dbr DAILY BUSINESS REVIEW

Rare Standing Granted in Bankruptcy Argument Hinged on 13th Amendment

By Cedra Mayfield | March 11, 2021|

Thirteenth Amendment defenses in bankruptcies cases are nothing new, but an appeals court's establishment of standing in a recent case might have implications for merit going forward.

The U.S. Court of Appeals for the Eleventh Circuit has sided with an Alabama real estate developer, who argued that the appointment of a trustee to control his assets after he voluntarily filed for Chapter 11 bankruptcy protection violated his 13th Amendment rights by subjecting him to involuntary servitude.

'And We Are Skeptical'

Developer Charles Breland Jr. lost control of his holdings when the bankruptcy court determined he was "transferring assets and defrauding his creditors," according to the Eleventh Circuit decision. The bankruptcy court removed him as the debtor-in-possession and appointed a trustee to administer the estate, the appellate ruling said. But Breland challenged that decision, arguing that the trustee would use all his post-petition earnings to benefit his creditors.

"Whatever the merits of Breland's Thirteenth Amendment challenge—and we are skeptical—we hold that the appointment of the trustee sufficiently diminished Breland's ability to control the assets in his own bankruptcy estate to satisfy Article III's standing requirements," Judge Kevin C. Newsom wrote for the Eleventh Circuit.

The decision opened a door for arguments hinged on legal standing.

"My first reaction was a bit of a chuckle, because this issue has come up quite a few times over the life of bankruptcy law, and bankruptcy code in particular, and it's never

really gotten a lot of traction," said Luis Salazar, managing partner of Miami-based Salazar Law, who is not involved in the litigation.

While Salazar doubted the 13th Amendment claim would hold up in court, given the voluntary nature of Chapter 11 proceedings, he said significance lay in the court finding standing.

“The perception is that the 13th Amendment applies to slavery, not to a voluntary economic process. So the claim is somewhat disproportionate to what’s actually happening,” said Salazar. “The idea that you have standing because you lose some rights under a bankruptcy code is an actual potential injury, even though you may not have suffered an actual economic injury, is significant.”

Leon S. Jones, managing partner of Jones & Walden in Atlanta, noted the case was particularly interesting because, unlike Chapter 13 petitions, Chapter 11 filings do not provide debtors the automatic right to dismiss their cases at any time.

“The 13th Amendment issue becomes front and center if there’s a plan to repay,” said Jones, who was not involved in the litigation.

If the real estate developer-turned-plaintiff is bound by a repayment plan, Jones said the issue of involuntary servitude might have merit.

“This decision really doesn’t answer the meaty, important question of whether a plan which proposes to require a debtor to work for five years can be done, if debtor is not a participant in that process,” Jones said. “That’s the important question.”

Loss of Authority

The litigation pitted plaintiff Breland Jr. against attorney A. Richard Maples Jr., U.S. bankruptcy administrator, corporate entity Levada EF Five and the United States of America.

The court did not weigh in on the merit of Breland’s claim, but it did find he had shown an injury-in-fact sufficient to confer standing under Article III of the U.S. Constitution. It ruled that, when Breland was removed as debtor-in-possession and a trustee was appointed, the developer had suffered an injury by losing the authority to control his estate.

It found Breland had been “stripped” of the ability “to assist in the reorganization, use, sell, or lease estate property or obtain unsecured credit outside the ordinary course of business.”

The court also found that Breland’s loss of authority and control over his estate constituted a qualifying injury-in-fact, both traceable to the bankruptcy court’s appointment of the trustee and redressable by an order vacating that appointment.

As such, the Eleventh Circuit ruled Breland had standing to pursue his 13th Amendment claim.

“Subjecting someone who voluntarily petitions for bankruptcy to the plan of a trustee after the debtor has demonstrably breached their duties to their creditors is likely a permissible ‘string,’ so to speak,” said Joe Pack of Pack Law in Miami. “The fact that the debtor loses their unqualified right to convert their Chapter 11 reorganization to a Chapter 7 liquidation under Section 1112 of the Bankruptcy Code is a trickier issue, however.”

“In that circumstance, there is a very real argument that the debtor has been stripped of any escape and is indeed involuntarily working solely for their creditors’ benefit without any say as to benefits the debtor could or should reap from doing so,” Pack continued. “The mere fact that a bankruptcy was voluntary to begin with may be of no defense, because what starts as voluntary case may become involuntary with changes in circumstances.”

Now, the case returns to the lower court. I am hoping there are no far-reaching implications resulting from this decision and that it is simply an anomaly,” said Brett Almon, partner of BAST AMRON in Miami. “My concern here is that future Chapter 11 debtors and their counsel may see this as an opening to contest and draw out the fight over removal and appointment of a trustee.”

“It will be very interesting to read a decision on the merit of the 13th Amendment claim as to indentured servitude,” said **Ray Garcia** of the **Law Office of Ray Garcia** in Miami. “A ruling on the merits in favor of Breland could dramatically change Chapter 11 cases.”