Uncorking the Alternative Vintage: Out-of-Court Workouts and ABCs on Tap

Before turning to bankruptcy, companies may find a better blend in out-of-court workouts. This panel will compare workouts with formal proceedings and explore when they are especially advantageous—particularly in industries such as cannabis, venture-backed companies, and crypto—before diving into the structure and strategy of Assignments for the Benefit of Creditors (ABCs), including stakeholder perspectives and asset sales mechanics. The discussion will also address director liability, choice-of-law considerations between California and Delaware, and recent statutory developments, equipping attendees to uncork practical solutions outside the courtroom.

Speakers:

Keith Banner, Esq. – Partner, Greenberg Glusker LLP

Tony Bisconti, Esq. – Partner, Bienert Katzman Littrell Williams LLP

Annie Stoops, Esq. – Counsel, ArentFox Schiff LLP

Nicholas Wilson – Chief Operating Officer, Douglas Wilson Companies

Producers:

Samuel Boyamian, Esq. – Attorney, Margulies Faith LLP

Lane Hilton, Esq. – Attorney, Robberson Schroedter LLP

Uncorking the Alternative Vintage: Out-of-Court Workouts and ABCs on Tap

Saturday, May 16, 2026

8:30 a.m.

60-minute program outline

- Introduction:
  - Brief Panelist introductions
  - Areas of focus and relevant experience
- Why choose an out-of-court workout?
  - Bankruptcy vs. Workouts
    - Overview of key differences
    - Cost, timeline, complexity comparisons and considerations
    - Advantages of workouts
  - Industry examples
    - Cannabis companies
    - Venture capital-backed startups
    - Crypto/digital asset companies
- Assignments for the Benefit of Creditors ("ABCs")
  - Overview
  - Key differences between ABCs and bankruptcy
  - General overview of process and timeline
  - Perspectives and Points of View
    - Assignor
    - Assignees
    - Secured creditors
    - Unsecured Creditors
  - Assets Sales
    - Overview
      - How sales differ in ABCs
    - Voluntary/going-concern sales
    - Pros + Cons of doing sales concurrent with ABC
    - Pros + Cons of doing sales separate from ABC
- Directors/principals personal liability in Workouts
  - Duties
    - What duties?
    - To whom do the duties run, and when?
    - Solvency v. insolvency
    - Business judgment rule
    - LLC v. corporate distinctions
  - Guaranties
    - Do not go away in the ABC
    - ABC as leverage for guaranty settlement terms
    - Tax implications
  - Practical steps to minimize personal exposure

        - Act early
        - Assess exposure before electing path
        - Document, document, document.
        - Separate counsel for principal(s)/directors and company.
        - Ensuring necessary consents are obtained, including potentially by shareholders/members.
        - D&O insurance
    - State Laws – Which State Governs?
        - Choice of law principles
        - Conflict-of-law scenarios
        - Multi-state considerations
    - Legislative Updates (Annie)
        - California
            - New CA tax priority statute
        - Delaware
- Pure Workouts
    - Pure workouts can be anything
        - Multi-party sign onto one agreement
        - Individual settlements or agreements
        - Examples
    - Forbearance Agreements
        - Core deal points of forbearance agreements (reporting, milestones, etc.)
        - Pros + Cons
    - Cannabis Industry
        - Why bankruptcy is not an option
            - Statutory prohibition
                - *In re Arenas*, 535 B.R. 845 (10th Cir. BAP 2015)
            - But, trend towards loosening standards
                - *In Hacienda Co., LLC*, 647 B.R. 748 (Bankr. C.D. Cal. 2023)
        - Out-of-court workouts structured in the cannabis space
        - Regulatory/licensing issues
        - Receiverships are also an option
    - Practical tips and examples
- Conclusion
    - Final tips from panelists
    - Closing remarks and future outlook
    - Questions

ASSIGNMENT FOR THE BENEFIT OF CREDITORS

This Assignment for the Benefit of Creditors ("Assignment") is made and entered into as of **[DATE]**, by and between **[ASSIGNOR NAME]**, a California corporation ("Assignor") and **[ASSIGNEE NAME]**, a California limited liability company ("Assignee") with respect to the following facts:

RECITALS

WHEREAS California law including, but not limited to, California Code of Civil Procedures sections 493.010 through 493.060 and sections 1800 through 1802 provide that debtors may make an assignment for the benefit of creditors, pursuant to which the Assignee will liquidate the debtor's assets and, in accordance with the requirements of applicable law, distribute the proceeds.

WHEREAS Assignor has carefully considered the various options available to Assignor to deal with Assignor's creditors and has decided that it would be in Assignor's best interest and the best interests of Assignor's creditors to make an assignment for the benefit of creditors pursuant to California law.

WHEREAS Assignor believes Assignee is well qualified to efficiently administer the Assignment for the benefit of Assignor's creditors.

WHEREAS Assignor desires to, pursuant to the terms herein, retain Assignee for the purposes of making an assignment for the benefit of creditors pursuant to which Assignee will liquidate the assets of Assignor and distribute the proceeds thereof in accordance with applicable law, and Assignee desires to be so retained, pursuant to the terms herein.

Now, therefore, in consideration of the assignments, covenants, conditions, representations and agreements, Assignor and Assignee agree as follows:

AGREEMENT

1.0 Assignment of Assets for the Benefit of Creditors. Assignor hereby makes this Assignment to Assignee for the benefit of Assignor's creditors. Assignor does hereby grant, bargain, sell, assign, convey and transfer unto Assignee, its successors and assigns, in trust, for the benefit of Assignor's creditors, all of the property of the Assignor of every kind and nature and where so ever situated, both real property (but not facility lease arrangements) and personal, and any interest or equity, including, but not limited to, all that certain stock of merchandise, furniture, fixtures, equipment, book accounts, books, bills receivable, cash on hand, cash in bank, deposits, patents, copyrights, trademarks and trade names and all associated good will, source codes, software and related documents, insurance policies, tax refunds, rebates, insurance refunds and claims, choses in action that are legally assignable, together with the proceeds of any existing non-assignable choses in action that may hereafter be recovered or received by the Assignor to Assignee. Assignor agrees to execute such additional documents as shall be necessary to accomplish the purposes of this Assignment.

Without limiting the foregoing, this Assignment specifically includes and covers all claims for refund or abatement of all excess taxes heretofore or hereafter assessed against or collected from the Assignor by the U.S. Treasury Department and any State or local taxing agency, and Assignor agrees to sign and execute a Power of Attorney attached hereto as **Schedule C** or all other documents as required to enable Assignee to file, prosecute, compromise and/or settle all such claims before the Internal Revenue Service and any state or local taxing agency, and agrees to endorse any tax refund checks relating to the prior operations of Assignor's business and to deliver such checks to Assignee.

Assignee is to receive said property, conduct said business (should it deem it proper), and is hereby authorized at any time after the signing hereof by Assignor to sell and dispose of said property upon such time and terms as Assignee may see fit, and is to pay pro rata to creditors of Assignor the net proceeds arising from the conducting of said business and sale and disposal of said property, after deducting all moneys which Assignee may, at its option, pay for the discharge of any lien on any of said property and any indebtedness, which under the law is entitled to priority of payment, and all expenses including a reasonable fee to Assignee and its attorneys.

Notwithstanding the foregoing, leases and leasehold interests in real estate are not included in this assignment. However, if Assignee shall determine that the same may be assigned and also that the same has a realizable value for creditors, then Assignor agrees that upon written demand of the Assignee, it will assign and transfer said lease or leasehold interest to said Assignee, or nominee, for administration under the terms of this Assignment.

In addition, notwithstanding the foregoing, any employee benefit plan of Assignor (which includes any related employee trust fund), including, without limitation, any ERISA-qualified plan or other similar employee plan, is not being assumed by Assignee or assigned to Assignee and is not being included in the assignment estate. Assignee shall not be or be deemed to be an administrator under any such employee benefit plan, nor shall Assignee be deemed to have assumed or to have any role in, or responsibility for, the termination of any such employee benefit plan. Assignee shall not be deemed to have hired or employed any of Assignor's employees, contractors, representatives or agents nor has Assignee assumed any responsibility for any such employees, contractors, representatives or agents of Assignor or for the termination of any such employees, contractors, representatives or agents of Assignor. Any employment or other business relationship between Assignee and any such employee, contractor, representative or agent of Assignor could only occur and be effective through the joint execution of a written agreement entered into by Assignee and any such employee, contractor, representative or agent of Assignor.

All property assigned to Assignee is hereinafter referred to as "Assigned Property."

Notwithstanding the foregoing, contracts and/or agreements between Assignor and any Labor Union, or Trade Associations and properties exempt from executions are excluded from this Assignment and are not hereby assigned.

2.0 Certain Acknowledgments Regarding Transfer. Assignor acknowledges that certain of the assets being assigned under this Assignment may be subject to restrictions on the use or transfer of such assets, the unauthorized use or transfer of which may result in further damages

or claims. Such assets may include, without limitation, intellectual property rights of Assignor (e.g., trade names, service names, registered and unregistered trademarks and service marks and logos; internet domain names; patents, patent rights and applications therefore, copyrights and registrations and applications therefor; software and source code (and software licenses with respect thereto); customer lists and customer information; know-how, trade secrets, inventions, discoveries, concepts, ideas, methods, processes, designs, formulae, technical data, drawings, specifications, data bases and other proprietary assets (collectively, "Intellectual Property")). Assignor represents and warrants that its officers, directors, shareholders, employees, agents, customers and other third parties have been advised not to use, remove or cause a transfer (other than pursuant to this Assignment) of any of the assets of Assignor, including without limitation the Intellectual Property, either prior or subsequent to this Assignment, except as expressly authorized in writing in advance, which written authorization is not inconsistent with or otherwise may constitute a breach of any other written agreement. Except as authorized in writing, which has been disclosed in writing to Assignee, Assignor further represents and warrants that no asset (including, without limitation, the Intellectual Property) has been transferred, used, or removed; in whole or in part, in a manner that interferes with the rights and interests of a third party(ies) in such asset or otherwise may constitute a breach of any contract with such third party(ies).

3.0 Duties of Assignor.

3.1 Mail. Assignor hereby agrees that all postal correspondence is hereby routed to Assignee through Assignee's method of delivery designated in writing by Assignee.

3.2 Creditor List. Assignor shall concurrently herewith furnish to Assignee a true and complete listing of all Assignor's creditors and shareholders, including but not limited to name, address, contact information, amount of the claim and a brief description of the claims, together with an affidavit verifying same in the form attached hereto as **Schedule A**.

4.0 Duties of Assignee.

4.1 Care for Assigned Property. Assignee shall provide commercially reasonable care for the Assigned Property, to the extent that the Assigned Property includes funds and materials necessary to do so.

4.2 Operation of the Business. Assignee may, at Assignee's discretion, continue to operate the business of Assignor, pending the sale or other liquidation of the Assigned Property. Such operation may include the use of independent contractors retained through an outside service and such other consultants, counsel and advisors as Assignee deems appropriate.

4.3 Conduct of the Assignment for the Benefit of Creditor. Assignee shall be responsible to conduct this Assignment in accordance with applicable law, including but not necessarily limited to the following:

(a) Within 30 days of the date hereof, provide notice to all creditors of the bar date for claims to be filed of not less than 150 days and not more than 180 days of the notice;

(b) Conduct the orderly disposition of the Assigned Property; and

(c) Distribute the proceeds of the disposition of Assigned Property, less Assignee's and its attorneys' fees and expenses in accordance with applicable legal requirements.

5.0 Compensation to Assignee and Reimbursement of Expenses. Assignee is hereby authorized a fee for such service and expense reimbursement as follows:

(a) Assignee's normal hourly rates plus

(b) Out-of-pocket expenses, plus

(c) [**Negotiated Percentage]** commission on any assets liquidated.

Not included in these fees are administrative costs including but not limited to Assignee's and its attorneys' costs and legal fees to administer the Assignment.

[Language for Retainer Payment if any]

6.0 Warranties of Assignee. While having performed preliminary due diligence, Assignee hereby relies upon many representations made by Assignor. Assignee makes no warranties other than the following:

(a) A list of creditors and equity holders has been delivered to Assignee along with an affidavit by Assignor's agents verifying same.

