NORTON JOURNAL OF BANKRUPTCY LAW AND PRACTICE

Vol. 23, No. 2 (2014)

Norton Journal of Bankruptcy Law & Practice (USPS 012-091), (ISSN 1059-048X) is published bimonthly, six times per year, by Thomson Reuters, 610 Opperman Drive, Eagan, MN 55123. Subscription Price: $546.96 annually. Periodicals postage paid at St. Paul, MN, and additional mailing offices. Postmaster: send address changes to Journal of Bankruptcy Law & Practice, PO Box 64526, St. Paul, MN 55164-0526.

Managing Editor, Norton Journal of Bankruptcy Law and Practice, Thomson Reuters, 50 Broad Street East, Rochester, NY 14694, (800) 327-2665, ext. 2586, fax (585) 258-3774, clay.mattson@thomsonreuters.com.

For Customer Assistance Call 1-800-328-4880

Mat #41433600

We welcome the submission of material to be considered for publication, including articles, essays, decisions, or other items of interest to practicing attorneys, corporate counsel, and executives. The utmost care will be given to material submitted, although we cannot accept responsibility for unsolicited manuscripts. The manuscript should be sent electronically to each of the following editors:

Richard Lieb
St. John's University School of Law
LL.M. in Bankruptcy Office
8000 Utopia Parkway
Jamaica, NY 11439
(212) 479-6020
rlieb@cooley.com

Clay Mattson, Managing Editor
Norton Journal of Bankruptcy Law & Practice
Thomson Reuters
50 Broad Street East
Rochester, NY 14694
(800) 327-2665, ext. 2586
clay.mattson@thomsonreuters.com

The Enforceability of *Ipso Facto* Clauses in Financing Agreements: *American Airlines* and Beyond

By Emil A. Kleinhaus & Peter B. Zuckerman[*]

Introduction

Provisions that purport to modify or terminate the rights of contracting parties on account of a bankruptcy filing are ubiquitous in commercial financing agreements. These provisions — commonly referred to as "*ipso facto* clauses" — typically provide that a bankruptcy filing or other insolvency event of the borrower is an "event of default," permitting the lender to accelerate the loan and to receive interest at a default rate. To avoid running afoul of the Bankruptcy Code's automatic stay, many loan agreements further provide that the default and acceleration resulting from a bankruptcy filing will occur automatically, so that the consequences of default and acceleration, including the increased interest rate and in some cases the imposition of a "make-whole" obligation, are not dependent on any post-petition action by the lenders or their representative.

Subject to specified exceptions, section 365(e) of the Bankruptcy Code explicitly invalidates *ipso facto* clauses in executory contracts, which are traditionally defined as contracts "on which performance remains due to some extent on both sides."[1] Loan agreements, however, generally are not considered to be executory, on the basis that after extending financing, lenders usually do not have ongoing material obligations. For this reason and others, the enforceability of *ipso facto* clauses in loan agreements has been an area of controversy.

In a recent decision arising out of the bankruptcy of American Airlines, the U.S. Court of Appeals for the Second Circuit provided significant guidance on the question of whether *ipso facto* clauses are enforceable in loan agreements. In that case, over the objection of secured lenders, the court enforced provisions in indentures that called for the automatic acceleration of debt upon bankruptcy and that specified that no make-whole payments would be due from the debtor following such acceleration. In arguing for the invalidation of the indenture provisions, the secured lenders asserted that *ipso facto* clauses are generally unenforceable, even in cases where such clauses benefit the debtor. In rejecting this argument, the Second Circuit did

[*]The authors are a partner and an associate, respectively, at the law firm of Wachtell, Lipton, Rosen & Katz. The views expressed are the authors' and do not necessarily represent the views of the firm or its clients, which include issuers of commercial debt and banks and other financial firms that hold commercial debt.

not focus on the fact that the lenders were seeking the protection of a statutory provision, section 365(e), that was enacted to protect the debtor. Instead, the court distinguished more broadly between executory and non-executory contracts, concluding, based on the text of the statute, that "*ipso facto* clauses in a *non*executory contract are not unenforceable pursuant to 11 U.S.C § 365(e) or any other Bankruptcy Code provision."[2]

American Airlines, however, is in arguable tension with other decisions that have declined to enforce *ipso facto* clauses in commercial loan agreements. A notable example is *In re W.R. Grace & Co.*, in which the District Court in Delaware declined to enforce an *ipso facto* clause that would have provided a lender with default interest upon the borrower's bankruptcy filing. In doing so, the court concluded that the bar on *ipso facto* clauses extends beyond situations explicitly covered by the Bankruptcy Code.[3]

Amid this tension between the textual approach of *American Airlines* and the policy-based approach of cases such as *W.R. Grace*, this article revisits the question of whether *ipso facto* clauses in commercial loan agreements are enforceable in bankruptcy cases. As we explain, the Bankruptcy Code does not provide definitive guidance on the treatment of *ipso facto* clauses in commercial loan agreements. Section 365(e) does not apply easily to loan agreements, both because it is limited to "executory" contracts and also because it provides in section 365(e)(2)(B) that *ipso facto* clauses remain enforceable in any "contract to make a loan, or extend other debt financing or financial accommodations" to the debtor.[4] Other sections of the Bankruptcy Code, including sections 541(c)(1)(B) and 363(*l*), likewise reflect a policy against contractual provisions that prejudice the debtor as a result of a bankruptcy filing, but they too are not easily applied to standard provisions of loan agreements.

Absent a clear statutory basis to invalidate *ipso facto* clauses in loan agreements, it is difficult to defend a broad-based rule against enforcement of such clauses. Not only has Congress failed to impose a categorical bar on *ipso facto* clauses in loan agreements, but it has enacted other provisions that deal with the potential harms of such clauses. In the case of secured claims that arise based on *ipso facto* clauses — such as claims for default interest or make-whole payments — section 506(b) of the Bankruptcy Code already operates to prevent abusive or punitive claim enhancements. Likewise, in the case of unsecured claims, section 502(b)(2)'s disallowance of claims for "unmatured interest" will in many cases eliminate the effect of an *ipso facto* clause. Ultimately, although there may be some subset of cases in which enforcement of *ipso facto* clauses in loan agreements will undermine a debtor's ability to reorganize in some fundamental way, those cases are likely to be rare. In most cases, the enforcement or non-enforcement of *ipso facto* clauses in loan agreements will simply affect the allocation of value across creditor groups.

I. The Bankruptcy Code's Treatment of *Ipso Facto* Clauses

Three provisions of the Bankruptcy Code are most relevant in assessing *ipso facto* clauses: (a) section 365(e) renders unenforceable *ipso facto* clauses in executory contracts, subject to exceptions discussed below; (b) section 541(c)(1)(B) renders unenforceable *ipso facto* clauses that would cause forfeitures of property that would otherwise enter the bankruptcy estate; and (c) section 363(*l*) renders unenforceable *ipso facto* clauses that would hamper the trustee's ability to use, sell, or lease property of the estate. While these provisions differ in certain respects discussed below, they are all intended to protect the debtor from losing its rights and prerogatives as a result of a bankruptcy filing or change in financial condition.[5]

A. Section 365(e)

Prior to the enactment of the Bankruptcy Reform Act of 1978, *ipso facto* clauses in most contracts were not explicitly unenforceable, and *ipso facto* clauses in leases were explicitly enforceable.[6] Nonetheless, even in leases, courts at times refused to give effect to *ipso facto* clauses out of concern that "the debtor's estate would be deprived of the essential *res* to effect reorganization, and thus the purposes of the Act would be frustrated and the reorganization of the debtor thwarted."[7]

In 1978, Congress enacted section 365(e), which provides, in relevant part:

> Nothwithstanding a provision in an executory contract . . ., an executory contract may not be terminated or modified . . . at any time after the commencement of the case solely because of a provision in such contract that is conditioned on—(A) the insolvency of the debtor . . .; (B) the commencement of a [bankruptcy] case . . .; or (C) the appointment of or taking possession by a trustee in a [bankruptcy] case . . ..

