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# Alert

## US Supreme Court Allows Repossessing Secured Lender to Hold Collateral Pending Bankruptcy Stay

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A secured lender's "mere retention of property [after a pre-bankruptcy–repossession] does not violate" the automatic stay provision [§ 362(a)(3)] of the Bankruptcy Code ("Code"), held a unanimous U.S. Supreme Court on Jan. 14, 2021. *City of Chicago v. Fulton*, 2021 WL 125106, *4 (Jan. 14, 2021). Reversing the Seventh Circuit's affirmance of a bankruptcy court judgment holding a secured lender in contempt for violating the automatic stay, the Court resolved "a split" in the Circuits. *Id.*, at *2. The Second, Eighth and Ninth Circuits had agreed with the Seventh Circuit. But as we noted in our Oct. 31, 2019 *Alert*, the Third Circuit, like the D.C. and Tenth Circuits, had reached the right result in other cases. SRZ represented five law professors who submitted an amicus brief supporting the prevailing party in the Supreme Court.

**No Control**

The Court rejected the debtors' argument in *Fulton* that the repossessing lender had exercised "control over" their property in violation of the Code's stay. *Id.* The "language of [Code] § 362(a)(3) implies that something more than merely retaining power is required" for a stay violation. *Id.*, at *3.

**No Automatic Turnover**

"Reading § 362(a)(3) to cover mere retention of property," as the Seventh Circuit did, would make the Code's turnover provision (§ 542) meaningless and inconsistent. Because section 542 "carves out exceptions to the turnover command" and does not "mandate turnover" of valueless property, it would be "odd… to require a creditor to do immediately what § 542 specifically excuses," as the Seventh Circuit held. In sum, the stay provision (§ 362(a)(3)) imposes "no turnover obligation." *Id.* at *4. As the Tenth Circuit stressed, "[s]tay means stay, not go." *In re Cowen*, 849 F.3d 943, 949 (10th Cir. 2017). Secured lenders with statutory defenses to a debtor's turnover claim can now retain possession pending a bankruptcy court order resolving the issue after a hearing.

**Comment**

The Court's sensible, practical decision in *Fulton* keeps the right balance between debtors' and creditors' rights. By maintaining the status quo and the debtor's right to reclaim its property, it also relieves secured lenders from the threat of bankruptcy court sanctions. The Code's automatic stay does not require lenders, on pain of sanctions, to do what the Code's turnover provision does not — immediately surrender repossessed collateral in the absence of a court ruling.

*Fulton* hardly threatens a debtor's ability to reorganize. The debtor or trustee can quickly start a turnover proceeding to recover essential property with a court order. That is exactly what happened in *In re Denby-Peterson*, 941 F.3d 115 (3d Cir. 2019). Although debtors might argue that they should not

have this obligation as a policy matter, the Code makes no such provision. *Mission Products Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1665 (2019) ("Code … aims to make reorganizations possible [but] does not permit anything and everything that might advance that goal.").

*Authored by Michael L. Cook.*

If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or the author.

Schulte Roth & Zabel
New York | Washington DC | London
www.srz.com