(b) Assignor has completed Assignee's pro forma due diligence (or tendered an equivalent version thereof) and has certified that all information provided is true and correct to the best of its knowledge.

(c) Assignor also warrants that Assignee did not aid in the completion of said documents.

Apart from the receipt of said documents, Assignee makes no warranties or representations regarding Assignor's operations.

7.0 Warranties of Assignor. Assignor represents and warrants to Assignee, acknowledging Assignee will be relying upon the warranty of Assignor, as follows:

(a) Assignor has delivered to Assignee a true correct and complete list of creditors and equity holders, amounts due to each creditor, and contact information for each creditor, amount of equity held by each equity holder and contact information for each equity holder, along with an affidavit verifying same;

(b) Assignor has correctly and completely completed Assignee's pro forma due diligence (or tendered an equivalent version thereof acceptable in the sole discretion of Assignee) and has certified that all info provided is true and correct to the best of its knowledge;

(c) Assignor also warrants that Assignee did not aid in the completion of the documents referenced in Section 7.0(a) and (b) above;

(d) That this Assignment has been properly authorized by all appropriate actions, true and correct copies of which are attached hereto as **Schedule B** and the each of individual(s) executing this Assignment on behalf of Assignor are properly authorized to do so;

(e) That all information provided by Assignor to Assignee with respect to the Assigned Property and/or Assignor's business is true and correct in all material respects and does not fail or omit to state any facts with respect thereto which would be material;

(f) Assignor has all requisite power and authority to execute, deliver and perform its obligations under this Assignment, including, without limitation, to transfer the property transferred to the Assignee hereby;

(g) The execution, delivery and performance by Assignor of this Assignment has been duly authorized by all necessary corporate and other action and does not and will not require any registration with, consent or approval of, or notice to or action by, any person (including any governmental authority) in order to be effective and enforceable; and

(h) This Assignment constitutes the legal, valid and binding obligations of Assignor, enforceable against Assignor in accordance with their respective terms.

8.0 Limitations on Liability of Assignee. Assignor acknowledges that Assignee is acting solely as the Assignee in connection with this Assignment and no member, officer, agent, employee or representative of Assignee is serving as Assignee in their individual capacity. As a result, Assignor expressly agrees that neither Assignee nor any member, officer, agent, employee or representative of Assignee shall be subject to any personal liability whatsoever to any creditor of Assignor or to any other party. In furtherance thereof:

(a) Assignee shall not be required to perform any duties or obligations except for the performance of such duties and obligations as are specifically set forth in this Assignment or as otherwise required by law, and no implied covenants, duties or other obligations shall be read into this Assignment. Assignee may conclusively rely upon the truth, accuracy and completeness of all statements made by Assignor and all documents signed by Assignor or presented by Assignor to Assignee. Assignee shall not be liable for any error of judgment made in good faith, and neither Assignee nor the assignment estate shall be liable for any action taken or omitted to be taken by Assignee made in good faith or upon the advice of counsel or other professional employed by Assignee.

(b) The assignment estate shall defend, indemnify and hold Assignee and all of its past and present officers, members, managers, directors, agents, employees, counsel, representatives, successors and assigns (collectively, "Assignment Estate Representatives") harmless from and against any and all Indemnified Claims (defined below).

(c) The foregoing indemnification provisions shall survive any termination of this Assignment.

(d) For purposes hereof, "Indemnified Claims" means any and all claims, demands, actions, causes of action, judgments, obligations, liabilities, losses, damages and consequential damages, penalties, fines, costs, fees, expenses and disbursements (including without limitation, the fees and expenses of attorneys and all other professionals, consultants and experts in connection with investigation or defense) of every kind, known or unknown, existing or hereafter arising, foreseeable or unforeseeable, which may be imposed upon, threatened or asserted against, or incurred or paid by, any Assignment Estate Representatives at any time and from time to time, because of, resulting from, in connection with, or arising out of this Assignment, the transactions contemplated hereby, including but not limited to economic loss, property damage, personal injury or death in connection with, or occurring on or in the vicinity of, any assets of the assignment estate through any cause whatsoever, any act performed or omitted to be performed under this Assignment, the transactions contemplated hereby, or any breach by Assignor or Assignee, as applicable, of any representation, warranty, covenant, agreement or condition contained herein.

9.0 Reliance.

(a) Assignee may rely and shall be protected in acting upon any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, order, or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties.

(b) Persons dealing with Assignee shall look only to the assignment estate to satisfy any liability incurred by Assignee in good faith to any such person in carrying out the terms of this Assignment, and Assignee shall have no personal or individual obligation to satisfy any such liability.

10.0 Resignation and Replacement of Assignee. Assignee may resign and be discharged from its duties hereunder at any time; provided that such resignation shall not become effective until a successor assignee has been appointed by the resigning Assignee and such successor has accepted its appointment in writing delivered to the resigning Assignee. Any successor assignee appointed hereunder shall execute an instrument accepting such appointment hereunder and shall deliver one counterpart thereof to the resigning Assignee. Thereupon such successor assignee shall, without any further act, become vested with all the estate, properties, rights, powers, trusts, and duties of his predecessor in connection with the Assignment with like effect as if originally named therein, but the resigning Assignee shall nevertheless, when requested in writing by the successor assignee, execute and deliver an instrument or instruments

conveying and transferring to such successor assignee all of the estates, properties, rights, powers and trusts of such resigning Assignee in connection with the Assignment, and shall duly assign, transfer, and deliver to such successor assignee all property and money held by it hereunder.

11.0 Miscellaneous Provisions

a) Governing Law, Jurisdiction and Venue. This Assignment shall be construed under and in accordance with the laws of the State of California, including but not limited to Statute of Limitations laws. The state courts of California shall exercise jurisdiction with respect to any dispute hereunder, and the parties agree that the proper venue for any such dispute shall be in Los Angeles County, State of California.

b) Construction. This Assignment is to be viewed as having been drafted jointly by the parties and is not to be construed for or against any of the parties.

c) Duplicate Counterparts. This Assignment may be executed in duplicate counterparts, each of which shall be deemed to be an original; provided, however, such counterparts shall together constitute only one instrument.

d) Severability. If any provision of this Assignment or any portion of any provision of this Assignment shall be deemed to be invalid, illegal or unenforceable, such invalidity, illegality or unenforceability shall not alter the remaining portion of such provision, or any other provision hereof, as each provision of this Assignment shall be deemed severable from all other provisions hereof.

e) No Third-Party Beneficiary. No term or provision of this Assignment or the schedules hereto is intended to be, nor shall any such term or provision be construed to be, for the benefit of any person, firm, corporation or any other entity not a party hereto (including, without limitation, real estate brokers and finders), and no such other person, firm, corporation or entity shall have any right or cause of action hereunder.

f) Time of Essence. Time is expressly made of the essence as to the performance of each and every obligation and condition of this Assignment.

g) Notices. Any notice or other communication provided for herein or given hereunder to a party hereto must be in writing addressed to the respective party's address listed below and shall be deemed received upon a) actual receipt, or b) 24 hours after sent by email with verbal verification of receipt by receiving party, or c) by overnight delivery by major recognized carrier with verbal verification of receipt by receiving party, or d) five (5) days after sent by Certified Mail, Return Receipt Requested.

To Assignee

With a copy to:

To Assignor: [•]

Either party may change its address for notice purposes by giving notice in the manner set forth in this Section.

h) Headings. The headings of this Assignment are for the purpose of reference only and shall not limit or define the meaning hereof.

i) Attorney Fees. If there is any dispute between the parties with respect to the Assigned Property, this Assignment, the performance of the obligations hereunder or the effect of a termination under this Assignment, the prevailing party shall be paid all costs and expenses incurred by the other party in connection with such proceedings, including reasonable attorneys' fees (including fees for the service of salaried attorneys regularly employed by a party) and costs. The parties agree that each of them shall bear its own legal costs and expenses in connection with the negotiation, drafting, execution of this Assignment.

j) No Waiver. A waiver by either party of a breach of any of the covenants, conditions or obligations under this Assignment to be performed by the other party shall not be construed as a waiver of any succeeding breach of the same or other covenants, conditions or obligations of this Assignment.

k) Entire Agreement. This Assignment constitutes the entire agreement between the Parties. This Assignment may not be amended or modified except by an amendment in writing signed by the handwritten signature of each party. Without limiting the foregoing, no exchange of emails shall serve to amend this Assignment.

12 No Adequate Remedy at Law. Each party hereto acknowledges and agrees that damages will not adequately compensate the other party for a breach of the terms of this Assignment and that, as such, each party shall be entitled to specific performance of this Assignment.

In witness hereof the parties have executed this Agreement sufficient to bind themselves.

_____ _____

Its President Its President

SCHEDULE A

Affidavit

Attached hereto is a complete list of the creditors and shareholders of **[ASSIGNOR NAME]**, a California corporation, which includes names, addresses, cities, states, zip codes, together with the anticipated claim for each creditor of the assignment estate.

I declare under penalty of perjury that the information contained in the attached list is true and correct to the best of my knowledge.

Dated: Click or tap to enter a date.

_____

[•]
President

SCHEDULE B

CONSENT OF DIRECTORS TO HOLD MEETING

[CITY, STATE] [DATE]

We, the undersigned, being all the directors of **[ASSIGNOR NAME]**, a California corporation, assembled this day at the office of this corporation located at **[CITY]**, California, do hereby consent that a meeting of said directors be held at this time and place for the transaction of such business as may come before the meeting, and waive any notice of said meeting.

MINUTES OF THE MEETING

[CITY, STATE] , [DATE]

At a meeting of the directors of **[ASSIGNOR NAME]**, a California corporation, held at the office of the **[ASSIGNOR NAME]**, at [CITY] , California, at ___ o'clock ____, the following directors were present:

Click or tap here to enter text. Click or tap here to enter text.

Click or tap here to enter text. Click or tap here to enter text.

Absent:

The President announced that the purpose of the meeting was to consider the financial condition of the company and the advisability of making a general assignment for the benefit of creditors.

On motion by [•], the following resolution was adopted, to-wit:

BE IT RESOLVED:

That any of the officers of this corporation be, and , hereby authorized and directed by the directors of this company, in meeting assembled, to make an assignment of all assets of the corporation to **[ASSIGNEE NAME]**, a California corporation, of Los Angeles, California ("Assignee"), for the pro rata benefit of all creditors of this corporation, and that any officer, and hereby authorized and directed to execute said assignment containing such provisions as may be agreed upon between them and Assignee, and this corporation is also authorized and directed to execute and deliver to Assignee such other deeds, assignments, and agreements as may be necessary to carry this resolution into effect.

BE IT FURTHER RESOLVED:

That Assignee be, and it hereby is, authorized to execute and file and prosecute on behalf of this corporation all claims for refund or abatement of all excess taxes heretofore or hereafter assessed against or collected from this corporation and any one officer of this corporation be, and it is, hereby authorized and directed to make, execute and deliver in favor of such person as may be designated by the assignee for the benefit of creditors, a power of attorney on the regular printed form thereof used by the United States Treasury Department so as to authorize said attorney-in-fact to process any tax claims for it on behalf of this corporation.

There being no further business to come before the directors, the meeting adjourned subject to the call of the President or Vice-President.

_____

President

I, [•], President of **[ASSIGNOR NAME]**, a California corporation, do hereby certify that the foregoing is a true and correct copy of the minutes of the meeting of directors held in [CITY], CA, at the place and hour stated and that the resolution contained in said minutes was adopted by the directors at said meeting and the same has not been modified or rescinded.

Dated: _____

_____

President

CORPORATE

SEAL

CONSENT TO ASSIGNMENT BY STOCKHOLDERS

I, the undersigned, being owners and holders of shares of stock, being more than 50% of the subscribed and issued stock of **[ASSIGNOR NAME]**, a California corporation, do hereby give our consent to the within assignment and transfer of the property of said corporation.

Signature	Shares Held
[•]	[•]
[•]	[•]
[•]	[•]
[•]	[•]

Schedule C

POWER OF ATTORNEY

[ASSIGNOR NAME], a California corporation, ("Assignor"), is the Assignor under that certain Assignment for the Benefit of Creditors, dated [DATE OF ASSIGNMENT] (the "Assignment"), by and between Assignor and **[ASSIGNEE NAME]**, a California corporation ("Assignee").