In enacting this provision, legislators made clear that their purpose was to protect the debtor from losing valuable contract rights as a result of a bankruptcy filing. The House Report on the Bankruptcy Reform Act of 1978 states that *ipso facto* clauses "frequently hamper[ ] rehabilitation efforts" and that "[i]f the trustee may assume or assign [a] contract . . ., then the contract . . . may be utilized to assist in the debtor's rehabilitation or liquidation."[8]

By its terms, section 365(e)(1) applies only to contracts that are "executory." In addition, section 365(e)(2) excludes two categories of contracts from the rule of section 365(e)(1) even if they are executory: First, section 365(e)(2)(A) excludes contracts, such as personal service contracts and certain intellectual property licenses, as to which applicable law excuses a party from accepting performance from or rendering performance to an assignee.[9] Second, and more importantly here, section 365(e)(2)(B) preserves the enforceability of *ipso facto* clauses in any "contract to make a loan, or extend other debt financing or financial accommodations." Based on its plain language, section 365(e)(2)(B) appears to apply to all loan agreements, and the bankruptcy court in *American Airlines* suggested such a reading is plausible.[10] Nonetheless, relying on legislative history, various courts have held that "[t]he [financial accommodations] exception pertains only to executory commitments to extend *future* credit."[11] Under this view, financing agreements such as note indentures, which normally do not commit lenders to extend credit beyond the initial loan, do not fall within the statutory exception;[12] rather, the exception applies only to arrangements such as revolving credit facilities that have not been fully drawn as of the borrower's bankruptcy filing.[13]

In light of the uncertainty as to whether the "financial accommodations" exception to section 365(e)(1) applies to loan agreements that do not require further extensions of credit, a critical question in analyzing *ipso facto* clauses in loan agreements is whether the agreements are "executory." The term "executory" is not defined in the Bankruptcy Code. The legislative history states broadly that executory contracts "generally include[] contracts on which performance remains due to some extent on both sides."[14] Absent a precise definition in the statute, many courts have turned to a more expansive formulation proffered by Professor Vern Countryman, under which a contract is executory if "the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other."[15] Alongside or in lieu of the Countryman definition, other courts have relied on a so-called "functional approach" that determines "whether a contract is executory . . . by the benefits that assumption or rejection would produce for the estate."[16]

Professor Countryman's article itself states that mortgages are not executory contracts.[17] And based on the Countryman approach, courts generally have not treated funded loan agreements as executory contracts.[18] These decisions rely in part on the House Report accompanying the Bankruptcy Reform Act of 1978, which states that "[a] note is not usually an executory contract if the only performance that remains is repayment."[19] Although this language could be interpreted simply to mean that a loan agreement is not executory where repayment by the borrower is the only material performance due on either side, some decisions interpret it more broadly to mean that "a contract is not executory as to a party simply because the party is obligated to make payments of money," so that a financing contract is not executory even if the lender has material outstanding obligations.[20] Under either view, however, courts are likely to find that fully funded loan agreements are not executory because the lenders have no ongoing material obligations.[21] Consistent with this logic, in several recent cases, including *American Airlines*, parties have simply assumed that financing agreements are non-executory.[22]

Nonetheless, the case law is not entirely uniform on the issue of whether a funded loan agreement is executory. In *In re Texaco*, a case involving an indenture governing unsecured notes, the court held that "[i]n light of the fact that performance remains due on both sides, the Indenture may be classified as an executory contract."[23] The "continued performance" by the indenture trustee referenced by the court included:

> (a) Maintaining an office where the Notes may be presented for payment. (b) Maintaining a current list of names and addresses of security holders. (c) Ef-

> fecting transfers and exchanges of securities. (d) Replacing lost, mutilated or destroyed securities. (e) Delivery of securities to the Trustee for cancellation. (f) Redeeming securities. (g) Depositing the redemption price.[24]

Although *In re Texaco* has never been overruled, it has not been widely followed.[25] The decision is open to question given that the obligations at issue were owed to the noteholders, not to the debtor.[26] Because these obligations were owed to the noteholders, even if they were sufficiently material to make the contract executory, it is doubtful that their non-performance could have excused the debtor's performance in favor of the trustee.

B. Section 541(c)(1)(B)

Section 541(c)(1)(B) of the Bankruptcy Code provides that, with certain exceptions, "an interest of the debtor in property becomes property of the estate . . . notwithstanding any provision in an agreement . . . that is conditioned on the insolvency or financial condition of the debtor, [or] on the commencement of a case under this title . . . and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property."[27] Unlike section 365(e), this provision applies without regard to "executoriness"; indeed, some courts have held that it does not apply to executory contracts because it is superseded as to those contracts by section 365.[28]

By its terms, section 541(c)(1)(B) invalidates *ipso facto* clauses only to the extent that they cause a forfeiture, modification, or termination of an "interest in property" of the debtor that would otherwise enter the estate. Although Congress could have drafted a provision that would simply invalidate any contractual provision that negatively impacts a debtor as a result of a bankruptcy filing, the language of the statute is not that broad. Thus, in applying section 541(c)(1)(B) to *ipso facto* clauses in loan agreements, the key question is whether enforcement of such provisions against the debtor will have the effect of depriving the debtor of any of its "legal and equitable interests . . . in property as of the commencement of the case."[29]

There is no question that the enforcement of an *ipso facto* clause in a loan agreement can alter the size of a debtor's obligation to a lender. But it is less clear that the enforcement of a loan agreement by its terms — for example, by generating a claim for default interest — effects "a forfeiture, modification, or termination of the debtor's interest in property," as the statute requires. In one of the few cases to address the issue directly, *In re Saint Vincent's*, a bankruptcy court in the Southern District of New York concluded that section 541(c)(1)(B) did not prevent enforcement of a provision in secured loan documents that required payment of default interest upon the debtor's bankruptcy. The court explained that "the collateral," i.e., the property of the debtor securing the loan at issue, "unquestionably came into the bankruptcy estate," and that the question presented was simply "how much the Creditor may recover" out of the debtor's estate.[30] The court, accordingly, distinguished between impairment of a property interest, on the one hand, and the creation of a contractual claim, on the other.

A decision arising out of the Lehman Brothers bankruptcy, also in the Southern District of New York, adopted an apparently broader view of section 541(c)(1)(B).[31] *Lehman Brothers* involved a swap agreement, as opposed to a commercial loan.[32] Under the relevant transaction documents, the debtor — in that case, a subsidiary of the holding company called Lehman Brothers Special Financing (LBSF) — had rights in collateral securing its exposure that had priority over the rights of certain noteholders. However, the transaction documents also provided that, if an event of default occurred, including a bankruptcy, a reversal of priorities would take place such that the noteholders would have priority in the collateral.[33] The bankruptcy court held that both section 365(e)(1) and section 541(c)(1)(B) barred a contractual reversal of priorities as a result of a bankruptcy filing.[34] In reaching this conclusion, the court used broad language, stating that it is "axiomatic that *ipso facto* clauses are, as a general matter, unenforceable."[35] As noted, however, the court squarely held that the governing swap agreement was executory for purposes of section 365(e)(1), so the discussion of section 541(c)(1)(B) was of secondary importance. The court also expressly found that the debtor's priority in the collateral was a "valuable property interest," the modification of which would contravene section 541(c)(1)(B).[36] It is unclear whether *Lehman Brothers*' treatment of section 541(c)(1)(B) would extend to provisions in loan agreements that simply affect the size of a creditor's claim.

