

ALERT

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Supreme Court Breaks Divide: Mere Retention Of Debtor Property Is Not A Stay Violation

By: Allison Arotzky

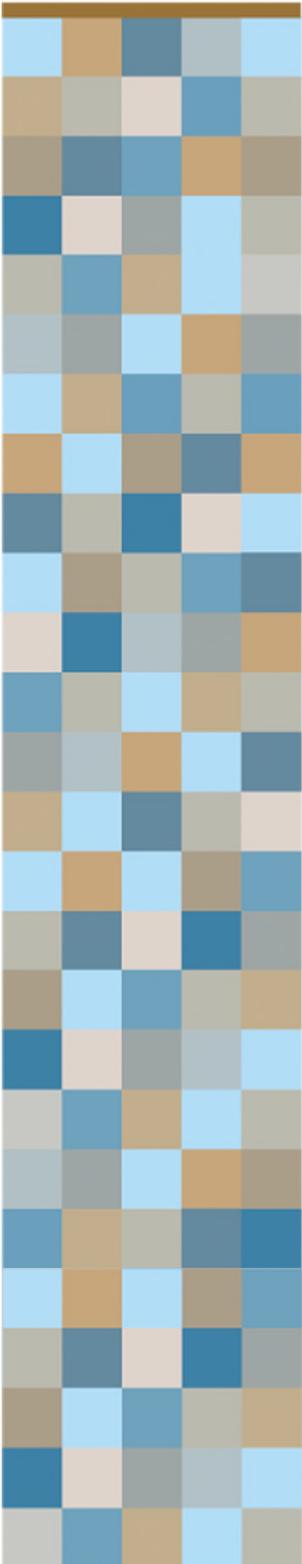
The United States Supreme Court has resolved a split among lower courts on the issue of whether a lessor who repossesses debtor collateral on eve of bankruptcy violates the automatic stay by failing to surrender such property immediately following the bankruptcy filing.

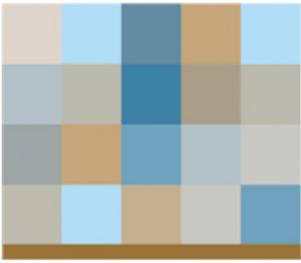
In *City of Chicago, IL v. Fulton*, 141 S.Ct. 585 (2021), the Court ruled unanimously that retaining possession of a debtor's property after a bankruptcy filing is not an act to exercise control over the bankruptcy estate prohibited by the automatic stay. In the matter before the Court, individuals who had filed Chapter 13 bankruptcy petitions requested that the City return their vehicles, which had been impounded prior to the bankruptcy cases for failure to pay motor vehicle fines. The Court reversed the lower courts' rulings, which had found that the City's refusal to return the vehicles violated the automatic stay.¹

The filing of a bankruptcy petition "creates an estate" comprised of all legal or equitable interests of the debtor in property as of the commencement of the case. 11 U.S.C. §541(a)(1). With limited exceptions, property of the estate must be turned over to the trustee. The filing of a bankruptcy petition also imposes an automatic stay of efforts to collect from the debtor outside of the bankruptcy forum, including among other things "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate." 11 U.S.C. §362(a)(3). The Court observed that merely retaining property does not necessarily qualify as an "act" or an "exercise." In addition, the Court pointed to section 542(a) of the Bankruptcy Code, which requires that property of the estate must be turned over to the trustee. Reading section 362(a)(3) to prohibit retention of estate property would render the separate turnover provision superfluous.

Accordingly, a lessor's retention of property that it repossessed prior to the bankruptcy will not violate the automatic stay on the basis that the lessor is acting "to exercise control over property of the estate." Nevertheless, the Court cautioned that it was not addressing the operation of the turnover requirement or the meaning of other actions proscribed by section 362(a). For example the automatic stay also bars "any act to create, perfect, or enforce any lien against property of the estate" and "any act to collect, assess, or recover a claim against [a] debtor." 11 U.S.C. §362(a) (4), (6). The Court left open the question of whether these provisions might require a creditor to return a debtor's property under certain circumstances.

¹ See *In re Fulton*, 926 F.3d 916 (7th Cir. 2019).





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Allison Arotzky is an associate of the firm in its Creditors' Rights, Restructuring & Bankruptcy practice group. Ms. Arotzky concentrates her practice in the areas of bankruptcy and commercial litigation. Her practice includes the representation of debtors, creditors, and other parties-in-interest in Chapter 11 cases and insolvency-related litigation.

Individual debtors injured by a lessor's willful violations of the automatic stay may recover actual damages, including costs and attorneys' fees as well as punitive damages.² Even following the *Fulton* decision, lessors should still proceed with caution in dealing with seized property upon learning of an individual lessee bankruptcy filing in order to insure that the lessor is not in violation of the automatic stay and is in compliance with turnover requirements.

MHH is available to provide assistance with respect to the issues raised herein. If you have questions or require assistance, please contact Theresa A. Driscoll, Chair of the firm's Creditors' Rights, Restructuring & Bankruptcy practice group, at (516) 880-7278 or tdriscoll@moritthock.com.

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² 11 U.S.C. § 362(k).