WHEREAS, pursuant to the Assignment, Assignor is assigning substantially all of its assets to Assignee to be administered, liquidated and distributed by Assignee as described therein;

NOW, THEREFORE, in order for Assignor to fully effectuate the Assignment and each of the other transactions contemplated thereby, Assignor hereby appoints Assignee its attorney-in-fact and hereby grants to such attorney-in-fact full power and authority to do and perform any and every act and thing whatsoever requisite, necessary, or proper to be done in the exercise of any of the rights and powers herein granted, hereby ratifying and confirming all that such attorney-in-fact shall lawfully do or cause to be done by virtue of this Power of Attorney and the rights and powers herein granted. Assignee, acting through any one of its duly appointed officers, and with full power of attorney in the name of, and for and on behalf of Assignor, may execute, acknowledge, deliver, and record and document or process required to effectuate the Assignment, including but not limited to:

(1) such transfer powers, deeds, bills of sale, assignments of leases, assignments of liens, assignment of notes, assignments of any other assets whatsoever, memoranda of assignments, and such other instruments of transfer and assignment and releases as Assignee shall determine to be necessary or appropriate to consummate or to provide notice of the transfer of any or all of Assignor's assets to Assignee pursuant to the Assignment, in form and substance satisfactory to Assignee, with the execution, acknowledgment, delivery and/or recordation thereof by Assignee to constitute evidence of such determination and Assignee's satisfaction thereof;

(2) such other documents, certificates, receipts, notices, instructions, statements and other writing as Assignee shall determine to be necessary or appropriate in connection with or to carry out the administration or transfer of the Assignor's assets as contemplated by the Assignment, in form and substance satisfactory to Assignee, with the execution, acknowledgment, delivery and/or recordation thereof by Assignee to constitute evidence of such determination and Assignee's satisfaction thereof;

(3) any amendments to the documents of transfer delivered in connection with the transfer or administration of the Assignor's assets as contemplated by the Assignment, as Assignee shall determine to be necessary or appropriate to vest full right, title and interest of the Assignor in and to the Assignor's assets in Assignee pursuant to the terms of the Assignment, in form and substance satisfactory to Assignee, with the execution, acknowledgment, delivery and/or recordation thereof by Assignee to constitute evidence of such determination and Assignee's satisfaction thereof; and

(4) such other documents, certificates, receipts, notices, instructions, statements and other writing as Assignee shall determine to be necessary or appropriate in connection with or to obtain any refund or abatement of excess taxes heretofore or hereafter assessed against or collected from Assignor by the U.S. Treasury Department, and any state or local taxing agency; and

(5) such other documents, certificates, receipts, notices, instructions, statements and other writing as Assignee shall determine to be necessary or appropriate in connection with the administration of employee benefit and retirement programs.

Assignee is hereby empowered to determine in its sole discretion the time or times when, the purpose for and the manner in which any power herein conferred upon it shall be exercised, and the conditions, provisions or covenants of any instrument or document which may be executed by it pursuant hereto. Assignee is further empowered take any other action of any type whatsoever in connection with the foregoing which, in the opinion of Assignee, may be of benefit to, in the best interest of, or legally required to be performed by, the Assignor. Assignee may file and prosecute, compromise and/or settle, all claims before the Internal Revenue Service and any state or local taxing agency as contemplated by the Assignment.

The foregoing is made for the benefit of, and may be relied upon by, Assignee, its successor, assigns, agents and representatives.

This Power of Attorney shall be governed by the laws of the State of California, without regard to choice of law principles.

IN WITNESS WHEREOF, the undersigned has executed this Power of Attorney this ___day of [DATE], to be effective as of such date.

By:_____

[•], President

Statutes Governing Assignments for the Benefit of Creditors

I. California

A. Cal. Civ. Proc. Code §§ 493.010-493.060

1. § 493.010. General Assignment for the Benefit of Creditors; Requirements
2. § 493.020. Authority of Defendant to Make a General Assignment for Benefit of Creditors
3. § 493.030. Termination of Lien of Temporary Protective Order or of Attachment upon Assignment; Effect of Filing Bankruptcy Petition
4. § 493.040. Release of Attachment After Lien Terminates; Procedure
5. § 493.050. Reinstatement of Lien of Temporary Protective Order or Attachment; Particular Cases
6. § 493.060. Subrogation; Preservation of Lien

B. Cal. Civ. Proc. Code §§ 1204-1204.5

1. § 1204. Assignments for Benefit of Creditors; Preferred Labor Claims; Payments; PRO Rata Distribution; Presentation of Claims; Disputed Claims; Receivership Actions
2. § 1204.5. Assignments for Benefit of Creditors; Priority of Deposits for the Purchase or Lease of Realty or Purchase of Services

C. Cal. Civ. Proc. Code §§ 1800-1802

1. § 1800. Recovery of Preferences
2. § 1801. Assignments for Benefit of Creditors; Exempt Property
3. § 1802. Notice of Assignment to Parties in Interest; Claims Filing Deadline; List of Parties in Interest

II. Delaware

A. 10 Del. C. §§ 7381-7387

1. § 7381. Filing Inventory of Property Assigned
2. § 7382. Appointment and Duties of Appraisers
3. § 7383. Assignee's Bond
4. § 7384. Proceedings on Bond
5. § 7385. Assignees' Accounts and Exceptions
6. § 7386. Removal of Assignees
7. § 7387. Void Preferences of Creditors

West's Annotated California Codes
Code of Civil Procedure (Refs & Annos)
Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.010

§ 493.010. General assignment for the benefit of creditors; requirements

Currentness

As used in this chapter, "general assignment for the benefit of creditors" means an assignment which satisfies all of the following requirements:

(a) The assignment is an assignment of all the defendant's assets that are transferable and not exempt from enforcement of a money judgment.

(b) The assignment is for the benefit of all the defendant's creditors.

(c) The assignment does not itself create a preference of one creditor or class of creditors over any other creditor or class of creditors, but the assignment may recognize the existence of preferences to which creditors are otherwise entitled.

Credits
(Added by Stats.1977, c. 499, § 1. Amended by Stats.1982, c. 1198, p. 4319, § 61, operative July 1, 1983.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1982 Amendment

Section 493.010 is amended to conform to the terminology of Title 9 (commencing with Section 680.010) (Enforcement of Judgments Law). See, e.g., Section 703.010, (16 Cal.L.Rev.Comm. Reports 701).

Notes of Decisions (1)

West's Ann. Cal. C.C.P. § 493.010, CA CIV PRO § 493.010
Current with urgency legislation through Ch. 6 of 2026 Reg.Sess. Some statute sections may be more current, see credits for details.

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Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.020

§ 493.020. Authority of defendant to make a general assignment for benefit of creditors

Currentness

Notwithstanding any other provision of this title, the defendant may make a general assignment for the benefit of creditors.

Credits
(Added by Stats.1977, c. 499, § 1.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1977 Addition

Section 493.020 makes clear that, regardless of the terms of any writ of attachment, temporary protective order (Sections 486.010-486.110), or turnover order (Section 482.080), the defendant may make a general assignment for the benefit of creditors. Section 493.020 and the remainder of Chapter 13 reflect the policy favoring general assignments for the benefit of creditors (which contemplate the ratable distribution to creditors of the assignor's assets) over attachment (which permits an unsecured creditor to establish a priority over other unsecured creditors).

West's Ann. Cal. C.C.P. § 493.020, CA CIV PRO § 493.020
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Code of Civil Procedure (Refs & Annos)
Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.030

§ 493.030. Termination of lien of temporary protective order or of attachment upon assignment; effect of filing bankruptcy petition

Currentness

(a) The making of a general assignment for the benefit of creditors terminates a lien of a temporary protective order or of attachment if the lien was created within 90 days prior to the making of the general assignment.

(b) The filing of a petition commencing a voluntary or involuntary case under Title 11 of the United States Code (Bankruptcy) [1] terminates a lien of a temporary protective order or of attachment if the lien was created within 90 days prior to the filing of the petition.

(c) Subdivisions (a) and (b) do not apply unless all liens of attachment on the defendant's property in other states that were created within 90 days prior to the making of a general assignment for the benefit of creditors or the filing of a petition commencing a case under Title 11 of the United States Code (Bankruptcy) have terminated.

Credits

(Added by Stats.1977, c. 499, § 1. Amended by Stats.1979, c. 177, p. 395, § 1, eff. June 29, 1979, operative Oct. 1, 1979.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1977 Addition

Section 493.030 provides for the termination of the lien of a temporary protective order or of an attachment upon the making of a general assignment for the benefit of creditors (defined in Section 493.010) or the commencement of bankruptcy proceedings within [90 days] after the creation of the lien. See also Sections 486.090 (expiration of temporary protective order), 486.110 (lien of temporary protective order from time of service), 488.500 (lien of attachment), 488.510 (duration of lien of attachment).

Section 493.030 is derived from a portion of former Section 542b which provided for the termination of the lien created by service of the notice of attachment hearing and the temporary restraining order when the defendant filed a proceeding under the Bankruptcy Act or made a general assignment for the benefit of creditors. It broadens the former section to provide for the automatic termination of the lien of attachment, thereby making it unnecessary to initiate court proceedings under the Bankruptcy Act to have the lien of attachment declared void. This principle is also applied where the defendant makes a general assignment for the benefit of creditors (defined in Section 493.010) within the specified time. . . .

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Subdivision (c) prevents the termination of attachment liens under this section in a case where attachment liens on the defendant's property in other states are not terminated. This provision recognizes that, in another state, the lien may not be voided under Section 67a(1) of the Bankruptcy Act, 11 U.S.C. § 107(a) (1) (1970), or under the applicable laws in that state relating to general assignments for the benefit of creditors. For example, if the law relating to general assignments in another state does not provide for the termination of an attachment lien in that state, the making of a general assignment would not terminate the attachment lien in California if there is an attachment lien on the defendant's property located elsewhere that would not be terminated. Similarly, if the trustee in bankruptcy does not obtain a court order voiding an attachment lien in another state, an attachment lien in California will not be automatically terminated under subdivision (b) of this section.

This chapter does not affect other provisions voiding liens arising under this title. See, e.g., Ins. Code § 1034 (voidable preferences in insolvency proceedings applicable to insurers) (14 Cal.L.Rev.Comm. Reports 61, amended by 16 Cal.L.Rev.Comm. Reports 701).

1979 Amendment

Section 493.030 is amended to conform to the 90-day preference period prescribed by the Bankruptcy Reform Act of 1978 (Pub.L. No. 95-598), 11 U.S.C. § 547. Other changes in this section conform to the terminology of the new act. The provision relating to general assignments is made uniform with the bankruptcy provision. The reference to preservation of liens for the benefit of the estate is superseded by Section 493.060. See Comment to Section 493.060.

Notes of Decisions (10)

Footnotes

1 11 U.S.C.A. § 101 et seq.

West's Ann. Cal. C.C.P. § 493.030, CA CIV PRO § 493.030
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Code of Civil Procedure (Refs & Annos)
Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.040

§ 493.040. Release of attachment after lien terminates; procedure

Currentness

(a) Where a lien of attachment terminates pursuant to Section 493.030, the assignee under a general assignment for the benefit of creditors or, in the case of a bankruptcy, the trustee, interim trustee, or the debtor in possession if there is no trustee or interim trustee, may secure the release of the attached property by filing with the levying officer a request for release of attachment stating the grounds for release and describing the property to be released, executed under oath, together with a copy thereof.

(b) In the case of an assignee, the request shall include two copies of the general assignment for the benefit of creditors.

(c) In the case of a trustee, interim trustee, or debtor in possession, the request shall include a certified copy of the petition in bankruptcy, together with a copy thereof.

(d) If immediate release of the attachment is sought, the request shall be accompanied by an undertaking to pay the plaintiff any damages resulting from an improper release of the attachment, in the amount to be secured by the attachment, executed by an admitted surety insurer.

(e) Within five days after the filing of the request for release of attachment, the levying officer shall mail to the plaintiff:

(1) A copy of the request for release of the attachment, including the copy of the document filed pursuant to subdivision (b) or (c).

(2) If an undertaking has not been given, a notice that the attachment will be released pursuant to the request for release of attachment unless otherwise ordered by a court within 10 days after the date of mailing the notice.

(3) If an undertaking has been given, a notice that the attachment has been released.