As discussed below, even cases that have declined to enforce *ipso facto* clauses in loan agreements generally have not relied on section 541(c)(1)(B), and have instead concluded that the bar on *ipso facto* clauses extends beyond the terms of the Bankruptcy Code. Nonetheless, since the statute is not entirely clear in its application to contractual provisions that affect the size of a lender's prepetition claim — and there is some basis to argue that such provisions do "modify" property interests insofar as they generate larger claims against the debtors' property — debtors can be expected to invoke section 541(c)(1)(B) in seeking to disallow claims for default interest or make-whole payments that result from a bankruptcy filing.

C. Section 363(*l*)

Using language that tracks section 541(c)(1)(B) of the Bankruptcy Code, section 363(*l*) of the Code provides that a trustee or debtor may "use, sell, or lease property" of the debtor "notwithstanding any provision in a contract . . . that is conditioned on the insolvency or financial condition of the debtor, [or] on the commencement of a case under this title, . . . and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property."[37] Unlike section 541(c)(1)(B), section 363(*l*) is expressly "subject to the terms of section 365"; as a result, it follows that section 363(*l*) is subject to the exception for "financial accommodations" clauses in section 365(e)(2)(B).

Like section 541(c)(1)(B), section 363(*l*) has not generally been treated by courts as a basis to invalidate *ipso facto* clauses in loan agreements. By its terms, the statute protects the debtor's ability to use its property; it does not speak to creditor recoveries or the claims allowance process. However, section 363(*l*) has been used to invalidate a "springing lien" clause in a note indenture pursuant to which a bankruptcy filing purported to provide the noteholder with a lien, i.e., a property interest, on additional property owned by the debtor.[38] According to the court, not only did this clause contravene the Bankruptcy Code's policy of providing debtors with a fresh start, but it violated section 363(*l*) by effecting a "bald modification" of the debtor's interest in property that was otherwise unencumbered.[39] This ruling was cited by another court that disallowed an *ipso facto* clause requiring the borrower to pay a 5% fee to a secured noteholder upon the borrower's bankruptcy filing.[40] The court found this clause to be "void as a matter of public policy" and violative of section 363(*l*) because, by increasing the secured creditor's claim, the clause effected "a modification of the debtor's interest in property."[41] This decision, however, has not been widely cited, and debtors in recent cases have not generally argued that section 363(*l*) applies to loan agreements.

II. *American Airlines* and Its Predecessors

American Airlines and earlier bankruptcy cases in New York, including *General Growth* and *Saint Vincent's*, present one approach to analyzing the enforceability of *ipso facto* clauses in loan agreements. Under the textual approach adopted in these cases, the courts consider whether the provisions of the Bankruptcy Code that relate to *ipso facto* clauses apply by their terms to the clauses at issue. Based on this straightforward approach, the courts have enforced *ipso facto* clauses where not expressly invalidated by the Code.

A. *American Airlines*

In *American Airlines*, the debtors aimed to "take advantage of the existing low interest rate environment" by refinancing $1.3 billion of notes secured by various aircraft with up to $1.5 billion of new notes at interest rates that would save the company "well in excess of $200 million."[42] The relevant indentures provided that: (i) American Airlines's filing of a voluntary bankruptcy was an event of default; (ii) the bankruptcy default automatically accelerated the notes; and (iii) upon such acceleration, the principal of the notes, the accrued but unpaid interest, and all other amounts owing — "*but for the avoidance of doubt, without Make-Whole Amount*" — were immediately due and payable.[43] Based on these provisions, including the explicit language providing that no make-whole amount was payable in the event of a bankruptcy acceleration, American Airlines argued that it was entitled to repay the notes without a make-whole.

U.S. Bank, as trustee under the three indentures, contended that the indenture provisions that excused the debtor from paying a make-whole were unenforceable as *ipso facto* clauses, even though they would benefit rather than prejudice the debtor. Since U.S. Bank presumed that the indentures at issue were not executory, in arguing that the *ipso facto* clauses were unenforceable, it pointed to statutory provisions beyond section 365(e), such as sections 541(c) and 363(*l*), as evidence of a general policy against *ipso facto* provisions. U.S. Bank also contended that American Airlines's reliance on *ipso facto* clauses was inconsistent with its election under section 1110(a) of the Bankruptcy Code, which enabled it to retain possession of aircraft collateral by curing defaults other than *ipso facto* defaults.[44]

In January 2013, the United States Bankruptcy Court for the Southern District of New York overruled U.S. Bank's objections.[45] The court held that, under the indentures, the bankruptcy filing triggered an automatic acceleration event and that, under the indentures, no make-whole was due in that scenario.[46] With regard to sections 363(*l*) and 541(c)(1)(B), the court explained that "[n]othing in the plain language of either section" invalidated the *ipso facto* clauses at issue.[47] If anything, the court observed, not enforcing the *ipso facto* clauses would undermine the purpose of section 541(c)(1)(B), which was enacted to protect the debtor, insofar as it would "harm the estate by depriving the Debtors of a valuable contractual right, namely the right to not pay a Make-Whole Amount."[48]

In September 2013, the Second Circuit affirmed the bankruptcy court's decision.[49] The court observed that "[the] case required [it] to address two questions of law important to the workings of the Bankruptcy Code," one of which was "whether indenture clauses declaring a debtor's default upon the filing of a voluntary bankruptcy petition and providing for automatic debt acceleration are unenforceable *ipso facto* provisions under § 365(e)(1) of the Bankruptcy Code . . . or other Code provisions cited by U.S. Bank."[50] The court concluded that the Code did not invalidate the clauses at issue, holding that "the pertinent clauses, contained in nonexecutory contracts, [were] not within the scope of . . . § 365(e)(1) and [were] not rendered unenforceable by any other Bankruptcy Code provision identified by U.S. Bank."[51]

Despite the significance that the court accorded to the issue, the appellate court's analysis of the enforceability of the indentures' *ipso facto* clauses was notably brief. First, the court found that sections 365(e)(1), 363(*l*), and 541(c)(1)(B) were all inapplicable. According to the court, section 365(e)(1) did not apply because the parties had agreed that the indentures were not executory; section 541(c)(1)(B) did not apply because the *ipso facto* clauses did not prevent any property from entering the estate; and section 363(*l*) did not apply because the clauses did not preclude the trustee from using, selling, or leasing estate property. Having concluded that none of those provisions were applicable, the court rejected U.S. Bank's contention that the Bankruptcy Code invalidates *ipso facto* clauses in a more general way. As the court explained, the specificity of the provisions in the Bankruptcy Code that do speak to *ipso facto* clauses "demonstrate[s] that Congress clearly knows how to limit or negate the effect of *ipso facto* clauses when it wants to" and thus, "counsels against" a broader invalidation of such clauses.[52] The court concluded that " '[t]he absence of textual support [was] fatal' to U.S. Bank's position that *ipso facto* provisions are broadly or categorically denied enforcement by the Code."[53] In sum, the Second Circuit grounded its decision in the text of statute rather than the fact that the provisions at issue were enacted for the benefit of debtors rather than creditors.

