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Ninth Circuit Allows Bankruptcy Courts to Recharacterize Loans as Equity, Applying State Law

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The Ninth Circuit held on April 30, 2013 that a bankruptcy court “has the authority to determine whether a transaction creates a debt or an equity interest for purposes of [Bankruptcy Code] § 548, and that a transaction creates a debt if it creates a ‘right to payment’ under state law.” *In re Fitness Holdings International, Inc.*, 2013 WL 1800000, *1 (9th Cir. April 30, 2013). The court agreed with five other circuits, but explicitly followed the reasoning of the Fifth Circuit’s recent *In re Lothian Oil, Inc.* decision. 650 F.3d 539, 543–44 (5th Cir. 2011) (looked to state law to “distinguish between debt and equity”). In this article, SRZ business reorganization partner Michael L. Cook discusses the Ninth Circuit’s decision.

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