(f) Unless otherwise ordered by a court, if an undertaking has not been given, the levying officer shall release the attachment pursuant to the request for release of attachment after the expiration of 10 days from the date of mailing the papers referred to in subdivision (e) to the plaintiff. If an undertaking has been given, the levying officer shall immediately release the attachment pursuant to the request for release of attachment.

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(g) Where the attached property has been taken into custody, it shall be released to the person making the request for release of attachment or some other person designated in the request. Where the attached property has not been taken into custody, it shall be released as provided in subdivision (c) or (d) of Section 488.730.

(h) The levying officer is not liable for releasing an attachment in accordance with this section nor is any other person liable for acting in conformity with the release.

Credits

(Added by Stats.1977, c. 499, § 1. Amended by Stats.1979, c. 177, p. 395, § 2, eff. June 29, 1979, operative Oct. 1, 1979; Stats.1982, c. 517, p. 2337, § 117; Stats.1982, c. 1198, p. 4321, § 62.5, operative July 1, 1983.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1977 Addition

Section 493.040 provides a procedure for releasing property from an attachment the lien of which has terminated pursuant to Section 493.030. Under Section 493.040, the levying officer is provided with sufficient information to dispose of the attached property in an expeditious and orderly manner. By giving the plaintiff notice before the release takes place, the plaintiff in an appropriate case is able to protect his or her interests in preserving the attachment priority. In the alternative, where the person seeking release has given a proper undertaking, the property is released from attachment immediately and the plaintiff is protected by the undertaking in the amount of the plaintiff's claim to be secured by the attachment. Under the release provisions of Section ..... [488.730], which are incorporated by Section 493.040(g), garnishees are informed that they are relieved of the duties and liabilities of a garnishee arising from service of the notice and writ of attachment. Subdivision (h) protects persons acting in conformity with the release provisions of this section and is the same ..... [in substance as Section 488.730(e)] (14 Cal.L.Rev.Comm. Reports 61, amended by 16 Cal.L.Rev.Comm. Reports 701).

1979 Amendment

Section 493.040 is amended to conform to the elimination of receivers and the creation of interim trustees by the Bankruptcy Reform Act of 1978 (Pub.L. No. 95-598), 11 U.S.C. §§ 105, 303, 701.

1982 Amendment

Section 493.040 is amended [by Stats.1982, c. 1198] to insert a reference to Section 488.730 which replaced former Section 488.560 (16 Cal.L.Rev.Comm. Reports 701).

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Code of Civil Procedure (Refs & Annos)
Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.050

§ 493.050. Reinstatement of lien of temporary protective order or attachment; particular cases

Currentness

(a) The lien of a temporary protective order or of attachment, which has terminated pursuant to Section 493.030, is reinstated with the same effect as if it had not been terminated in the following cases:

(1) Where the termination is the result of the making of a general assignment for the benefit of creditors and the general assignment for the benefit of creditors is set aside otherwise than by the filing of a petition commencing a case under Title 11 of the United States Code (Bankruptcy). [1]

(2) Where the termination is the result of the filing of a petition commencing a case under Title 11 of the United States Code (Bankruptcy) and the petition is dismissed.

(3) Where the termination is the result of the filing of a petition commencing a case under Title 11 of the United States Code (Bankruptcy) and the trustee abandons property which had been subject to the lien of the temporary protective order or of attachment.

(b) The period from the making of a general assignment for the benefit of creditors until reinstatement of the lien of the temporary protective order or of attachment is not counted in determining the duration of the temporary protective order or the lien of attachment.

Credits
(Added by Stats.1977, c. 499, § 1. Amended by Stats.1979, c. 177, p. 396, § 3, eff. June 29, 1979, operative Oct. 1, 1979.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1977 Addition

Section 493.050 provides for reinstatement of the terminated lien where the general assignment for the benefit of creditors is set aside, the [petition commencing a case under Title 11 of the United States Code is dismissed], or the trustee in bankruptcy abandons property that had been subject to a terminated lien. Paragraph (2) of subdivision (a) is derived from a proviso contained

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in Section 67a(1) of the Bankruptcy Act, 11 U.S.C. § 107(a) (1) (1970). Paragraph (1) applies this principle to the analogous situation where the general assignment for the benefit of creditors fails. Paragraph (3) codifies for the purposes of this chapter the principle that, after abandonment, the property is restored to its former status as if it had never been held by the trustee. See Pounds v. Chicago Ins. Co., 298 So.2d 134 (La.Ct.App.1974).

Subdivision (b) provides for the tolling of the running of the effective periods of the temporary protective under Section 486.090 and the lien of attachment under Section 488.510 when the defendant makes a general assignment for the benefit of creditors. Federal law provides for the tolling of state statutes of limitation upon the filing of a petition in bankruptcy. Bankruptcy Act § 11f, 11 U.S.C. § 29(f) (1970); Booloodian v. Ohanesian, 13 Cal.App.3d 635, 91 Cal.Rptr. 923 (1970) (tolling of period of attachment lien under former Section 542b). Note that the effective date of the lien of the reinstated attachment may relate back to the date of service of a temporary protective order as provided in Section 488.500 (14 Cal.L.Rev.Comm. Reports 61, amended by 16 Cal.L.Rev.Comm. Reports 701).

1979 Amendment

Section 493.050 is amended to conform to the terminology of the Bankruptcy Reform Act of 1978 (Pub.L. No. 95-598), 11 U.S.C. § 303.

Footnotes

1 11 U.S.C.A. § 101 et seq.

West's Ann. Cal. C.C.P. § 493.050, CA CIV PRO § 493.050
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Code of Civil Procedure (Refs & Annos)
Part 2. Of Civil Actions (Refs & Annos)
Title 6.5. Attachment (Refs & Annos)
Chapter 13. Effect of Bankruptcy Proceedings and General Assignments for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 493.060

§ 493.060. Subrogation; preservation of lien

Currentness

(a) Upon the making of a general assignment for the benefit of creditors that terminates a lien under this chapter, the assignee is subrogated to the rights of the plaintiff under the temporary protective order or attachment.

(b) Upon the filing of a petition commencing a case under Title 11 of the United States Code (Bankruptcy), a lien terminated pursuant to this chapter is preserved for the benefit of the estate.

Credits

(Added by Stats.1977, c. 499, § 1. Amended by Stats.1979, c. 177, p. 397, § 4, eff. June 29, 1979, operative Oct. 1, 1979.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1977 Addition

Section 493.060 subrogates the assignee under the general assignment for the benefit of creditors to the rights of the attaching plaintiff in order to prevent the termination of the lien of the temporary protective order or of attachment from benefiting a lienholder whose lien was subordinate to the plaintiff's lien but whose lien is not terminated by the making of the general assignment. Hence, where the plaintiff has attached property of the defendant and the property later becomes subject to a security interest, a general assignment by the defendant gives the assignee the priority of the attaching plaintiff whose lien is terminated by Section 493.030(a). Without this provision, the secured party whose interest would otherwise be prior to the assignee's would move up in the line of priorities and the termination of the attachment lien would benefit the secured party rather than the entire estate under control of the assignee. This provision is analogous in effect to the provision in the Bankruptcy Act which permits the trustee to be subrogated to the rights of a lienholder whose lien is void. See Bankruptcy Act § 67a(3), 11 U.S.C. § 107(a)(3) (1970).

1979 Addition

Subdivision (b) is added to Section 493.060 for consistency with the Bankruptcy Reform Act of 1978 (Pub.L. No. 95-598), 11 U.S.C. § 551. This subdivision supersedes the provision formerly found in Section 493.030(b) relating to a court order preserving the lien for the benefit of the bankrupt estate.

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West's Ann.Cal.C.C.P. § 1204

§ 1204. Assignments for benefit of creditors; preferred labor claims; payments; pro rata distribution; presentation of claims; disputed claims; receivership actions

Effective: January 1, 2000
Currentness

When any assignment, whether voluntary or involuntary, and whether formal or informal, is made for the benefit of creditors of the assignor, or results from any proceeding in insolvency or receivership commenced against him or her, or when any property is turned over to the creditors of a person, firm, association or corporation, or to a receiver or trustee for the benefit of creditors, the following claims have priority in the following order:

(a) Allowed unsecured claims, but only to the extent of four thousand three hundred dollars ($4,300) for each individual or corporation, as the case may be, earned within 90 days before the date of the making of such assignment or the taking over of the property or the commencement of the court proceeding or the date of the cessation of the debtor's business, whichever occurs first, for either of the following:

(1) Wages, salaries, or commissions, including vacation, severance and sick leave pay earned by an individual.

(2) Sales commissions earned by an individual, or by a corporation with only one employee, acting as an independent contractor in the sale of goods or services of the debtor in the ordinary course of the debtor's business if, and only if, during the 12 months preceding the date of the making of the assignment or the taking over of the property or the commencement of the proceeding or the date of the cessation of the debtor's business, whichever occurs first, at least 75 percent of the amount that the individual or corporation earned by acting as an independent contractor in the sale of goods or services was earned from the debtor.

(b) Allowed unsecured claims for contributions to employee benefit plans arising from services rendered within 180 days before the date of the making of the assignment or the taking over of the property or the commencement of the court proceeding or the date of the cessation of the debtor's business, whichever occurs first; but only for each employee benefit plan, to the extent of the number of employees covered by the plan multiplied by four thousand three hundred dollars ($4,300), less the aggregate amount paid to the employees under subdivision (a), plus the aggregate amount paid by the estate on behalf of the employees to any other employee benefit plan.

(c) The above claims shall be paid by the trustee, assignee or receiver before the claim of any other creditor of the assignor, insolvent, or debtor whose property is so turned over, and shall be paid as soon as the money with which to pay same becomes available. If there is insufficient money to pay all the labor claims in full, the money available shall be distributed among the claimants in proportion to the amount of their respective claims. The trustee, receiver or assignee for the benefit of creditors shall have the right to require sworn claims to be presented and shall have the right to refuse to pay any such preferred claim,

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either in whole or in part, if he or she has reasonable cause to believe that a claim is not valid but shall pay any part thereof that is not disputed, without prejudice to the claimant's rights, as to the balance of his or her claim, and withhold sufficient money to cover the disputed portion until the claimant in question has a reasonable opportunity to establish the validity of his or her claim by court action, either in his or her own name or through an assignee.

(d) This section is binding upon all the courts of this state and in all receivership actions the court shall order the receiver to pay promptly out of the first receipts and earnings of the receivership, after paying the current operating expenses, such preferred labor claims.

Credits

(Added by Stats.1907, c. 256, p. 321, § 1. Amended by Stats.1931, c. 820, p. 1699, § 1; Stats.1933, c. 175, p. 621, § 1; Stats.1945, c. 1192, p. 2244, § 1; Stats.1951, c. 476, p. 1613, § 1; Stats.1961, c. 1082, p. 2813, § 1; Stats.1979, c. 394, p. 1465, § 3, eff. July 27, 1979, operative Oct. 1, 1979; Stats.1999, c. 202 (S.B.219), § 1.)

Editors' Notes

CODE COMMISSION NOTES

2007 Main Volume

[Sections 1204 to 1027] Have been rewritten and 1208 added, because the first four sections were ambiguous and carelessly drawn. Nothing new is intended by the chapter. It having been noticed too late for correction that a section 1208 had been added to this code at the session of 1905 (1905:632), the section 1208 passed at the session of 1907 should be re-numbered 1207a. The section 1208 which had been passed in 1905 was merely a codification of the provisions concerning foreclosure of liens in the statutes of 1873-4, page 499, and 1901, page 287, relating to cruelty to animals, the penal features whereof have already been codified in the Penal Code and the civil features into the Civil Code.

Notes of Decisions (34)

West's Ann. Cal. C.C.P. § 1204, CA CIV PRO § 1204
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Code of Civil Procedure (Refs & Annos)
Part 3. Of Special Proceedings of a Civil Nature (Refs & Annos)
Title 4. Of the Enforcement of Liens
Chapter 3. Certain Liens and Priorities for Salaries, Wages and Consumer Deposits (Refs & Annos)

West's Ann.Cal.C.C.P. § 1204.5

§ 1204.5. Assignments for benefit of creditors; priority of deposits for the purchase or lease of realty or purchase of services

Currentness

In any general assignment for the benefit of creditors, the following claims shall have priority, subordinate to the priorities for labor claims under Section 1204, but prior to all other unsecured claims: allowed unsecured claims of individuals, to the extent of nine hundred dollars ($900) for each such individual, arising from the deposit, before the commencement of the case, of money in connection with the purchase, lease, or rental of property, or the purchase of services, for the personal, family, or household use of such individuals, that were not delivered or provided. The priority granted by this section shall be subordinate to that granted by Sections 18933 and 26312 of the Revenue and Taxation Code.