B. *General Growth* and *Saint Vincent's*

The *American Airlines* decision was unusual insofar as the *ipso facto* clauses at issue benefited the debtor. As a result, the provisions of the Bankruptcy Code that deal with preserving the debtor's property did not apply, and the policy underlying the Code's disfavor toward *ipso facto* clauses was not directly implicated.[54] Nonetheless, in adopting a text-based approach, the Second Circuit's decision was consistent with at least two decisions by bankruptcy courts in the Second Circuit that enforced *ipso facto* provisions against the debtor.

In *In re General Growth Properties, Inc.*, the Bankruptcy Court for the Southern District of New York enforced provisions in a loan agreement under which lenders were entitled to a 3% bump-up in their interest rate following the debtor's bankruptcy filing.[55] The court concluded first that: (i) the lenders were entitled to receive contractual default interest under section 506(b) of the Bankruptcy Code, which provides that an oversecured creditor is entitled to post-petition interest; and (ii) the debtor could not reinstate the loans at issue without paying such default interest. The court then rejected the argument that the contract provision requiring payment of default interest following a bankruptcy was an unenforceable *ipso facto* clause. The court held that *ipso facto* "clauses are not *per se* invalid in the Second Circuit except where contained in an executory contract or unexpired lease."[56] Although the court noted that an *ipso facto* clause might not be enforced if it impaired the debtor's ability to "file for bankruptcy" and "enjoy a fresh start," the court ultimately grounded its decision in the statute, emphasizing that "Congress singled out only executory contracts and unexpired leases for special treatment under [section] 365(e)(1) when it could have spoken in broader terms."[57]

In *In re Saint Vincent's Catholic Medical Centers of New York*, the Bankruptcy Court for the Southern District of New York likewise enforced an *ipso facto* clause requiring payment of charges and attorneys' fees to secured creditors following a bankruptcy default.[58] After concluding that the mortgage loans at issue were not "executory" under the Countryman definition, and that section 541(c)(1)(B) did not apply because the debtor's estate was not being deprived of pre-petition property, the court upheld the charges and fees.[59] *General Growth* and *Saint Vincent's* demonstrate that *American Airlines*, although unusual because it involved contractual provisions that improved the debtor's position following a bankruptcy filing, reflects a broader trend in favor of enforcing *ipso facto* clauses where they do not run afoul of particular provisions of the Bankruptcy Code.

III. *W.R. Grace* and Its Predecessors

In contrast to *American Airlines* and the cases that preceded it in the Bankruptcy Court for the Southern District of New York, other decisions have relied on a policy-based approach to conclude that *ipso facto* clauses are broadly unenforceable, even where no provision of the Bankruptcy Code squarely applies.

A. *W.R. Grace*

In *W.R. Grace*, the United States District Court for the District of Delaware refused to enforce an *ipso facto* clause that would have entitled unsecured creditors to default interest, which was 2% higher than the contractual non-default rate.[60] The court agreed with the lenders that the credit agreement was not executory and did not cause a forfeiture of estate property, and thus found that sections 365(e) and 541(c) were not applicable by their terms.[61] However, the court also "agree[d] with the general trend of the federal courts that the prohibition against *ipso facto* clauses is not limited to actions based upon §§ 541(c) and 365(e)."[62] In reaching its decision, the court invoked the "purpose" of bankruptcy — "to provide the debtor with a 'fresh start' " — and concluded that "enforcement of *ipso facto* clauses," including in loan agreements, "would punish debtors by negating this central purpose."[63]

The *W.R. Grace* court's discussion of default interest was arguably unnecessary because the court went on to find that the unsecured lenders were not entitled to any post-petition interest under section 502(b)(2) of the Bankruptcy Code, which disallows claims for post-petition interest, subject to certain exceptions, including section 506(b)'s protection of post-petition interest on secured debt.[64] Since the lenders in *W.R. Grace* were not secured, they were not eligible for post-petition interest under section 506(b). Moreover, since there was not enough evidence to conclude that the debtor was solvent, the lenders were not eligible for interest under section 1129(a)(7) of the Code, which requires that each creditor receive as much in a reorganization as it would in a liquidation. (In a liquidation, section 726(a)(5) of the Code requires that unsecured creditors receive interest at the "legal rate" before any payments may be made to equity.)

In a footnote, the *W.R. Grace* court distinguished the case from *General Growth* largely on the grounds that *General Growth* involved a secured creditor and debtors that were "unquestionably solvent."[65] Based on this distinction, the court in *W.R. Grace* may have enforced the *ipso facto* clause if the debtors were clearly solvent or if the lenders were secured. Nonetheless, in explaining its rationale for not enforcing the clause at issue, the court did not distinguish between secured and unsecured creditors or solvent and insolvent debtors.

B. *W.R. Grace's* Predecessors

W.R. Grace cited several cases in support of its holding that *ipso facto* clauses are unenforceable on non-statutory grounds. Those cases, however, involved notably different factual or legal circumstances from those at issue in *W.R. Grace*. The corporate bankruptcies cited by *W.R. Grace* all invalidated *ipso facto* clauses on statutory grounds, relying on section 365(e), 363(*l*), or 541(c).[66] The two cases that invalidated *ipso facto* clauses on non-statutory grounds were personal bankruptcies where *ipso facto* clauses threatened to deprive the debtors of their cars.[67] Moreover, one of those decisions expressly "decline[d] to draw any inferences regarding Congressional intent insofar as nonexecutory contracts are concerned."[68] The other personal bankruptcy case, *In re Rose*, relied on legislative history and principles of equity to conclude that invalidation of *ipso facto* clauses should not be limited to executory contracts.[69] According to the court, "[t]he legislative history [of section 365(e)] indicates that bankruptcy-default clauses are to be invalid in all types of contracts, without limitation."[70] The court further concluded that enforcing a clause that would in effect penalize debtors for a bankruptcy filing would be inequitable and "defeat the purpose of providing a 'fresh start.' "[71]

IV. Analysis of Case Law: *Ipso Facto* Clauses in Financing Agreements

The case law summarized above shows that there is still a meaningful divergence of opinion among courts regarding the proper treatment of *ipso facto* clauses in loan agreements. One strand of case law, including *W.R. Grace*, has looked beyond the text of the Bankruptcy Code to conclude that *ipso facto* clauses are at odds with bankruptcy policy and generally unenforceable. A second strand of case law, including *American Airlines*, *General Growth*, and *Saint Vincent's*, has adopted a more text-based approach and enforced *ipso facto* clauses in the absence of an express statutory prohibition, regardless of whether they benefit or prejudice the debtor.

Yet despite these differing approaches, courts have generally been careful to avoid per se rules. As noted above, the *W.R. Grace* court, in denying a claim for default interest predicated on a bankruptcy default provision, went out of its way to distinguish *General Growth* on the basis that it involved a solvent debtor and secured loans. Likewise, the bankruptcy court in *American Airlines*, although endorsing the textual approach of *General Growth* as opposed to the policy rationale of *W.R. Grace*, stated in a footnote that *W.R. Grace* was "factually distinguishable."[72] The bankruptcy court in *American Airlines* also explained in a footnote that enforcement of the *ipso facto* clause in the circumstances presented, rather than impeding the debtor's "fresh start," would "do just the opposite by saving the estate and its creditors several hundred million dollars."[73]

Although *W.R. Grace* leaves open the possibility that *ipso facto* clauses might be enforced in extraordinary circumstances, the court's conclusion that "the ban on *ipso facto* clauses" is "much broader" than "the confines of §§ 541(c) and 365(e)(1)" is not well supported.[74] On the simplest level, as noted by the Second Circuit in *American Airlines*, the provisions of the Bankruptcy Code that invalidate *ipso facto* clauses in specific situations "demonstrate that Congress clearly knows how to limit or negate the effect of *ipso facto* clauses when it wants to."[75] An extra-statutory prohibition on *ipso facto* clauses has the effect of interfering with private contractual relations in a broader category of cases than Congress appears to have intended.

