

## Know your limits? The statute of limitations in the Bankruptcy Code

By John B. Butler III, Esq.

The bankruptcy statute of limitations can provide an effective defense when a bankruptcy trustee brings a lawsuit against your client. Knowing and using the bankruptcy statute of limitations is an important tool for protecting clients in bankruptcy court.

### THE BANKRUPTCY STATUTE OF LIMITATIONS

The bankruptcy statute of limitations is found in 11 U.S.C. § 546(a), which provides in pertinent part:

- (a) An action or proceeding under Section 544, 545, 547, 548 or 553 of this title may not be commenced after the *earlier of*—
- (1) the *later of*—
- (A) 2 years after the entry of the order for relief; or
- (B) 1 year after the appointment or election of the first trustee under Section 702, 1104, 1163, 1202 or 1302 of this title if such appointment or such election occurs before the expiration of the period specified in subparagraph (A); or
- (2) the time the case is closed or dismissed.<sup>1</sup>

The language “the earlier of the later of” in Section 546(a) is confusing. The easy part is what comes earlier, the events in subsection (1) or the event in subsection (2). The closing of the bankruptcy case under Section 350(a)<sup>2</sup> is an administrative event where the trustee is

discharged of his duties, and the bankruptcy case is ended. An action by a trustee or debtor in possession will almost certainly be brought before the case is closed, so that option is not used often.

The real confusion is found in subsection (1) where the deadline is determined by the later of subsection (A) and subsection (B). If the case is open, the deadline is the later of two years from the entry of the order for relief, or, if a trustee was appointed or elected during the two-year period, one year from the date of the appointment or election of the first trustee.

---

Because the trustee was appointed and elected during the two years following the order for relief, the deadline is extended to one year from the appointment and election of the trustee.

---

This test is usually applied when a case was originally filed as a Chapter 11 case with a debtor in possession, but is converted to Chapter 7, and an interim trustee is appointed who brings a lawsuit against a party. The crux of the determination is based on when the trustee was appointed and elected under Section 702, 1104, 1163, 1202 or 1302.

For example, a voluntary Chapter 11 petition for relief is filed Jan. 26, 2012. On June 29, 2012, the case is converted to one under Chapter 7, and on the same day, an interim trustee is appointed by the court. On July 27, 2012, the Section 341 meeting of creditors is held and, as is usually the case, no replacement trustee is elected pursuant to

Section 702(b). Thus, under Section 702(d), the interim trustee becomes the trustee.

The deadline under Section 546(a) is therefore the later of two years from the order for relief dated Jan. 26, 2012, or one year from the appointment and election of the trustee July 27, 2012. Therefore, the deadline is Jan. 26, 2014.<sup>3</sup>

A slight variation of the dates exemplifies how the deadline can change. If the Chapter 11 order for relief remains Jan. 26, 2012, but the Section 341 meeting/election date is July 27, 2013, the deadline is the later of

Jan. 26, 2014, or July 27, 2014. Because the trustee was appointed and elected during the two years following the order for relief, the deadline is extended to one year from the appointment and election of the trustee, which will be greater than two years after the order for relief.

Consider another variation: the Chapter 11 order for relief remains Jan. 26, 2012, but the Section 341 meeting/election date is Jan. 29, 2014. Now the deadline is simply Jan. 26, 2014, because the trustee was not appointed and elected during the two-year period after the order for relief; therefore, there is no extension of the two-year period.<sup>4</sup>

The chart below may help with this concept, but we need to examine some of the terms in subsection (1) determining when the key events occur, such as “order for relief” and “appointment or election of the first trustee.”

### ORDER OF RELIEF

Since the two-year period of Section 546(a)(1) is calculated from the date of entry of the order for relief, it is essential to define the term “order for relief.” Fortunately, in voluntary cases, the most frequent type of bankruptcy



**John B. Butler III** was law clerk to U.S. Bankruptcy Judge J. Bratton Davis, a standing Chapter 13 trustee for 15 years and an adjunct professor of bankruptcy law at the University of South Carolina School of Law. He is the author of the two-volume “Bankruptcy Handbook” from Knowles Publishing, and he specializes in representing creditors in bankruptcy cases in South Carolina.

case, the order for relief is the date of the commencement of the voluntary case,<sup>5</sup> which is when the petition is filed.<sup>6</sup>

