UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Baldi v. Samuel Son & Co., Ltd.

548 F.3d 579 (7th Cir. 2008) · No. Nos. 08-1022, 08-1136 · Decided November 24, 2008

SUMMARY

The Seventh Circuit affirmed judgments rejecting a bankruptcy trustee's attempt to avoid payments made by Longview Aluminum LLC under 11 U.S.C. § 544(b) and the Illinois Uniform Fraudulent Transfer Act. The court held that the trustee failed to establish that Longview was insolvent at the beginning of the relevant period because the expert improperly treated contingent liabilities as certain and confused undercapitalization with insolvency.

CASE DETAILS

COURT	United States Court of Appeals for the Seventh Circuit
WRITING FOR THE COURT	Richard A. Posner; Diane P. Wood; John L. Tinder
JURISDICTION	Federal
DECIDED	November 24, 2008
DOCKET	Nos. 08-1022, 08-1136
DISPOSITION	affirmed
PROCEDURAL POSTURE	The bankruptcy trustee brought adversary proceedings seeking to avoid payments made by Longview Aluminum LLC before bankruptcy under 11 U.S.C. § 544(b) and Illinois's Uniform Fraudulent Transfer Act. The bankruptcy court found that Longview was not insolvent during the relevant period, and the district court affirmed. The trustee appealed.
STANDARD OF REVIEW	The opinion does not expressly state a standard of review; the court reviewed the lower courts' factual finding regarding insolvency and the evidentiary basis for the trustee's expert opinion.
PRECEDENTIAL VALUE	published and precedential
PARTIES	Joseph A. Baldi, et al. v. Samuel Son & Company, Ltd., et al.

TOPICS

fraudulent transfer · adversary proceedings · bankruptcy · commercial litigation · remedies

PRACTICE AREAS

bankruptcy · commercial litigation · fraudulent transfer · remedies · corporate law

QUESTIONS PRESENTED

1. Whether the trustee established that Longview was insolvent at the beginning and end of the transfer period so that the rule of retrojection could establish insolvency on the dates of the challenged transfers.
2. Whether contingent liabilities could be treated as certain liabilities, without discounting them according to the probability that they would materialize, when determining insolvency under 11 U.S.C. § 544(b), the Illinois Uniform Fraudulent Transfer Act, and the Bankruptcy Code's balance-sheet test.
3. Whether Longview's alleged undercapitalization independently established insolvency or supported avoidance of the transfers.

HOLDINGS

1. The court accepted the rule of retrojection as a permissible inference that insolvency on both the beginning and ending dates of the transfer period would support an inference of insolvency on the intervening transfer dates, but held that the trustee failed to prove insolvency at the beginning of the period.
2. Contingent liabilities must be discounted according to the probability that the contingency will occur and the liability will become real; treating contingent liabilities as certain invalidates an insolvency opinion based on that treatment.
3. When a debtor has an existing debt but the creditor may be unable to collect it, the debt may remain a full liability for solvency purposes; that principle does not apply when the contingency is whether any liability will arise in the first place.
4. Undercapitalization is not synonymous with insolvency and does not independently establish that liabilities exceeded assets for purposes of the bankruptcy avoidance claim.

KEY QUOTATIONS

> *"By definition, a contingent liability is not certain—and often is highly unlikely—ever to become an actual liability. To value the contingent liability it is necessary to discount it by the probability that the contingency will occur and the liability become real."* (at 582)

> *"To decide whether a firm is insolvent within the meaning of § 548(a)(2)(B)(i), a court should ask: What would a buyer be willing to pay for the debtor's entire package of assets and liabilities? If the price is positive, the firm is solvent; if negative, insolvent."* (at 583)

> *"'Undercapitalization,' which should rather be termed excessive leverage, while it increases the risk of insolvency, is not insolvency and does not require separate consideration in a bankruptcy case."* (at 584)

FACTUAL BACKGROUND

Longview Aluminum LLC was formed to acquire and operate an aluminum manufacturing plant and received $226 million from the Bonneville Power Administration in exchange for curtailing electricity purchases for sixteen months. At formation, Longview's balance sheet showed assets of $248 million and liabilities of $206 million, although the trustee's expert increased the liabilities by treating several contingent obligations as certain. Longview never resumed operations because aluminum prices fell and electricity prices rose, later declaring bankruptcy. The trustee sought to avoid payments made during the preceding four-year period, claiming that Longview was insolvent when the payments were made.

PROCEDURAL HISTORY

The bankruptcy judge rejected the trustee's fraudulent-transfer claims, finding that Longview had not been insolvent during the period in which the challenged transfers occurred. The district judge affirmed, and the Seventh Circuit affirmed the district court.

DISPOSITION

affirmed

CASES CITED

- Haynes & Hubbard, Inc. v. Stewart, 387 F.2d 906, 908 (5th Cir. 1967)
- In re Mama D'Angelo, Inc., 55 F.3d 552, 554 (10th Cir. 1995)
- Briden v. Foley, 776 F.2d 379, 382-83 (1st Cir. 1985)
- In re Xonics Photochemical, Inc., 841 F.2d 198, 199 (7th Cir. 1988)
- Freeland v. Enodis Corp., 540 F.3d 721, 730 (7th Cir. 2008)
- In re Chase & Sanborn Corp., 904 F.2d 588, 594 (11th Cir. 1990)
- In re Wallace's Bookstores, Inc., 316 B.R. 254, 260-62 (Bankr. E.D. Ky. 2004)
- FDIC v. Bell, 106 F.3d 258, 264-65 (8th Cir. 1997)
- Covey v. Commercial National Bank, 960 F.2d 657, 660 (7th Cir. 1992)
- In re Advanced Telecommunication Network, Inc., 490 F.3d 1325, 1334-36 (11th Cir. 2007)
- Office & Professional Employees International Union v. FDIC, 27 F.3d 598, 601-02 (D.C. Cir. 1994)
- Moody v. Security Pacific Business Credit, Inc., 971 F.2d 1056, 1069-71 (3d Cir. 1992)