Beyond the lack of statutory support for interfering with *ipso facto* clauses in loan agreements, it is questionable whether such interference is necessary in light of other protections in the Bankruptcy Code. As discussed above, *W.R. Grace* itself involved a situation where the default interest at issue was subject to disallowance under section 502(b)(2) of the Bankruptcy Code because the loans were unsecured and the debtor was not demonstrably solvent.

The Bankruptcy Code also places limits on *ipso facto* clauses in secured loan agreements. In cases where bankruptcy defaults lead to the incurrence of default interest, section 506(b) provides that creditors, to the extent that they are oversecured, are entitled to "interest" on their claims as well as "any reasonable fees, costs or charges provided for under the agreement."[76] In the Second Circuit, the application of section 506(b) to award secured creditors interest at the contractual default rate, as opposed to a lesser non-default rate, has generally been subject to "equitable considerations," including the debtor's solvency.[77] When the debtor is solvent, "there is much more leeway to grant the default rate because other creditors will not be injured."[78]

Like default interest, make-whole obligations resulting from bankruptcy defaults also invite scrutiny. Under section 502(b)(1) of the Bankruptcy Code, for a prepayment provision to yield a valid bankruptcy claim, it must be enforceable under applicable non-bankruptcy law.[79] Under New York state law, prepayment clauses are typically construed as liquidated damages provisions and, accordingly, are enforceable only "where (1) actual damages may be difficult to determine and (2) the sum stipulated is not 'plainly disproportionate' to the possible loss."[80] Additionally, as in the case of default interest, secured claims arising from prepayment clauses must pass muster under 506(b) of the Bankruptcy Code, which requires that fees or charges arising under credit documents be "reasonable."[81] Although even substantial make-whole provisions have been deemed reasonable under section 506(b),[82] sections 502(b)(1) and 506(b) ensure that such provisions are, at the very least, thoroughly reviewed by courts prior to being enforced against the debtor.

Conclusion

Despite the Second Circuit's recent decision in *American Airlines*, the law on the enforceability of *ipso facto* clauses in loan agreements is to some degree unsettled and fact-dependent. In the Second Circuit, there is reason to believe that *ipso facto* clauses in commercial financing agreements will generally be enforced, although, even there, provisions that disadvantage the debtor have drawn scrutiny. Beyond the Second Circuit, decisions such as *W.R. Grace* present a greater obstacle to enforcement of *ipso facto* clauses in loan agreements. As discussed above, there is no compelling justification to invalidate *ipso facto* clauses that, while affecting creditor recoveries, are not punitive and do not jeopardize a debtor's prospects for reorganization. Whether persuasive or not, however, the reasoning of *W.R. Grace* and similar cases presents a risk to parties seeking enforcement of *ipso facto* clauses adverse to the debtor. Given the ubiquity of *ipso facto* clauses in commercial loan agreements, it is certain that neither *American Airlines* nor *W.R. Grace* will be the last word on these issues.

NOTES:

[1]N.L.R.B. v. Bildisco and Bildisco, 465 U.S. 513, 523 n.6, 104 S. Ct. 1188, 79 L. Ed. 2d

482, 11 Bankr. Ct. Dec. (CRR) 564, 9 Collier Bankr. Cas. 2d (MB) 1219, 5 Employee Benefits Cas. (BNA) 1015, 115 L.R.R.M. (BNA) 2805, Bankr. L. Rep. (CCH) P 69580, 100 Lab. Cas. (CCH) P 10771 (1984) (quoting H.R. Rep No. 95-595, at 347 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6303).

[2]In re AMR Corp., 730 F.3d 88, 112, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014) (emphasis added).

[3]In re W.R. Grace & Co., 475 B.R. 34, 153–54 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[4]11 U.S.C. § 365(e)(2)(B).

[5]See H.R. Rep. No. 95-595, at 348, reprinted in 1978 U.S.C.C.A.N. 5963, 6304 (By invalidating *ipso facto* clauses, section 365(e) may enable an otherwise terminable "contract or lease [to] be utilized to assist in the debtor's rehabilitation or liquidation."); H.R. Rep. No. 95-595, at 348, reprinted in 1978 U.S.C.C.A.N. 5963, 6325 ("[Section 541(c)] invalidates restrictions on the transfer of property of the debtor, in order that all of the interests of the debtor in property will become property of the estate."); H.R. Rep. No. 95-595, at 346, reprinted in 1978 U.S.C.C.A.N. 5963, 6302 ("[Section 363(*l*)] permits the trustee to use, sell, or lease property notwithstanding certain . . . *ipso facto* clauses that terminate the debtor's interest in the property or that work a forfeiture or modification of that interest.").

[6]See Act of June 22, 1938, ch. 575, § 70(b), 52 Stat. 840, 881 (providing that "an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto or of either party shall terminate the lease or give the other party an election to terminate the same is enforceable"), repealed by Bankruptcy Reform Act of 1978; see also Finn v. Meighan, 325 U.S. 300, 302–03, 65 S. Ct. 1147, 89 L. Ed. 1624 (1945); Matter of Railway Reorganization Estate, Inc., 133 B.R. 578, 583, 22 Bankr. Ct. Dec. (CRR) 376, 25 Collier Bankr. Cas. 2d (MB) 1383 (Bankr. D. Del. 1991).

[7]Matter of Triangle Laboratories, Inc., 663 F.2d 463, 469, 8 Bankr. Ct. Dec. (CRR) 317, 5 Collier Bankr. Cas. 2d (MB) 517, Bankr. L. Rep. (CCH) P 68391 (3d Cir. 1981); see also, e.g., Smith v. Hoboken R.R. Warehouse & S.S. Connecting Co., 328 U.S. 123, 131–33, 66 S. Ct. 947, 90 L. Ed. 1123, 168 A.L.R. 497 (1946); Queens Boulevard Wine & Liquor Corp. v. Blum, 503 F.2d 202, 206–07 (2d Cir. 1974).

[8]H.R. Rep. No. 95-595, at 348, reprinted in 1978 U.S.C.C.A.N. 5963, 6304.

[9]See In re Footstar, Inc., 337 B.R. 785, 788 (Bankr. S.D. N.Y. 2005) (noting that "courts addressing Section 365(e)(2) have opined that . . . [it] addresses the same executory contracts that fall within the scope of Section 365(c)(1)" of the Bankruptcy Code, which precludes assumption of certain contracts).

[10]See Transcript of Omnibus Hearing at 83, In re AMR Corp., No. 11-15463 (Bankr. S.D.N.Y. Nov. 29, 2012) (Docket No. 5581).