The date of the order for relief is less clear in an involuntary petition. The commencement of an involuntary petition against an alleged debtor is not the same as an order for relief. The order for relief must be entered by the court after a hearing if the involuntary petition is resisted, or without a hearing if the involuntary petition is not timely controverted.<sup>7</sup> The calculation of the two-year time period under Section 546(a)(1) starts when the order for relief is entered by the court against the involuntary debtor — not when the involuntary petition was filed.<sup>8</sup>

Much of the confusion surrounding Section 546(a) arises when a case is converted from one chapter to another. It is, therefore, essential to note that pursuant to Section 348(a)<sup>9</sup>, the conversion of a case from one chapter to another does not change the date of the order for relief for purposes of calculating the Section 546(a) deadline.<sup>10</sup>

In voluntary cases, the most frequent type of bankruptcy case, the order for relief is the date of the commencement of the voluntary case, which is when the petition is filed.

## APPOINTMENT OR ELECTION OF THE FIRST TRUSTEE

The phrase “appointment or election of the first trustee under Section 702, 1104, 1163, 1202 or 1302” has also caused confusion. In a Chapter 13 case, it is clear, because the standing Chapter 13 trustee is appointed when petition for relief is filed and the order for relief is entered pursuant to Section 1302(a).<sup>11</sup> The same would be true in a Chapter 12 case where the standing trustee is appointed under Section 1202(a). The confusion arises in a Chapter 7 case.

It would seem the appointment or election of a Chapter 7 trustee would mean when the interim trustee is appointed by the court pursuant to Section 701(a). This is usually shortly after the filing of a voluntary petition or conversion of the case from another chapter to Chapter 7.

The majority of cases, however, hold that the appointment of the interim Chapter 7 trustee is not the “appointment or election of the first trustee under Section 702.” The majority rule is that the election date under Section 702(b)<sup>12</sup> (which is the date of the meeting of creditors)

Was a trustee appointed or elected during the two-year period after the entry of the order of relief?	
YES	NO
Statute of limitation is the later of: two years after the entry of the order for relief OR one year after the appointment or election of the first trustee.	Statute of limitation is two years after the entry of the order for relief.

is the beginning of the one-year time period of Section 546(a)(1)(B), even if no successor trustee is elected and the interim trustee continues to serve as the trustee.<sup>13</sup>

The majority case law position is that the election of a successor trustee at the meeting of creditors delays the date of the appointment or election of a Chapter 7 trustee under Section 702. An issue may arise, therefore, with respect to the date Section 546(a)(1)(B) begins, when a Chapter 11 trustee is appointed.

entry of the order for relief’ for the application of Section 546(a)(1)(A) in the converted case. September 27, 1996 was the date ‘1 year after the appointment ... of the first trustee under ... 702.’ The later of the two — and the last date on which the original trustee could timely file an adversary proceeding under 11 U.S.C. § 548 — was June 28, 1997. He filed his complaint after that. There is no way around it, then. The plain language of Sections 348 and 546, which this court is obligated to apply, time-bars the estate’s claim under Section 548 against the defendants. They are entitled to dismissal of the plaintiff’s complaint, as originally drawn” (footnote omitted).

<sup>4</sup> See *In re Draiman*, 714 F.3d 462, 463-64 (7th Cir. 2013) (Bankruptcy court erred in finding “date of appointment or election under Section 702” was date of appointment for the interim trustee instead of later date of the first meeting of creditors, even though no successor trustee was elected at the first meeting of creditors. Therefore, bankruptcy court erred in finding the trustee was appointed within two years after the order for relief and a one-year extension was applicable. Court of Appeals held permanent trustee must be elected or appointed within the two-year period in order to trigger the extension, and the election of the trustee occurred outside the two-year period. Therefore, there was no one-year extension, and the complaint was not timely filed. Chapter 11 case filed May 14, 2009; case converted to Chapter 7 on May 13, 2011; interim trustee appointed May 13, 2011, and no successor trustee appointed at first meeting June 30, 2011; adversary proceeding filed May 11, 2012); *In re Am. Pad & Paper Co.*, 478 F.3d 546 (3d Cir. 2007) (Complaints were not timely filed, because successor trustee was not elected at the Section 341 meeting until after expiration of the initial two-year period. Appointment of the interim trustee prior to expiration of the initial two-year period did not extend the deadline by one year; therefore, the complaints would have had to be filed by Feb. 14, 2002. Chapter 11 cases filed Jan. 14, 2000; Chapter 11 cases converted Jan. 3, 2002; interim Chapter 7 trustee appointed Jan. 3, 2002; successor Chapter 7 trustee elected at 341 meeting Feb. 13, 2002; first complaint filed Aug. 8, 2002); *In re NM Holdings Co.*, 405 B.R. 830, 853 (Bankr. E.D. Mich. 2008), adopted, 411 B.R. 542 (E.D. Mich. 2009), *aff’d*, 622 F.3d 613 (6th Cir. 2010) (Chapter 11 cases filed March 28,

