Not Paid Until the Check Clears*

If a debtor pays a debt to a creditor by check before the debtor files a bankruptcy petition, but the check does not clear until after the bankruptcy filing, is the payment a pre-bankruptcy or a post-bankruptcy transfer by the debtor? If the transfer is pre-bankruptcy, it is proper, although it might be subject to recovery as a preference depending on the circumstances. If the transfer is post-bankruptcy, it is improper, because post-bankruptcy payments of pre-bankruptcy debts require bankruptcy court approval, which is lacking.

A bankruptcy appellate panel in California recently ruled that an ordinary check does not transfer property until the check clears. Thus, the creditor was required to return the funds to the Chapter 7 trustee.

*Lewis v. Kaelin (In re Cresta Technology Corp.)*, 583 B.R. 224 (Bankr. 9<sup>th</sup> Cir. 2018).

## *Mere Threat Violates Stay*

Mr. Siegal was a minority member of a limited liability company and also the LLC's employee. After Mr. Siegal filed a Chapter 13 bankruptcy petition, the majority members of the LLC requested that he sign an employment agreement and threatened to withhold his compensation until he did. Although Mr. Siegal signed the employment agreement and no compensation was withheld, Mr. Siegal sued the other members for violation of the automatic stay.

A Baltimore bankruptcy judge ruled that a threat to take action which would "disrupt the status quo and inhibit the debtor's ability to effectively proceed through the bankruptcy" is sufficient to constitute a violation of the automatic stay, even where the threat is never carried out. *Siegal v. Everett (In re Siegal)*, 2018 Bankr. LEXIS 2374 (Bankr. D. Md. 2018).

## *Bankruptcy Filing Freezes Creditor Rights*

Under Maryland law, in order to perfect a security interest in all assets of a borrower, a lending bank must file a financing statement. The financing statement lapses after five years, unless the bank timely files a continuation statement. If the financing statement lapses, the perfected security interest of a junior lender will move into first position. An exception to the automatic stay permits post-bankruptcy filing of a continuation statement.

First Bank loaned Borrower funds secured by all assets and filed a financing statement. Subsequently, Second Bank made a secured loan and filed a financing statement. Borrower filed a Chapter 11 petition, and First Bank's financing statement expired without a continuation statement. Second Bank sought a determination that its security interest was now in first position in the bankruptcy case. A Maryland bankruptcy judge rejected Second Bank's argument, explaining that federal bankruptcy law froze the rights of creditors when the bankruptcy commenced, and the subsequent expiration of First Bank's financing statement had no effect in the case. *Firsttrust Bank v. Indus. Bank (In re Essex Constr., LLC)*, 2018 Bankr. LEXIS 2908 (Bankr. D. Md. 2018)



*This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation. Congress has required bankruptcy attorneys to state: "I am a debt relief agency. I help people file for bankruptcy relief under the Bankruptcy Code." 11 U.S.C. § 528. If you wish to receive "Notes on Debtor/Creditor Relations", go to [www.jamesolsonattorney.com/newsletter.html](http://www.jamesolsonattorney.com/newsletter.html) and click on the link at the word "here".*

Prepared by James C. Olson, Attorney and Counselor at Law