

ALERTS

Fifth Circuit Orders Mandatory Subordination of Contractual Guaranty Claims

June 5, 2015

A creditor's guaranty claim "arising from equity investments in a debtor's affiliate should be treated the same as equity investments in the debtor itself — i.e., ... subordinated to the claims of general creditors," held the U.S. Court of Appeals for the Fifth Circuit on April 28, 2015. *In re American Housing Foundation*, 2015 WL 1918854 (5th Cir. April 28, 2015). Also reversing the trustee's preference judgment against the creditor because the debtor's business was not a "Ponzi scheme," the court held that the creditor could rely on the "ordinary course of business defense" to the trustee's preference claim. Finally, because the record before it was unclear as to whether the creditor "gave value to" the debtor and because the "bankruptcy court applied the wrong standard" as to whether the creditor had received \$1 million "in good faith," the Fifth Circuit reversed the lower court's dismissal of the trustee's fraudulent transfer claim and remanded the case for trial. This case deals with important issues arising under Bankruptcy Code Sections 510(b) (mandatory subordination of securities fraud claims); 547(c)(2) (ordinary course of business defense to preference claims); and 548(c) (good-faith-for-value defense to fraudulent transfer claims).

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