Section 546(a)(1)(B) also refers to the appointment or election of a Chapter 11 trustee under Section 1104. Section 1104(a)<sup>14</sup> provides for the initial appointment of a trustee, and Section 1104(b)(1)<sup>15</sup> provides for the election of a successor trustee on request of a party at a meeting of creditors.

It remains unclear whether the requirement that a party in interest must request the appointment and election of a Chapter 11 trustee is sufficient to distinguish the beginning of the Section 546(a)(1)(B) deadline from the Section 702 election deadline. **WJ**

## NOTES

<sup>1</sup> Emphasis added.

<sup>2</sup> 11 U.S.C. § 350(a) states, “After an estate is fully administered and the court has discharged the trustee, the court shall close the case.”

<sup>3</sup> See *In re Am. Energy Trading*, 291 B.R. 159, 163 (Bankr. W.D. Mo. 2003) (Chapter 11 filed Sept. 8, 1999; case converted to Chapter 7 and trustee appointed July 14, 2000; adversary commenced July 12, 2002, was determined to be untimely); *In re Quality Pontiac Buick GMC Truck*, 222 B.R. 865, 868 (Bankr. D. Minn. 1998) (“Thus, June 28, 1997, was the date ‘2 years after the

2003; Chapter 11 cases converted Jan. 11, 2006; Chapter 7 trustee appointed Jan. 19, 2006; complaint filed March 31, 2006. Deadline was March 28, 2005 because there was no extension since trustee was not appointed during two years after petition for relief.); *In re Hydro-Action Inc.*, 341 B.R. 186, 189 (Bankr. E.D. Tex. 2006) (Because no trustee was appointed or elected two-years after the order for relief, subparagraph (A) set the deadline for bringing actions under Sections 544, 547 and 548 at two years after the order for relief.)

<sup>5</sup> 11 U.S.C. § 301(b) states, "The commencement of a voluntary case under a chapter of this title constitutes an order for relief under such chapter."

<sup>6</sup> 11 U.S.C. § 301(a) states, "A voluntary case under a chapter of this title is commenced by the filing with the bankruptcy court of a petition under such chapter by an entity that may be debtor under such chapter."

<sup>7</sup> See 11 U.S.C. § 303(h).

<sup>8</sup> *In re Gen. Creations Inc.*, 343 B.R. 548, 552 (Bankr. W.D. Va. 2006) (Involuntary petition filed April 28, 2003; order for relief entered and interim trustee appointed July 22, 2003; Section 341 meeting held and interim trustee became final trustee Sept. 21, 2003; complaint filed July 22, 2005. The court rejected the defendant's argument that the complaint was untimely, because it was filed 731 days after petition for relief.); *In re Harry Levin Inc.*, 175 B.R. 560, 571 (Bankr. E.D. Pa. 1994) (Involuntary petition filed Jan. 29, 1992; order for relief entered March 5, 1992, which was the date for starting calculation under Section 546(a)).

<sup>9</sup> 11 U.S.C. § 348(a) states, "Conversion of a case from a case under one chapter of this title to a case under another chapter of this title constitutes an order for relief under the chapter to which the case is converted, but, except as provided in subsections (b) and (c) of this section, does not effect a change in the date of the filing of the petition, the commencement of the case or the order for relief."

<sup>10</sup> *In re Wofford*, 2012 WL 3070625 (Bankr. E.D. Tenn. July 30, 2012) ("Section 348 of the Bankruptcy Code provides that conversion has no effect on the date of the order for relief. 11 U.S.C.A. § 348(a)."); *In re Wray*, 258 B.R. 777, 781 (Bankr. D. Idaho 2001) ("The trustee has attempted to read this section in such a fashion that the conversion date is the date of the order for relief for purposes of Section 546(a)(1) even though Section 546 is not listed in Section 348(b). The Trustee provides no decisional authority supporting her interpretation."); *In re Quality Pontiac*, 222 B.R. at 868.