[11]In re Peninsula Intern. Corp., 19 B.R. 762, 764 (Bankr. S.D. Fla. 1982) (emphasis added); see also In re Texaco Inc., 73 B.R. 960, 965, 16 Collier Bankr. Cas. 2d (MB) 1398, Bankr. L. Rep. (CCH) P 71812 (Bankr. S.D. N.Y. 1987) (citing H.R. Rep. No. 95-595, at 348, reprinted in 1978 U.S.C.C.A.N. 5963, 6304 (explaining that the purpose of section 365(c)(2), which, like section 365(e)(2)(B), excepts financial accommodations contracts (in that instance, from the trustee's assumption and assignment powers), "at least in part, is to prevent the trustee from requiring new advances of money or other property")).

[12]See In re Texaco Inc., 73 B.R. 960, 965, 16 Collier Bankr. Cas. 2d (MB) 1398, Bankr. L. Rep. (CCH) P 71812 (Bankr. S.D. N.Y. 1987) (holding that an indenture governing notes that had already been issued was not a financial accommodations contract because it was not a

commitment to extend future credit to the debtor); accord In re Schwegmann Giant Super Markets, 287 B.R. 649, 657–58 (E.D. La. 2002).

[13]See Foothill Capital Corp. v. Official Unsecured Creditors' Committee of Midcom Communications, Inc., 246 B.R. 296, 300–01, Bankr. L. Rep. (CCH) P 78161 (E.D. Mich. 2000) (finding that a revolving credit facility fell under the financial accommodations exception because the lender might have been obligated to make further loans); Mims v. Fidelity Funding, Inc., 307 B.R. 849, 858 (N.D. Tex. 2002) (finding section 365(e)(2)(B) applicable to a revolving credit facility).

[14]H.R. Rep. No. 95-595, at 347, reprinted in 1978 U.S.C.C.A.N. 5963, 6303.

[15]Vern Countryman, Executory Contracts in Bankruptcy: Part I, 57 Minn L. Rev. 439, 460 (1973). On the broad acceptance of Professor Countryman's formulation, see, for example, In re General Growth Properties, Inc., 451 B.R. 323, 330 n.11, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011), which noted that the definition "has been widely accepted in [the Second Circuit] and other Circuits."

[16]In re General Development Corp., 177 B.R. 1000, 1012 (S.D. Fla. 1995), opinion aff'd, 84 F.3d 1364 (11th Cir. 1996) (applying the functional approach and noting the Eleventh Circuit's preference for it); see also In re Cardinal Industries, Inc., 146 B.R. 720, 727–29 (Bankr. S.D. Ohio 1992) (applying the functional approach alongside the Countryman approach and indicating the Sixth Circuit's use of both).

[17]Countryman, supra note 15, at 472 ("[T]he mortgage should not be viewed as an executory contract . . ..").

[18]See, e.g., In re General Growth Properties, Inc., 451 B.R. 323, 329, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011) (noting that "loan agreements are generally not considered to be executory contracts"); accord In re Kane, 248 B.R. 216, 223, 36 Bankr. Ct. Dec. (CRR) 19 (B.A.P. 1st Cir. 2000), aff'd, 254 F.3d 325, 46 Collier Bankr. Cas. 2d (MB) (1st Cir. 2001); In re Moody Nat. SHS Houston H, LLC, 426 B.R. 667, 673, 52 Bankr. Ct. Dec. (CRR) 262 (Bankr. S.D. Tex. 2010); In re Wait, 2008 WL 5427634 (Bankr. N.D. Iowa 2008). Under the less common functional approach, the analysis is more case specific insofar as it depends on the benefits to the estate and its creditors of a finding of executoriness. For example, one court found a partially unfunded loan agreement to be executory under the functional approach on the grounds that such a finding would permit rejection, which would both facilitate the rehabilitation of the debtor and clarify the rights of certain creditors by giving them a claim for breach. But in reaching this conclusion, the court also noted that if assumption had been permitted (and it was not because the court found the agreement to be a financial accommodations contract), the analysis may have been more difficult. See In re Cardinal Industries, Inc., 146 B.R. 720, 730 & nn. 10–11 (Bankr. S.D. Ohio 1992).

[19]H.R. Rep. No. 95-595, at 347, reprinted in 1978 U.S.C.C.A.N. 5963, 6303 to 04.

[20]Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1046, 12 Bankr. Ct. Dec. (CRR) 1281, 12 Collier Bankr. Cas. 2d (MB) 310, 226 U.S.P.Q. 961, Bankr. L. Rep. (CCH) P 70311 (4th Cir. 1985); In re Digicon, Inc., 71 Fed. Appx. 442 (5th Cir. 2003); In re Chateaugay Corp., 102 B.R. 335, 347, 19 Bankr. Ct. Dec. (CRR) 1102, 21 Collier Bankr. Cas. 2d (MB) 135 (Bankr. S.D. N.Y. 1989).

[21]See, e.g., In re Calpine Corp., 50 Bankr. Ct. Dec. (CRR) 92, 2008 WL 3154763 (Bankr. S.D. N.Y. 2008); see also In re Saint Vincent's Catholic Medical Centers of New York, 440 B.R. 587, 601, 53 Bankr. Ct. Dec. (CRR) 257 (Bankr. S.D. N.Y. 2010).

[22]See In re AMR Corp., 730 F.3d 88, 106, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014) (lenders assumed indentures to be non-executory); In re General Growth Properties, Inc., 451 B.R. 323, 329, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011) (debtor assumed note to be non-executory).

[23]In re Texaco Inc., 73 B.R. 960, 964, 16 Collier Bankr. Cas. 2d (MB) 1398, Bankr. L.

Rep. (CCH) P 71812 (Bankr. S.D. N.Y. 1987).

[24]In re Texaco Inc., 73 B.R. 960, 964, 16 Collier Bankr. Cas. 2d (MB) 1398, Bankr. L. Rep. (CCH) P 71812 (Bankr. S.D. N.Y. 1987).

[25]See, e.g., In re Premier Entertainment Biloxi LLC, 445 B.R. 582, 617–18 (Bankr. S.D. Miss. 2010) (noting that the parties to the indenture, which was substantially similar to that in *In re Texaco*, had not even considered that the indenture could be executory and after briefing the issue, concluded it was not); In re Saint Vincent's Catholic Medical Centers of New York, 440 B.R. 587, 601, 53 Bankr. Ct. Dec. (CRR) 257 (Bankr. S.D. N.Y. 2010) (distinguishing *In re Texaco*).

[26]See In re Texaco Inc., 73 B.R. 960, 964, 16 Collier Bankr. Cas. 2d (MB) 1398, Bankr. L. Rep. (CCH) P 71812 (Bankr. S.D. N.Y. 1987).

[27]11 U.S.C. §§ 541(c)(1), (B).

[28]E.g., In re First Protection, Inc., 440 B.R. 821, 830, 54 Bankr. Ct. Dec. (CRR) 47, 64 Collier Bankr. Cas. 2d (MB) 821 (B.A.P. 9th Cir. 2010); In re Warner, 480 B.R. 641, 648–49 (Bankr. N.D. W. Va. 2012); In re Ehmann, 319 B.R. 200, 202 (Bankr. D. Ariz. 2005); but cf. In re Lehman Bros. Holdings Inc., 422 B.R. 407, 422, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010) (applying both section 365(e)(1) and section 541(c)(1)(B) to invalidate *ipso facto* clauses in contracts held to be executory).

[29]11 U.S.C. § 541(a)(1) (providing that such interests are "property of the estate").

[30]See In re Saint Vincent's Catholic Medical Centers of New York, 440 B.R. 587, 602, 53 Bankr. Ct. Dec. (CRR) 257 (Bankr. S.D. N.Y. 2010).

[31]In re Lehman Bros. Holdings Inc., 422 B.R. 407, 415–16, 422, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010).