Credits

(Added by Stats.1979, c. 394, p. 1466, § 4, eff. July 27, 1979, operative Oct. 1, 1979. Amended by Stats.1980, c. 135, § 5.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1980 Amendment

Section 1204.5 is amended to delete the distinction between general assignments at common law "or otherwise." Former Civil Code Sections 3448 through 3473, which prescribed a general assignment other than at common law, are not continued. See Comment thereto.

West's Ann. Cal. C.C.P. § 1204.5, CA CIV PRO § 1204.5
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West's Annotated California Codes
Code of Civil Procedure (Refs & Annos)
Part 3. Of Special Proceedings of a Civil Nature (Refs & Annos)
Title 11.7. Recovery of Preferences and Exempt Property in an Assignment for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 1800

§ 1800. Recovery of preferences

Effective: July 1, 2012
Currentness

(a) As used in this section, the following terms have the following meanings:

(1) “Insolvent” means:

(A) With reference to a person other than a partnership, a financial condition such that the sum of the person's debts is greater than all of the person's property, at a fair valuation, exclusive of both of the following:

(i) Property transferred, concealed, or removed with intent to hinder, delay, or defraud the person's creditors.

(ii) Property that is exempt from property of the estate pursuant to the election of the person made pursuant to Section 1801.

(B) With reference to a partnership, financial condition such that the sum of the partnership's debts are greater than the aggregate of, at a fair valuation, both of the following:

(i) All of the partnership's property, exclusive of property of the kind specified in clause (i) of subparagraph (A).

(ii) The sum of the excess of the value of each general partner's separate property, exclusive of property of the kind specified in clause (ii) of subparagraph (A), over the partner's separate debts.

(2) “Inventory” means personal property leased or furnished, held for sale or lease, or to be furnished under a contract for service, raw materials, work in process, or materials used or consumed in a business, including farm products such as crops or livestock, held for sale or lease.

(3) “Insider” means:

(A) If the assignor is an individual, any of the following:

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(i) A relative of the assignor or of a general partner of the assignor.

(ii) A partnership in which the assignor is a general partner.

(iii) A general partner of the assignor.

(iv) A corporation of which the assignor is a director, officer, or person in control.

(B) If the assignor is a corporation, any of the following:

(i) A director of the assignor.

(ii) An officer of the assignor.

(iii) A person in control of the assignor.

(iv) A partnership in which the assignor is a general partner.

(v) A general partner of the assignor.

(vi) A relative of a general partner, director, officer, or person in control of the assignor.

(C) If the assignor is a partnership, any of the following:

(i) A general partner in the assignor.

(ii) A relative of a general partner in, general partner of, or person in control of the assignor.

(iii) A partnership in which the assignor is a general partner.

(iv) A general partner of the assignor.

(v) A person in control of the assignor.

(D) An affiliate of the assignor or an insider of an affiliate as if the affiliate were the assignor.

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(E) A managing agent of the assignor.

As used in this paragraph, the following terms have the following meanings:

“Relative” means an individual related by affinity or consanguinity within the third degree as determined by the common law, or an individual in a step or adoptive relationship within the third degree.

An “affiliate” means a person that directly or indirectly owns, controls, or holds, with power to vote, 20 percent or more of the outstanding voting securities of the assignor, or 20 percent or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote by the assignor, excluding securities held in a fiduciary or agency capacity without sole discretionary power to vote, or held solely to secure a debt if the holder has not in fact exercised the power to vote, or a person who operates the business of the assignor under a lease or operating agreement or whose business is operated by the assignor under a lease or operating agreement.

(4) “Judicial lien” means a lien obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding.

(5) “New value” means money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to the transferee in a transaction that is neither void nor voidable by the assignor or the assignee under any applicable law, but does not include an obligation substituted for an existing obligation.

(6) “Receivable” means a right to payment, whether or not the right has been earned by performance.

(7) “Security agreement” means an agreement that creates or provides for a security interest.

(8) “Security interest” means a lien created by an agreement.

(9) “Statutory lien” means a lien arising solely by force of a statute on specified circumstances or conditions, or lien of distress for rent, whether or not statutory, but does not include a security interest or judicial lien, whether or not the interest or lien is provided by or is dependent on a statute and whether or not the interest or lien is made fully effective by statute.

(10) “Transfer” means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, or disposing of or parting with property or with an interest in property, including retention of title as a security interest.

(b) Except as provided in subdivision (c), the assignee of any general assignment for the benefit of creditors, as defined in Section 493.010, may recover any transfer of property of the assignor that is all of the following:

(1) To or for the benefit of a creditor.

(2) For or on account of an antecedent debt owed by the assignor before the transfer was made.

(3) Made while the assignor was insolvent.

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(4) Made on or within 90 days before the date of the making of the assignment or made between 90 days and one year before the date of making the assignment if the creditor, at the time of the transfer, was an insider and had reasonable cause to believe the debtor was insolvent at the time of the transfer.

(5) Enables the creditor to receive more than another creditor of the same class.

(c) The assignee may not recover under this section a transfer as follows:

(1) To the extent that the transfer was both of the following:

(A) Intended by the assignor and the creditor to or for whose benefit the transfer was made to be a contemporaneous exchange for new value given to the assignor.

(B) In fact a substantially contemporaneous exchange.

(2) To the extent that the transfer was all of the following:

(A) In payment of a debt incurred in the ordinary course of business or financial affairs of the assignor and the transferee.

(B) Made in the ordinary course of business or financial affairs of the assignor and the transferee.

(C) Made according to ordinary business terms.

(3) Of a security interest in property acquired by the assignor that meets both of the following:

(A) To the extent the security interest secures new value that was all of the following:

(i) Given at or after the signing of a security agreement that contains a description of the property as collateral.

(ii) Given by or on behalf of the secured party under the agreement.

(iii) Given to enable the assignor to acquire the property.

(iv) In fact used by the assignor to acquire the property.

(B) That is perfected within 20 days after the security interest attaches.

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(4) To or for the benefit of a creditor, to the extent that, after the transfer, the creditor gave new value to or for the benefit of the assignor that meets both of the following:

(A) Not secured by an otherwise unavoidable security interest.

(B) On account of which new value the assignor did not make an otherwise unavoidable transfer to or for the benefit of the creditor.

(5) Of a perfected security interest in inventory or a receivable or the proceeds of either, except to the extent that the aggregate of all the transfers to the transferee caused a reduction, as of the date of the making of the assignment and to the prejudice of other creditors holding unsecured claims, of any amount by which the debt secured by the security interest exceeded the value of all security interest for the debt on the later of the following:

(A) Ninety days before the date of the making of the assignment.

(B) The date on which new value was first given under the security agreement creating the security interest.

(6) That is the fixing of a statutory lien.

(7) That is payment to a claimant, as defined in Section 8004 of the Civil Code, in exchange for the claimant's waiver or release of any potential or asserted claim of lien, stop payment notice, or right to recover on a payment bond, or any combination thereof.

(8) To the extent that the transfer was a bona fide payment of a debt to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of, the spouse or child, in connection with a separation agreement, divorce decree, or other order of a court of record, or a determination made in accordance with state or territorial law by a governmental unit, or property settlement agreement; but not to the extent that either of the following occurs:

(A) The debt is assigned to another entity voluntarily, by operation of law or otherwise, in which case the assignee may not recover that portion of the transfer that is assigned to the state or any political subdivision of the state pursuant to Part D of Title IV of the Social Security Act (42 U.S.C. Sec. 601 et seq.) and passed on to the spouse, former spouse, or child of the debtor.

(B) The debt includes a liability designated as alimony, maintenance, or support, unless the liability is actually in the nature of alimony, maintenance, or support.

(d) An assignee of any general assignment for the benefit of creditors, as defined in Section 493.010, may avoid a transfer of property of the assignor transferred to secure reimbursement of a surety that furnished a bond or other obligation to dissolve a judicial lien that would have been avoidable by the assignee under subdivision (b). The liability of the surety under the bond or obligation shall be discharged to the extent of the value of the property recovered by the assignee or the amount paid to the assignee.

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(e)(1) For the purposes of this section:

(A) A transfer of real property other than fixtures, but including the interest of a seller or purchaser under a contract for the sale of real property, is perfected when a bona fide purchaser of the property from the debtor, against whom applicable law permits the transfer to be perfected, cannot acquire an interest that is superior to the interest of the transferee.

(B) A transfer of a fixture or property other than real property is perfected when a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee.

(2) For the purposes of this section, except as provided in paragraph (3), a transfer is made at any of the following times:

(A) At the time the transfer takes effect between the transferor and the transferee, if the transfer is perfected at, or within 10 days after, the time, except as provided in subparagraph (B) of paragraph (3) of subdivision (c).

(B) At the time the transfer is perfected, if the transfer is perfected after the 10 days.

(C) Immediately before the date of making the assignment if the transfer is not perfected at the later of:

(i) The making of the assignment.

(ii) Ten days after the transfer takes effect between the transferor and the transferee.

(3) For the purposes of this section, a transfer is not made until the assignor has acquired rights in the property transferred.

(f) For the purposes of this section, the assignor is presumed to have been insolvent on and during the 90 days immediately preceding the date of making the assignment.

(g) An action by an assignee under this section must be commenced within one year after making the assignment.

Credits

(Added by Stats.1979, c. 394, p. 1467, § 5, eff. July 27, 1979, operative Oct. 1, 1979. Amended by Stats.1980, c. 135, § 6; Stats.1982, c. 35, p. 64, § 3, eff. Feb. 17, 1982; Stats.1982, c. 497, p. 2175, § 81.5, operative July 1, 1983; Stats.1992, c. 1348 (A.B.2616), § 7; Stats.1995, c. 152 (A.B.1156), § 1; Stats.1999, c. 202 (S.B.219), § 2; Stats.2006, c. 538 (S.B.1852), § 75; Stats.2010, c. 697 (S.B.189), § 26, operative July 1, 2012.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1980 Amendment

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Section 1800 is amended to delete the distinction between general assignments at common law "or otherwise." Former Civil Code Sections 3448 through 3473, which prescribed a general assignment other than at common law, are not continued. See Comment thereto. [15 Cal.L.Rev.Comm. Reports (1980)].

2010 Amendment

Section 1800 is amended to correct a cross-reference and terminology. [37 Cal.L.Rev.Comm. Reports 527 (2007)].

LEGISLATIVE COMMITTEE COMMENTS--SENATE

1982 Amendment

Section 1800 is amended to substitute a reference to Section 1801 in place of the former reference to Title 9 of Part 2.

Note. Section 1800 also was amended by 1982 Cal.Stats. ch. 35 to make substantive changes which are continued in the subsequently amended section as set out above. [16 Cal.L.Rev.Comm. Reports 1001 (1982)].

Notes of Decisions (14)

West's Ann. Cal. C.C.P. § 1800, CA CIV PRO § 1800
Current with urgency legislation through Ch. 6 of 2026 Reg.Sess. Some statute sections may be more current, see credits for details.

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West's Annotated California Codes
Code of Civil Procedure (Refs & Annos)
Part 3. Of Special Proceedings of a Civil Nature (Refs & Annos)
Title 11.7. Recovery of Preferences and Exempt Property in an Assignment for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 1801

§ 1801. Assignments for benefit of creditors; exempt property

Currentness

In any general assignment for the benefit of creditors (as defined in Section 493.010), the assignor, if an individual, may choose to retain as exempt property either the property which is otherwise exempt under Chapter 4 (commencing with Section 703.010) of Division 2 of Title 9 of Part 2 or, in the alternative, the following property:

(a) The assignor's aggregate interest, not to exceed seven thousand five hundred dollars ($7,500) in value, in real property or personal property that the assignor or a dependent of the assignor uses as a residence, in a cooperative that owns property that the assignor or a dependent of the assignor uses as a residence, or in a burial plot for the assignor or a dependent of the assignor.