<sup>11</sup> See *In re Bodenstein*, 253 B.R. 46, 50 (B.A.P. 8th Cir. 2000) ("The debtors filed their petition on November 21, 1996, and the order for relief was entered that same day. In accordance with Section 547(a)(1)(A), the period of two years after the entry of the order for relief expired

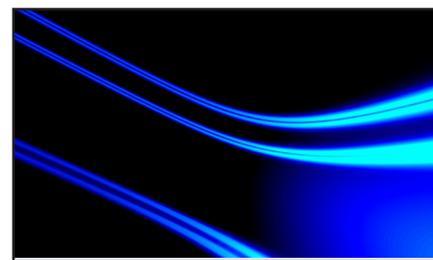
on November 21, 1998. The first trustee in this case, the Chapter 13 trustee, was appointed on the petition date; therefore, the alternate period enumerated in Section 547(a)(1)(B) of one year after the appointment of the first trustee expired on November 21, 1997. The later of these two dates is November 21, 1998. Accordingly, the time to initiate an avoidance action pursuant to Section 547 expired on November 21, 1998.").

<sup>12</sup> 11 U.S.C. § 702(b) states, "At the meeting of creditors held under Section 341 of this title, creditors may elect one person to serve as trustee in the case if election of a trustee is requested by creditors that may vote under subsection (a) of this section, and that hold at least 20 percent in amount of the claims specified in subsection (a)(1) of this section that are held by creditors that may vote under subsection (a) of this section."

<sup>13</sup> See *In re Draiman*, 714 F.3d at 463-64; *In re Am. Pad & Paper Co.*, 478 F.3d at 552; *In re Maxway Corp.*, 27 F.3d 980, 984 (4th Cir. 1994) (With respect to interpreting pre-1994 version of Section 546(a), the court said, "[T]he two-year limitations period for filing an avoidance action does not begin to run until a permanent trustee is selected pursuant to 11 U.S.C.A. § 702."); *In re Crowe Rope Indus.*, 311 B.R. 313, 314 (Bankr. D. Me. 2004) (Date of appointment or election of Chapter 7 trustee under Section 702 was the date of the Section 341 meeting, at which no successor trustee was appointed nor interim trustee under §701.); *In re Meyer's Bakeries*, 377 B.R. 229, 231 (Bankr. W.D. Ark. 2007) ("The date of the Section 341(a) meeting is commonly recognized as the date that the interim trustee becomes the trustee pursuant to 11 U.S.C. § 702(d)."); *Grella v. Zimmerman (In re Art & Co. Inc.)*, 179 B.R. 757, 762 (Bankr. D. Mass. 1995). Compare *In re Parmetex Inc.*, 199 F.3d 1029, 1031 (9th Cir. 1999) (Under pre-1994 version of Section 546(a) the "statute of limitations begins to run on the date the interim trustee is appointed pursuant to Section 701 of the Bankruptcy Code.").

<sup>14</sup> 11 U.S.C. § 1104 provides in pertinent part, "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."

<sup>15</sup> 11 U.S.C. § 1104(b)(1) states, "Except as provided in section 1163 of this title, on the request of a party in interest made not later than 30 days after the court orders the appointment of a trustee under subsection (a), the United States trustee shall convene a meeting of creditors for the purpose of electing one disinterested person to serve as trustee in the case. The election of a trustee shall be conducted in the manner provided in subsections (a), (b) and (c) of Section 702 of this title."



## WESTLAW JOURNAL DERIVATIVES

Losses stemming from complex derivatives investments linked to subprime mortgages and other debt instruments have led to a number of major lawsuits across the nation involving billions of dollars and many new important legal issues. This newsletter reviews cutting-edge cases, informing you of the most crucial developments in derivatives litigation nationwide. You'll receive detailed, continual coverage of litigation involving fiduciary duties, mortgage-backed securities, collateralized debt obligations, swaps, options, futures, and hedge funds.

Call your West representative for more information about our print and online subscription packages, or call 800.328.9352 to subscribe.