[32]Pursuant to a safe harbor in section 560, the Bankruptcy Code does give effect to certain *ipso facto* clauses in swap agreements that purport to enable specified parties to liquidate, terminate, or accelerate swap agreements upon a counterparty's bankruptcy filing. In the *Lehman Brothers* ruling described herein, however, the bankruptcy court held that this safe harbor did not apply because the provisions at issue were not part of the swap agreements themselves and did not deal with liquidation, termination, or acceleration. See In re Lehman Bros. Holdings Inc., 422 B.R. 407, 421, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010). But in a subsequent ruling arising out of a different swap dispute in the Lehman Brothers bankruptcy, the bankruptcy court held that the safe harbor did apply to *ipso facto* clauses mandating a special liquidation procedure in the event of bankruptcy (which proved unfavorable to the debtor). See Memorandum Decision at 6, Michigan State Hous. Dev. Auth. v. Lehman Bros. Derivatives Prods. Inc. (In re Lehman Bros. Holdings Inc.), No. 09-01728 (Bankr. S.D.N.Y. Dec. 19, 2013) (No. 61). Distinguishing the case from the decision discussed herein, the court found that "[t]here is a significant difference between the reordering of priorities within a hierarchy of distributions (an *ipso facto* contractual term that is not mentioned in Section 560) and selecting which method to use when disposing and valuing collateral in connection with liquidating a terminated swap agreement." Memorandum Decision at 6, Michigan State Hous. Dev. Auth. v. Lehman Bros. Derivatives Prods. Inc. (In re Lehman Bros. Holdings Inc.), No. 09-01728 (Bankr. S.D.N.Y. Dec. 19, 2013) (No. 61) Specifically, unlike provisions purporting to reorder priorities, the court held that "[t]he choice of an accepted and contractually specified method to liquidate, even if it produces a less desirable result from the point of view of the debtor, is consistent with full implementation of the exemption that is codified in Section 560." Memorandum Decision at 6, Michigan State Hous. Dev. Auth. v. Lehman Bros. Derivatives Prods. Inc. (In re Lehman Bros. Holdings Inc.), No. 09-01728 (Bankr. S.D.N.Y. Dec. 19, 2013) (No. 61)

[33]In re Lehman Bros. Holdings Inc., 422 B.R. 407, 413, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010).

[34]The noteholders had argued that these provisions of the Bankruptcy Code did not ap-

ply because, among other reasons, the reversal of priorities had occurred upon the bankruptcy filing of LBSF's parent company, not LBSF. In re Lehman Bros. Holdings Inc., 422 B.R. 407, 418, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010). The court, however, rejected this argument, finding that the reversal had not in fact occurred upon the filing of LBSF's parent and, even if it had, that it would have been barred because the *ipso facto* prohibition in sections 365(e)(1) and 541(c)(1)(B) was "not limited to the commencement of a case *by or against the debtor*." In re Lehman Bros. Holdings Inc., 422 B.R. 407, 418–19, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010). While the court thus concluded that *ipso facto* clauses based on the filing of a party other than the debtor could be invalidated at least in certain circumstances, it "decline[d] . . . to make any broad pronouncements . . . or to expand on the various relationships between or among debtor entities that would make it appropriate for one debtor to invoke *ipso facto* protection due to the filing of another affiliated member of a corporate family." In re Lehman Bros. Holdings Inc., 422 B.R. 407, 419, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010).

[35]In re Lehman Bros. Holdings Inc., 422 B.R. 407, 415, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010).

[36]In re Lehman Bros. Holdings Inc., 422 B.R. 407, 421, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010).

[37]11 U.S.C. § 363(l).

[38]See Matter of Railway Reorganization Estate, Inc., 133 B.R. 578, 580, 22 Bankr. Ct. Dec. (CRR) 376, 25 Collier Bankr. Cas. 2d (MB) 1383 (Bankr. D. Del. 1991).

[39]See Matter of Railway Reorganization Estate, Inc., 133 B.R. 578, 582–83, 22 Bankr. Ct. Dec. (CRR) 376, 25 Collier Bankr. Cas. 2d (MB) 1383 (Bankr. D. Del. 1991).

[40]See In re Chedick, 1996 WL 762329 (Bankr. D. D.C. 1996).

[41]In re Chedick, 1996 WL 762329 (Bankr. D. D.C. 1996).

[42]See In re AMR Corp., No. 11-15463 (Bankr. S.D.N.Y. Oct. 9, 2012) (No. 4959).

[43]In re AMR Corp., 485 B.R. 279, 289–90, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014) (emphasis added).

[44]Section 1110(a) enables creditors with a secured interest in aircraft to repossess such collateral notwithstanding the automatic stay. The debtor can avoid repossession if within 60 days of its filing, it agrees to perform all of its obligations under its agreement with the secured creditor and within specified periods, cures all defaults under this agreement "other than a default of a kind specified in section 365(b)(2)." 11 U.S.C. §§ 1110(a)(1), (a)(2); see also In re AMR Corp., 730 F.3d 88, 107, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[45]See In re AMR Corp., 485 B.R. 279, 284, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[46]See In re AMR Corp., 485 B.R. 279, 289–90, 293–98, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[47]In re AMR Corp., 485 B.R. 279, 297, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[48]In re AMR Corp., 485 B.R. 279, 297, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[49]In re AMR Corp., 485 B.R. 279, 297, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y.

2013), aff'd, 730 F.3d 88, 92, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[50]In re AMR Corp., 730 F.3d 88, 91–92, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014). (footnote omitted).

[51]In re AMR Corp., 730 F.3d 88, 92, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[52]In re AMR Corp., 730 F.3d 88, 107, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[53]In re AMR Corp., 730 F.3d 88, 107, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014) (quoting Travelers Cas. and Sur. Co. of America v. Pacific Gas and Elec. Co., 549 U.S. 443, 452, 127 S. Ct. 1199, 167 L. Ed. 2d 178, 47 Bankr. Ct. Dec. (CRR) 265, 57 Collier Bankr. Cas. 2d (MB) 314, Bankr. L. Rep. (CCH) P 80880 (2007)).

[54]Debtors have used bankruptcy acceleration clauses to their advantage in other recent bankruptcies as well. In *In re Calpine Corp.*, the debtors sought to refinance approximately $2.5 billion of secured debt at lower interest rates. Based on provisions in the loan documents under which the loans at issue were automatically accelerated upon bankruptcy, without providing for any prepayment fee, the Bankruptcy Court held that "the secured part[ies] [were] prohibited from incorporating [prepayment fees] into [their] allowed secured claim." In re Calpine Corp., 365 B.R. 392, 398–99 (Bankr. S.D. N.Y. 2007). Although the court went on to conclude that the secured creditors were entitled to an unsecured claim for damages, In re Calpine Corp., 365 B.R. 392, 399 (Bankr. S.D. N.Y. 2007), this aspect of the decision was overturned by the district court, which held that, absent a clause providing for the payment of particular amounts upon an acceleration event, no damages were recoverable. HSBC Bank USA, Nat. Ass'n v. Calpine Corp., 2010 WL 3835200 (S.D. N.Y. 2010). Similarly, in *In re Solutia Inc.*, the Bankruptcy Court gave effect to an automatic acceleration clause in holding that the debtors could repay debt in bankruptcy without any prepayment fee. See In re Solutia Inc., 379 B.R. 473, 484–85, 49 Bankr. Ct. Dec. (CRR) 38 (Bankr. S.D. N.Y. 2007).