(b) The assignor's interest, not to exceed one thousand two hundred dollars ($1,200) in value, in one motor vehicle.

(c) The assignor's interest, not to exceed two hundred dollars ($200) in value in any particular item, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the assignor or a dependent of the assignor.

(d) The assignor's aggregate interest, not to exceed five hundred dollars ($500) in value, in jewelry held primarily for the personal, family, or household use of the assignor or a dependent of the assignor.

(e) The assignor's aggregate interest, not to exceed in value four hundred dollars ($400) plus any unused amount of the exemption provided under subdivision (a), in any property.

(f) The assignor's aggregate interest, not to exceed seven hundred fifty dollars ($750) in value, in any implements, professional books, or tools, of the trade of the assignor or the trade of a dependent of the assignor.

(g) Any unmatured life insurance contract owned by the assignor, other than a credit life insurance contract.

(h) The assignor's aggregate interest, not to exceed in value four thousand dollars ($4,000) in any accrued dividend or interest under, or loan value of, any unmatured life insurance contract owned by the assignor under which the insured is the assignor or an individual of whom the assignor is a dependent.

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(i) Professionally prescribed health aids for the assignor or a dependent of the assignor.

(j) The assignor's right to receive any of the following:

(1) A social security benefit, unemployment compensation, or a local public assistance benefit except that this paragraph does not preclude the application of Section 1255.7 of the Unemployment Insurance Code.

(2) A veterans' benefit.

(3) A disability, illness, or unemployment benefit except that this paragraph does not preclude the application of Section 1255.7 of the Unemployment Insurance Code.

(4) Alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the assignor and any dependent of the assignor.

(5) A payment under a stock bonus, pension, profit sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the assignor and any dependent of the assignor, unless:

(i) The plan or contract was established by or under the auspices of an employer of which the assignor was a partner, officer, director or controlling person at the time the assignor's rights under the plan or contract arose;

(ii) The payment is on account of age or length of service; and

(iii) Such plan or contract does not qualify under Section 401(a), 403(a), 403(b), 408, or 409 of the Internal Revenue Code of 1954 (26 U.S.C. 401(a), 403(a), 403(b), 408, or 409). [1]

(k) The assignor's right to receive, or property that is traceable to any of the following:

(1) An award under a crime victim's reparation law.

(2) A payment on account of the wrongful death of an individual of whom the assignor was a dependent, to the extent reasonably necessary for the support of the assignor and any dependent of the assignor.

(3) A payment under a life insurance contract that insured the life of an individual of whom the assignor was a dependent on the date of such individual's death, to the extent reasonably necessary for the support of the assignor and any dependent of the assignor.

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(4) A payment, not to exceed seven thousand five hundred dollars ($7,500), on account of personal bodily injury, as compensation for pain and suffering or actual pecuniary loss (other than loss of future earnings), of the assignor or an individual of whom the assignor is a dependent.

(5) A payment in compensation of loss of future earnings of the assignor or an individual of whom the assignor is or was a dependent, to the extent reasonably necessary for the support of the assignor and any dependent of the assignor.

In this section, "dependent" includes spouse, whether or not actually dependent, "assignor" means each spouse, if the assignment is made by a married couple, and "value" means fair market value as of the date of the making of the assignment.

Credits

(Added by Stats.1982, c. 497, p. 2178, § 82, operative July 1, 1983. Amended by Stats.1983, c. 155, § 23, eff. June 30, 1983, operative July 1, 1983.)

Editors' Notes

LAW REVISION COMMISSION COMMENTS

1982 Addition

Section 1801 continues former Section 690.60 without substantive change (15 Cal.L.Rev.Comm. Reports 2001).

LEGISLATIVE COMMITTEE COMMENTS--SENATE

1983 Amendment

Section 1801 is amended to add references to Section 1255.7 of the Unemployment Insurance Code to preserve the substance of amendments made to its predecessor section (former Section 690.60) by Chapter 1072 of the Statutes of 1982. [16 Cal.L.Rev.Comm. Reports 2175 (1982)].

Footnotes

1 26 U.S.C.A. §§ 401(a), 403(a), 403(b), 408, 409.

West's Ann. Cal. C.C.P. § 1801, CA CIV PRO § 1801
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Title 11.7. Recovery of Preferences and Exempt Property in an Assignment for the Benefit of Creditors (Refs & Annos)

West's Ann.Cal.C.C.P. § 1802

§ 1802. Notice of assignment to parties in interest; claims filing deadline; list of parties in interest

Currentness

(a) In any general assignment for the benefit of creditors, as defined in Section 493.010, the assignee shall, within 30 days after the assignment has been accepted in writing, give written notice of the assignment to the assignor's creditors, equityholders, and other parties in interest as set forth on the list provided by the assignor pursuant to subdivision (c).

(b) In the notice given pursuant to subdivision (a), the assignee shall establish a date by which creditors must file their claims to be able to share in the distribution of proceeds of the liquidation of the assignor's assets. That date shall be not less than 150 days and not greater than 180 days after the date of the first giving of the written notice to creditors and parties in interest.

(c) The assignor shall provide to the assignee at the time of the making of the assignment a list of creditors, equityholders, and other parties in interest, signed under penalty of perjury, which shall include the names, addresses, cities, states, and ZIP Codes for each person together with the amount of that person's anticipated claim in the assignment proceedings.

Credits
(Added by Stats.1992, c. 1348 (A.B.2616), § 8.)

West's Ann. Cal. C.C.P. § 1802, CA CIV PRO § 1802
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West's Delaware Code Annotated
Title 10. Courts and Judicial Procedure
Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7381

§ 7381. Filing inventory of property assigned

Currentness

In every case in which any person makes a voluntary assignment of his or her estate, real or personal, or of any part thereof to any other person in trust for his or her creditors or some of them, the assignee, within 30 days after the execution thereof, shall file in the office of the Register in Chancery of the county in which the real and personal estate of the assignor is situate, an inventory or schedule of the estate or effects so assigned, accompanied with an affidavit by such assignee, that the same is a full and complete inventory of all such estate and effects, so far as the same has come to his or her knowledge.

Credits

15 Laws 1875, ch. 187, § 1. Amended by 70 Laws 1995, ch. 186, § 1, eff. July 10, 1995.

Codifications: Rev. Stat. Del. 1915, § 4651; Rev. Code Del. 1935, § 5109; 10 Del.C. 1953, § 7381

Notes of Decisions (7)

10 Del.C. § 7381, DE ST TI 10 § 7381

Current through ch. 237 of the 153rd General Assembly (2025-2026). Some statute sections may be more current, see credits for details. Revisions to 2026 Acts by the Delaware Code Revisors were unavailable at the time of publication.

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West's Delaware Code Annotated
Title 10. Courts and Judicial Procedure
Part IV. Special Proceedings
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Subchapter VI. Voluntary Assignments

10 Del.C. § 7382

§ 7382. Appointment and duties of appraisers

Currentness

Upon the filing of the inventory and affidavit required by § 7381 of this title, the Court of Chancery shall appoint 2 disinterested and competent persons to appraise the estate assigned, who shall, after being duly sworn or affirmed by some person having authority to administer oaths, to perform their duties with fidelity, forthwith proceed to make an appraisement of the estates and effects assigned, according to the best of their judgment, and having completed the same, shall return the inventory and appraisement to the office of the Register in Chancery of the county in which the inventory of the assignee and the affidavit accompanying the same were filed. The appraisers shall receive the same compensation as is now allowed by law to appraisers of the estate of a decedent.

Credits
15 Laws 1875, ch. 187, § 2.

Codifications: Rev. Stat. Del. 1915, § 4652; Rev. Code Del. 1935, § 5110; 10 Del.C. 1953, § 7382

Notes of Decisions (2)

10 Del.C. § 7382, DE ST TI 10 § 7382
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Title 10. Courts and Judicial Procedure
Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7383

§ 7383. Assignee's bond

Currentness

(a) The assignee shall, as soon as the inventory and appraisement required by § 7382 of this title have been filed, give bond with sufficient surety, to be approved by the Court of Chancery in an amount fixed by the Court, being not less than the total amount of inventory and appraisement of the estate so assigned. The bond shall be taken in the name of the State, and the condition thereof shall be as follows:

> "The condition of this obligation is such, that if the above bounden ... assignee of ... shall in all things comply with the provisions of this chapter, and shall faithfully execute the trust confided to him or her, then the above obligation to be void, otherwise to remain in full force and virtue."

(b) To the bond there shall be subjoined a warrant of attorney to confess judgment thereon, and the bond and warrant shall be joint and several, and such bond shall be filed in the office of the Register in Chancery of the county in which the inventory and appraisement were filed, and shall inure to the use of all persons interested in the property assigned.

Credits

15 Laws 1875, ch. 187, § 3. Amended by 48 Laws 1951, ch. 88, § 1; 70 Laws 1995, ch. 186, § 1, eff. July 10, 1995.

Codifications: Rev. Stat. Del. 1915, § 4653; Rev. Code Del. 1935, § 5111; 10 Del.C. 1953, § 7383

10 Del.C. § 7383, DE ST TI 10 § 7383

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Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7384

§ 7384. Proceedings on bond

Currentness

Upon the application of any person interested, the Court of Chancery may direct the bond provided under § 7383 of this title to be proceeded on if it deems it necessary and proper for the protection of such interested party.

Credits
15 Laws 1875, ch. 187, § 4.

Codifications: Rev. Stat. Del. 1915, § 4654; Rev. Code Del. 1935, § 5112; 10 Del.C. 1953, § 7384

10 Del.C. § 7384, DE ST TI 10 § 7384
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Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7385

§ 7385. Assignees' accounts and exceptions

Currentness

(a) The assignee shall render an account of the assignee's trusteeship every year from the date of the assignee's bond, required under § 7383 of this title, before the Register in Chancery of the proper county, until the trusteeship is closed and a final account rendered and approved. If the assignee fails to perform this duty, the Register in Chancery may issue a citation to such assignee, requiring the assignee to appear and exhibit under oath or affirmation the accounts of the trusts, within a certain time to be named in such citation.

(b) Upon the filing of any such account, notice thereof shall be given to all persons in interest as directed by an appropriate order of the Court of Chancery. Such order and notice shall set forth the time within which any person in interest may take and file with the Register in Chancery, in and for the proper county, exceptions to the account in question. The time within which exceptions to any such account may be filed by any person in interest shall be determined by the Court in the exercise of its discretion, and may be extended from time to time for good cause shown. Any exceptions so filed in respect of any such account shall be heard, determined and the particular account adjusted before the Court, as it may order or direct.

Credits
15 Laws 1875, ch. 187, § 5. Amended by 48 Laws 1951, ch. 80, § 1; 70 Laws 1995, ch. 186, § 1, eff. July 10, 1995.

Codifications: Rev. Stat. Del. 1915, § 4655; Rev. Code Del. 1935, § 5113; 10 Del.C. 1953, § 7385

Notes of Decisions (3)

10 Del.C. § 7385, DE ST TI 10 § 7385
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West's Delaware Code Annotated
Title 10. Courts and Judicial Procedure
Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7386

§ 7386. Removal of assignees

Currentness

The Court of Chancery, upon cause being shown, may remove the assignee or trustee referred to in this chapter, and compel an assignment of the trust estate to others appointed in their stead. Any order of the Court in the premises may be enforced by attachment and imprisonment.

Credits
15 Laws 1875, ch. 187, § 6.

Codifications: Rev. Stat. Del. 1915, § 4656; Rev. Code Del. 1935, § 5114; 10 Del.C. 1953, § 7386

Notes of Decisions (4)

10 Del.C. § 7386, DE ST TI 10 § 7386
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West's Delaware Code Annotated
Title 10. Courts and Judicial Procedure
Part IV. Special Proceedings
Chapter 73. Insolvency
Subchapter VI. Voluntary Assignments

10 Del.C. § 7387

§ 7387. Void preferences of creditors

Currentness

Whenever any person, in contemplation of insolvency or in contemplation of taking the benefit of any of the insolvent laws of this State, makes an assignment of his or her estate or effects for the benefit of creditors, and by such assignment, either under its provisions or otherwise, prefers any creditor to others, or in or by such assignment, secures or pays to any creditor a greater proportion of his or her debt or demand than shall be secured or paid to all his or her creditors, every such assignment so giving a preference shall be deemed fraudulent and absolutely void, and the estate or effects contained therein shall be liable to be taken in execution, or attached, for the payment of such assignor's debts, as fully as if no such assignment had been made; and whoever makes such fraudulent assignment shall forever be deprived of the benefit of any insolvent law of this State.