[55]In re General Growth Properties, Inc., 451 B.R. 323, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011).

[56]In re General Growth Properties, Inc., 451 B.R. 323, 330, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011).

[57]In re General Growth Properties, Inc., 451 B.R. 323, 330–31, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011).

[58]See In re Saint Vincent's Catholic Medical Centers of New York, 440 B.R. 587, 600–02, 53 Bankr. Ct. Dec. (CRR) 257 (Bankr. S.D. N.Y. 2010) (citing In re Frank's Nursery & Crafts, Inc., 2006 WL 2385418 (Bankr. S.D. N.Y. 2006).

[59]See In re Saint Vincent's Catholic Medical Centers of New York, 440 B.R. 587, 601–02, 53 Bankr. Ct. Dec. (CRR) 257 (Bankr. S.D. N.Y. 2010).

[60]See In re W.R. Grace & Co., 475 B.R. 34, 70 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917)(Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[61]See In re W.R. Grace & Co., 475 B.R. 34, 153 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013). In contrast, without considering whether the credit agreement

was executory, the bankruptcy court had invalidated the *ipso facto* clause on account of section 365(e). See In re W.R. Grace & Co., 51 Bankr. Ct. Dec. (CRR) 184, 2009 WL 1469831 (Bankr. D. Del. 2009), aff'd, 468 B.R. 81 (D. Del. 2012), opinion amended and superseded, 475 B.R. 34 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917)(Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013) and withdrawn from bound volume and aff'd, 475 B.R. 34 (D. Del. 2012).

[62]In re W.R. Grace & Co., 475 B.R. 34, 154 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[63]In re W.R. Grace & Co., 475 B.R. 34, 152 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[64]See In re W.R. Grace & Co., 475 B.R. 34, 159 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917)(Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[65]In re W.R. Grace & Co., 475 B.R. 34, 160–61 & n.134 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[66]For cited cases relying on section 365(e), see In re Chateaugay Corp., Bankr. L. Rep. (CCH) P 75302, 1993 WL 159969 (S.D. N.Y. 1993); In re Lehman Bros. Holdings Inc., 422 B.R. 407, 420, 52 Bankr. Ct. Dec. (CRR) 191, 63 Collier Bankr. Cas. 2d (MB) 586 (Bankr. S.D. N.Y. 2010). For cases relying on section 363(*l*) or 541(c), see In re EBC I, Inc., 356 B.R. 631, 640, 47 Bankr. Ct. Dec. (CRR) 131 (Bankr. D. Del. 2006) and Matter of Railway Reorganization Estate, Inc., 133 B.R. 578, 583, 22 Bankr. Ct. Dec. (CRR) 376, 25 Collier Bankr. Cas. 2d (MB) 1383 (Bankr. D. Del. 1991).

[67]See In re Perry, 29 B.R. 787, 790–91, 9 Collier Bankr. Cas. 2d (MB) 931 (D. Md. 1983), judgment aff'd, 729 F.2d 982, 11 Bankr. Ct. Dec. (CRR) 961, 10 Collier Bankr. Cas. 2d (MB) 701, Bankr. L. Rep. (CCH) P 69769 (4th Cir. 1984); Matter of Rose, 21 B.R. 272, 276–77, 6 Collier Bankr. Cas. 2d (MB) 1104 (Bankr. D. N.J. 1982).

[68]In re Perry, 29 B.R. 787, 791, 9 Collier Bankr. Cas. 2d (MB) 931 (D. Md. 1983), judgment aff'd, 729 F.2d 982, 11 Bankr. Ct. Dec. (CRR) 961, 10 Collier Bankr. Cas. 2d (MB) 701, Bankr. L. Rep. (CCH) P 69769 (4th Cir. 1984).

[69]See Matter of Rose, 21 B.R. 272, 276, 6 Collier Bankr. Cas. 2d (MB) 1104 (Bankr. D. N.J. 1982).

[70]Matter of Rose, 21 B.R. 272, 276, 6 Collier Bankr. Cas. 2d (MB) 1104 (Bankr. D. N.J. 1982) (citing H.R. Rep. No. 95-595, at 348 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6304).

[71]Matter of Rose, 21 B.R. 272, 277, 6 Collier Bankr. Cas. 2d (MB) 1104 (Bankr. D. N.J. 1982).

[72]In re AMR Corp., 485 B.R. 279, 296–97, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[73]In re AMR Corp., 485 B.R. 279, 297 n.14, 57 Bankr. Ct. Dec. (CRR) 146 (Bankr. S.D. N.Y. 2013), aff'd, 730 F.3d 88, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[74]In re W.R. Grace & Co., 475 B.R. 34 (D. Del. 2012), stay pending appeal denied, (3rd Circ. 12-2966) (June 27, 2012) and appeal dismissed, (3rd Circ. 12-2966) (Sept. 24, 2012) and appeal dismissed, (3rd Circ. 12-2917) (Oct. 4, 2012) and appeal dismissed, (3rd Circ. 12-2967) (Oct. 9, 2012) and aff'd, 532 Fed. Appx. 264 (3d Cir. 2013) and aff'd, 729 F.3d 311, 58 Bankr. Ct. Dec. (CRR) 113 (3d Cir. 2013) and aff'd, 729 F.3d 332, 58 Bankr. Ct. Dec. (CRR) 112 (3d Cir. 2013).

[75]In re AMR Corp., 730 F.3d 88, 107, 58 Bankr. Ct. Dec. (CRR) 122 (2d Cir. 2013), petition for cert. filed (U.S. Feb. 12, 2014).

[76]11 U.S.C. § 506(b).

[77]See, e.g., In re General Growth Properties, Inc., 451 B.R. 323, 328–29, 55 Bankr. Ct. Dec. (CRR) 6, 65 Collier Bankr. Cas. 2d (MB) 1351 (Bankr. S.D. N.Y. 2011); In re Vest Associates, 217 B.R. 696, 702–03 (Bankr. S.D. N.Y. 1998).

[78]In re Vest Associates, 217 B.R. 696, 703 (Bankr. S.D. N.Y. 1998); see also In re Dow Corning Corp., 456 F.3d 668, 679, 46 Bankr. Ct. Dec. (CRR) 222, Bankr. L. Rep. (CCH) P 80664, 2006 FED App. 0260P (6th Cir. 2006) (observing that "in solvent debtor cases, rather than considering equitable principles, courts have generally confined themselves to determining and enforcing whatever pre-petition rights a given creditor has against the debtor").

[79]11 U.S.C. § 502(b)(1).

[80]In re South Side House, LLC, 451 B.R. 248, 270, 55 Bankr. Ct. Dec. (CRR) 26 (Bankr. E.D. N.Y. 2011), order aff'd, Bankr. L. Rep. (CCH) P 82170, 2012 WL 273119 (E.D. N.Y. 2012) (quoting In re United Merchants and Mfrs., Inc., 674 F.2d 134, 142, 6 Collier Bankr. Cas. 2d (MB) 321, Bankr. L. Rep. (CCH) P 69005 (2d Cir. 1982)).

[81]See generally Scott K. Charles & Emil A. Kleinhaus, Prepayment Clauses in Bankruptcy, 15 Am. Bankr. Inst. L. Rev. 537, 556–63 (Winter 2007).

[82]See, e.g., Memorandum Opinion at 2–3, 9–10, In re School Specialty, Inc., No. 13-10125 (Bankr. D. Del. Apr. 22, 2013) (No. 854) (approving a loan make-whole premium that was more than 35% of the loan's outstanding principal).