Credits
Amended by 70 Laws 1995, ch. 186, § 1, eff. July 10, 1995.

Codifications: Rev. Code Del. 1852, § 2915; Rev. Stat. Del. 1915, § 4795; Rev. Code Del. 1935, § 5282; 10 Del.C. 1953, § 7387

Notes of Decisions (7)

10 Del.C. § 7387, DE ST TI 10 § 7387
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144 Cal.App.4th 590
Court of Appeal, Fourth District, Division 3, California.

CREDIT MANAGERS ASSOCIATION OF CALIFORNIA, Plaintiff and Appellant,
v.
COUNTRYWIDE HOME LOANS, INC., Defendant and Respondent.

No. G035739.
|
Oct. 4, 2006.
|
Review Denied Jan. 24, 2007. *

Synopsis

Background: Assignee of general assignment for the benefit of creditors filed action against mortgage company seeking to recover transfers debtor made to mortgage company while it was insolvent. The Superior Court of Orange County, No, 04CC11556, Thierry P. Colaw, J., sustained mortgage company's demurrer without leave to amend and assignee appealed.

The Court of Appeal, O'Leary, J., held that statute authorizing assignee to avoid and recover preferential transfers was not preempted by Bankruptcy Code.

Reversed.

Attorneys and Law Firms

****260** Winthrop Couchot, William John Wall, Newport Beach, for Plaintiff and Appellant.

Sanford Shatz, Calabasas, and Stephen T. Hicklin, Glendale, for Defendant and Respondent.

Glickfield, Fields & Jacobson and Lawrence M. Jacobson, Los Angeles, for CBS Radio Inc., as Amicus Curiae on behalf of Defendant and Respondent.

***593** OPINION

O'LEARY, J.

In this case, we must decide whether the United States Bankruptcy Code preempts Code of Civil Procedure section 1800, [1] recovery of preferences (Section 1800). In *Sherwood Partners, Inc. v. Lycos, Inc.* (9th Cir.2005) 394 F.3d 1198 (*Sherwood*), Judge Alex Kozinski of the Ninth Circuit Court of Appeals wrote for the majority and held the Bankruptcy Code preempted Section 1800. In *Haberbush v. Charles & Dorothy Cummins Family Limited Partnership* (2006) 139 Cal.App.4th 1630, 1633, 43 Cal.Rptr.3d 814 (*Haberbush*), the Second District Court of Appeal, citing to Judge Dorothy Nelson's dissent in *Sherwood,* held it did not.

Credit Managers Association of California (CMAC) argues the trial court erroneously relied on *Sherwood,* which is nonbinding federal authority, to find the Bankruptcy Code preempts Section 1800. Countrywide recognizes *Sherwood* is not binding on this court, but contends its reasoning is persuasive and we should rely on it to affirm the trial court's judgment. By "Supplemental Citation," CMAC suggests we rely on *Haberbush* to reverse the trial court's judgment. As we explain below, we find *Haberbush* persuasive and conclude the Bankruptcy Code does not preempt Section 1800.

FACTS

Where the facts are undisputed, and the propriety of the order sustaining the demurrer turns on an issue of federal preemption, we review the decision de novo. (*American Internat. Group, Inc. v. Superior Court* (1991) 234 Cal.App.3d 749, 755, 285 Cal.Rptr. 765.) Between September 23, 2003, and December 22, 2003, Instafi transferred approximately $267,051 to its creditor, Countrywide, while Instafi was insolvent. On or about December 22, 2003, Instafi executed an assignment for the benefit of its creditors to CMAC of all its assets pursuant to section 493.010. [2] ****261** There was no allegation Instafi filed for bankruptcy.

CMAC filed a complaint against Countrywide seeking to recover the transfers Instafi made to Countrywide citing Section 1800. Countrywide demurred to the complaint on the grounds ***594** section 547 of title 11 of the United States Code (Section 547) preempts Section 1800. CMAC opposed the demurrer, and Countrywide responded. After hearing argument, the trial court sustained Countrywide's demurrer without leave to amend.

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DISCUSSION

Section 1800, subdivision (b), states: "Except as provided in subdivision (c), the assignee of any general assignment for the benefit of creditors (as defined in [s]ection 493.010) may recover any transfer of property of the assignor: [¶] (1) To or for the benefit of a creditor; [¶] (2) For or on account of an antecedent debt owed by the assignor before the transfer was made; [¶] (3) Made while the assignor was insolvent; [¶] (4) Made on or within 90 days before the date of the making of the assignment or made between 90 days and one year before the date of making the assignment if the creditor, at the time of the transfer, was an insider and had reasonable cause to believe the debtor was insolvent at the time of the transfer; and [¶] (5) That enables the creditor to receive more than another creditor of the same class."

Section 547, subdivision (b), provides: "Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—[¶] (1) to or for the benefit of a creditor; [¶] (2) for or on account of an antecedent debt owed by the debtor before such transfer was made; [¶] (3) made while the debtor was insolvent; [¶] (4) made—(A) on or within 90 days before the date of the filing of the petition; or (B) between [90] days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and [¶] (5) that enables such creditor to receive more than such creditor would receive if —(A) the case were a case under chapter 7 of this title; (B) the transfer had not been made; and (C) such creditor received payment of such debt to the extent provided by the provisions of this title."

In *Sherwood,* the court addressed the same issue we are faced with here: whether the Bankruptcy Code preempted Section 1800. (*Sherwood, supra,* 394 F.3d at p. 1200.) Similar to the facts in our case, Thinklink transferred $1 million to Lycos. Two months later, Thinklink made a voluntary general assignment for the benefit of creditors to Sherwood. Sherwood sued Lycos to recover the $1 million pursuant to Section 1800. After the matter was removed to federal court, the district court rejected Lycos's preemption argument and granted Sherwood's motion for summary judgment. (*Ibid.*)

The *Sherwood* court began by explaining the applicable preemption principles: "Congress has broad authority to preempt state laws, but whether ***595** Congress has done so in a particular instance is a matter of congressional intent. This intent is most easily detected where the statute expressly preempts other laws, but preemption may also be inferred where it is clear from the statute and surrounding circumstances ****262** that Congress intended to occupy the field, leaving no room for state regulation. The Supreme Court[ ] [has] [citation] ... summarized the contours of the field preemption doctrine: Absent explicit pre-emptive language, Congress' intent to supersede state law altogether may be found from a ' "scheme of federal regulation ... so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it," because "the Act of Congress may touch a field in which the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject," or because "the object sought to be obtained by the federal law and the character of obligations imposed by it may reveal the same purpose." ' [¶] [Citations.] 'Even where Congress has not entirely displaced state regulation in a specific area,' the Court continued, 'state law is pre-empted ... where [it] "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." ' [Citations.]

"There can be no doubt that federal bankruptcy law is 'pervasive' and involves a federal interest 'so dominant' as to 'preclude enforcement of state laws on the same subject'—much like many other areas of congressional power listed in Article I, Section 8, of the Constitution, such as patents, copyrights, currency, national defense and immigration. The Bankruptcy Clause, which grants Congress the power to make bankruptcy laws, U.S. Const. art. I, § 8, cl. 4, stresses that such rules must be 'uniform.' Bankruptcy law occupies a full title of the United States Code. It provides a comprehensive system of rights, obligations and procedures, as well as a complex administrative machinery that includes a special system of federal courts and United States Trustees.

"At the same time, federal law coexists peaceably with, and often expressly incorporates, state laws regulating the rights and obligations of debtors (or their assignees) and creditors. *See, e.g.,* ... [11 United States Code] Section 544(b)[(1)] (making state law on voidable transfers available to the bankruptcy trustee)...." (*Sherwood, supra,* 394 F.3d at pp. 1200–1201.)

The *Sherwood* court first addressed Sherwood's claim the Bankruptcy Code does not preempt Section 1800 because it is specifically incorporated by 11 U.S.C. section 544(b)(1) of title 11 of the United States Code Section 544(b)(1)), which

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allows a bankruptcy trustee to avoid any transfers voidable by unsecured creditors under " 'applicable law[,]' " including state law. (*Sherwood, supra,* 394 F.3d at p. 1201.) The court disagreed with Sherwood because ***596** Section 544(b)(1) limits the trustee's powers to unsecured creditors whereas Section 1800 can only be exercised by general assignees. (*Ibid.*) Interpreting the statutory definitions of " 'creditor' " and " 'custodian,' " which includes " 'assignee[s] under a general assignment for the benefit of the debtor's creditors[ ]' " the court opined " 'creditor' " does not include "custodians." (*Id.* at p. 1202.)

Next, the *Sherwood* court addressed whether Section 1800's assignee's special avoidance powers could "coexist with the federal bankruptcy scheme." (*Sherwood, supra,* 394 F.3d at p. 1202.) The court explained the Bankruptcy Code embodies two separate and somewhat independent ideals: "It is generally agreed that chapter 7 of the Bankruptcy Code, which governs liquidations, embodies two ideals: (1) giving the individual debtor a fresh start, by giving him a discharge of most of his debts; and (2) equitably distributing a debtor's assets among competing creditors." ****263** (*Id.* at p. 1203.) The court explained the United States Supreme Court has held state laws that perform the first function, the discharge of debts, are preempted. (*Ibid.*)

As to the second function, the court, without citation to any authority, stated, "What goes for state discharge provisions also holds true for state statutes that implicate the federal bankruptcy law's other major goal, namely equitable distribution." (*Sherwood, supra,* 394 F.3d at p. 1203.) The court explained the federal bankruptcy scheme accomplishes equitable distribution through a collective proceeding created to prevent a "feeding frenzy" and " 'bring together and adjust all of the rights and duties of creditors and embarrassed debtors alike.' " (*Id.* at pp. 1203–1204.)

The court relied on several factors as a basis for its decision the Bankruptcy Code preempted state laws that implicate equitable distribution. First, Sections 547(b)[3] and 544(b)(1)[4] give the trustee "the power to avoid preferential transfers" and recover the sums to distribute to creditors. (*Sherwood, supra,* 394 F.3d at p. 1204, fn. omitted.) ***597** And there are safeguards in place to ensure the trustee is performing appropriately: the trustee is subject to the jurisdiction of the federal courts, the United States Trustee appoints and supervises the trustee or is elected by the creditors, unlike the "assignee" who is hand-picked by the debtor, and federal law protects creditors through conflict of interest laws. (*Ibid.*)

Second, if a state assignee recovers a preferential transfer pursuant to Section 1800 and distributes it, a federal trustee cannot recover "the same sum under the federal preference statute if a federal bankruptcy proceeding is [filed]." (*Sherwood, supra,* 394 F.3d at p. 1204.) "The distribution of the recovered sum will then have been made by a state assignee subject to state procedures and substantive standards, rather than by the federal trustee subject to bankruptcy law's substantive standards and procedural protections." (*Ibid.,* fn. omitted.)

Last, once state court proceedings begin, "they will affect the incentives of various parties as to whether they wish to avail themselves of federal bankruptcy law. The creditor whose ox is being gored by the state assignee may have a new incentive to begin an involuntary federal proceeding; other creditors ... may have diminished incentives[ ]" because they may share in sums recovered by the assignee and "might therefore have no interest in invoking the potentially more expensive and time-consuming federal processes." (*Sherwood, supra,* 394 F.3d at p. 1205.) The court concluded, "We believe that statutes that give state assignees or trustees avoidance powers beyond those that ****264** may be exercised by individual creditors trench too close upon the exercise of the federal bankruptcy power.... The exercise of the preference avoidance power by Sherwood under the authority of [S]ection 1800 is inconsistent with the enactment and operation of the federal bankruptcy system and is therefore preempted." (*Id.* at pp. 1205–1206.)

CMAC argues the trial court erred in relying on *Sherwood* to conclude the Bankruptcy Code preempted Section 1800. CMAC contends this court is not bound by *Sherwood,* there is a strong presumption against preemption, the United States Supreme Court has approved state statutes similar to Section 1800, and the *Haberbush* court's analysis of the issue is more persuasive.

Countrywide contends that although we are not bound by *Sherwood,* we should afford it great weight because it is a federal court's interpretation of federal law. Countrywide asserts the Bankruptcy Code, specifically Section 547, preempts Section 1800 because Section 547 granted to "trustees in bankruptcy" the ability to recover "preference payments." Therefore, Countrywide claims, Congress has " 'occupied the field' of bankruptcy law," or alternatively,

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Section 1800 " ' "stands as an obstacle" ' " to Section 547 because Section 1800 grants to "assignees" the power to recover preference payments.

***598** At the outset, we note we are mindful that lower federal court decisions on federal questions are persuasive authority, but they are not binding on this court. (*Walker v. Kiousis* (2001) 93 Cal.App.4th 1432, 1441, 114 Cal.Rptr.2d 69.) As we explain below, we find the *Haberbush* court's analysis of the issue more persuasive and conclude Section 547 does not preempt Section 1800 because Congress did not " 'occup[y] the field' " when it enacted Section 547 and Section 1800 does not " ' "stand[ ] as an obstacle" ' " to Section 547.

In *Haberbush,* the court faced the same issue the *Sherwood* court faced, and the same issue we are faced with here—does the Bankruptcy Code preempt Section 1800? (*Haberbush, supra,* 139 Cal.App.4th at p. 1633, 43 Cal.Rptr.3d 814.) Again, similar to the facts in our case, "Carolyn's Country Pies, Inc. ... executed a voluntary general assignment for the benefit of creditors [ ]" to Haberbush. (*Ibid.*) Haberbush sued three defendants to recover certain payments as preferential transfers pursuant to Section 1800. (*Id.* at p. 1634, 43 Cal.Rptr.3d 814.)

After reciting the *Sherwood* court's summary of the applicable preemption principles as correct, the *Haberbush* court disagreed with the *Sherwood* court's analysis of the issue because the court found "it impossible to conclude ... [S]ection 1800 is inconsistent with 'the essential goals and purposes of federal bankruptcy law....' [Citation.]" (*Haberbush, supra,* 139 Cal.App.4th at p. 1637, 43 Cal.Rptr.3d 814.)

The *Haberbush* court articulated five reasons for its conclusion the Bankruptcy Code does not preempt Section 1800 and the *Sherwood* court got it wrong.

"First, it is undisputed that Congress intended, in general, to permit the coexistence of state laws governing voluntary assignments for the benefit of creditors. As *Sherwood Partners* necessarily concedes, voluntary assignments for the benefit of creditors have 'a venerable common-law pedigree' [citation] and were expressly upheld [by the United States Supreme Court].... [(See *Pobreslo v. Jospeph M. Boyd Co.* (1933) 287 U.S. 518, 526[, 53 S.Ct. 262, 77 L.Ed. 469] (*Pobreslo*) [state law regulating voluntary assignments serving to protect creditors against each other and assuring equality of distribution in ****265** harmony with federal Act]; *Stellwagen v. Clum* (1918) 245 U.S. 605, 615[, 38 S.Ct. 215, 62 L.Ed. 507] (*Stellwagen*) [state law permitting appointment of a receiver to take charge of all assets of the debtor and administer them for the equal benefit of all creditors not opposed to bankruptcy law policy, rules or principles].)] Indeed, the Bankruptcy Code expressly makes state law on voidable transfers available to the bankruptcy trustee. (... § 544(b)[(1)].)" (*Haberbush, supra,* 139 Cal.App.4th at p. 1637, 43 Cal.Rptr.3d 814, fn. omitted.)

***599** "Second, *Sherwood* ... reaches too far in suggesting that any state statute that 'implicate[s]' the federal bankruptcy law's second major goal of equitable distribution is preempted. [Citation.] The statutes upheld against preemption challenges in *Pobreslo* and *Stellwagen* obviously implicate the federal bankruptcy law's goal of equitable distribution. Indeed, *Pobreslo* and *Stellwagen* expressly refer to that goal in upholding the state statutes. (*Pobreslo, supra,* 287 U.S. at p. 526[, 53 S.Ct. 262] [state law assures 'equality of distribution']; *Stellwagen, supra,* 245 U.S. at p. 615 [, 38 S.Ct. 215] [state law 'is not opposed to the policy of the bankruptcy law .... with a view to the fair distribution of the assets of the insolvent'].) In short, the mere fact that a state law 'implicate[s]' the Bankruptcy Code's goal of equitable distribution is not sufficient to justify the conclusion that the state law 'stands as an obstacle' to that goal. [Citation.]" (*Haberbush, supra,* 139 Cal.App.4th at pp. 1637–1638, 43 Cal.Rptr.3d 814, fn. omitted.)

"Third, the *Sherwood* ... [court's] conclusion ... [S]ection 1800 is preempted rests, in essence, on ... two points: (1) the fact that [S]ection 1800 gives the assignee powers beyond those that may be exercised by individual unsecured creditors; and (2) the proposition that the assignee's powers to avoid preferential transfers will 'affect the incentives of various parties as to whether they wish to avail themselves of federal bankruptcy law[,]' thereby interfering with the code's goal of equitable distribution of a debtor's assets. [Citation.] However: [¶]—As Judge Nelson points out in her dissent, '[s]tate voluntary assignments, by definition, give the assignee more power than may be exercised by an individual creditor.' [Citation.] The majority's reliance on this distinction thus would cast doubt on the validity of all voluntary assignment statutes, not merely those allowing the assignee to avoid preferential transfers. Yet[,] Supreme Court precedents clearly reject the notion that voluntary assignments generally are incompatible with federal bankruptcy law. [Citations.] [¶] —As for the alteration of incentives to use federal bankruptcy law, we do not doubt that incentives may be affected by the

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existence of an alternative to formal bankruptcy proceedings —particularly an alternative that may be less 'expensive and time-consuming....' [Citation.] Again, however, incentives to use bankruptcy law may be affected by any voluntary assignment laws, whether or not the assignee has the power to avoid preferential transfers. The only pertinent question is whether the state statute's effect on those incentives somehow interferes with or is an obstacle to the Bankruptcy Code's objective of equitable distribution. In our view, the *Sherwood* ... majority provides no cogent explanation of how the assignee's avoidance powers conflict with that objective. As Judge Nelson correctly observed, because the common law right to make an assignment of property for the benefit of creditors is well established, it is 'illogical that state laws that provide a forum for the equitable distribution of that property should be ***600** preempted by federal bankruptcy law.' [Citation.]" (*Haberbush, supra,* 139 Cal.App.4th at pp. 1638–1639, 43 Cal.Rptr.3d 814, fns. omitted.)

****266** "Fourth, the *Sherwood* ... majority correctly points out that if a preferential transfer is recovered by the assignee, the same sum could not be recovered if a federal bankruptcy proceeding were filed. However, as Judge Nelson observes: 'But California's preference recovery provision is, by design, virtually identical to the [B]ankruptcy [C]ode's preferential transfer statute. [Citations.] If the same transfer can be avoided in both the state and federal systems, how does the state system interfere with bankruptcy's goal of equitable distribution? Both the state and federal statutes serve to ensure equality of distribution and to deter the race to recover assets before insolvency. [Citations.] That California's voluntary assignment system has such a provision makes it more capable of effectuating the equality of distribution that is the aim of the bankruptcy law; it does not necessarily interfere with bankruptcy's goal of achieving equal distribution.' [Citation.]" (*Haberbush, supra,* 139 Cal.App.4th at pp. 1639–1640, 43 Cal.Rptr.3d 814, fn. omitted.)

"Finally, as Judge Nelson also pointed out, federal regulation should not be deemed preemptive of state regulatory power absent ' "persuasive reasons—either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained." ' [Citations.] This is not such a case. Voluntary assignments and the bankruptcy system have coexisted since the inception of bankruptcy law, and state laws regulating the rights and obligations of debtors or their assignees and creditors are often expressly incorporated in bankruptcy law. [Citation.] Congress has not indicated that voluntary assignments generally or preferential transfer avoidance laws specifically are to be preempted. [Citation.] Under these circumstances, we can discern no persuasive reason to conclude that California's 'less stigmatic, and less costly, voluntary assignment scheme' [citation]—which, like the federal bankruptcy system, serves to ensure equality of distribution of a debtor's assets—'stands as an obstacle to the accomplishment ... of the full purposes and objectives' of the federal bankruptcy system. [Citation.]" (*Haberbush, supra,* 139 Cal.App.4th at p. 1640, 43 Cal.Rptr.3d 814.)

Based on our independent reading of Section 1800 and Section 547, and their goals and underlying policies, and United States Supreme Court precedent, we conclude the *Haberbush* court's reasoning Congress did not intend to " 'occup [y] the field' " when it enacted Section 547, and Section 1800 does not " 'stand[ ] as an obstacle' " to Section 547 is persuasive. The Bankruptcy Code, specifically Section 547(b), does not preempt Section 1800.

***601** DISPOSITION

The judgment is reversed. Credit Managers Association of California shall recover its costs on appeal.

BEDSWORTH, Acting P.J., and IKOLA, J., concur.

All Citations

144 Cal.App.4th 590, 50 Cal.Rptr.3d 259, 06 Cal. Daily Op. Serv. 10,209

Footnotes

* Moreno, J., did not participate therein.

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1 All further statutory references are to the Code of Civil Procedure, unless otherwise indicated.

2 Section 493.010, the validity of which is not at issue in this appeal, states, “As used in this chapter, ‘general assignment for the benefit of creditors' means an assignment which satisfies all of the following requirements: [¶] (a) The assignment is an assignment of all the defendant's assets that are transferable and not exempt from enforcement of a money judgment. [¶] (b) The assignment is for the benefit of all the defendant's creditors. [¶] (c) The assignment does not itself create a preference of one creditor or class of creditors over any other creditor or class of creditors, but the assignment may recognize the existence of preferences to which creditors are otherwise entitled.”

3 Section 547(b) states: “Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—(1) to or for the benefit of a creditor; (2) for or on account of an antecedent debt owed by the debtor before such transfer was made; (3) made while the debtor was insolvent; (4) made—(A) on or within 90 days before the date of the filing of the petition; or (B) between [90] days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and (5) that enables such creditor to receive more than such creditor would receive if—(A) the case were a case under chapter 7 of this title; (B) the transfer had not been made; and (C) such creditor received payment of such debt to the extent provided by the provisions of this title.”

4 Section 544(b)(1) provides: “[T]he trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim....”

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KeyCite Yellow Flag
Distinguished by In re Roberts, Bankr.D.Colo., September 23, 2022

535 B.R. 845
United States Bankruptcy Appellate
Panel of the Tenth Circuit.

IN RE Frank Anthony ARENAS, doing business
as FA Husbandry LLC, doing business as
FSA LLC, doing business as Twenty Eighth
Larimer LLC, and Sarah Eve Arenas, Debtors.
Frank Anthony Arenas and
Sarah Eve Arenas, Appellants,
v.
United States Trustee, Appellee.

BAP No. CO–14–046
|
Bankr. No. 14–11406
|
Signed August 21, 2015

Synopsis

Background: United States Trustee (UST) moved to dismiss Chapter 7 case filed by Colorado marijuana grower and his wife, and debtors moved to convert case to one under Chapter 13. The United States Bankruptcy Court for the District of Colorado, Howard R. Tallman, J., 514 B.R. 887, ruled that "cause" existed to dismiss case based on trustee's inability to lawfully administer debtors' assets, and debtors could not convert case to one under Chapter 13. Debtors appealed.

Holdings: The Bankruptcy Appellate Panel, Nugent, J., held that:

[1] bankruptcy court did not abuse its discretion in denying debtors' motion to convert, and

[2] bankruptcy court did not abuse its discretion in dismissing debtors' case for cause.

Affirmed.

Procedural Posture(s): On Appeal; Motion to Dismiss.

West Headnotes (14)

[1] **Bankruptcy** Conclusions of law; de novo review

Bankruptcy Discretion

Bankruptcy court order granting or denying a motion to convert Chapter 7 case to one under Chapter 13 is reviewed for abuse of discretion, as is an order dismissing a Chapter 7 petition for cause, and if, in making those orders, the bankruptcy court makes conclusions of law, those are reviewable de novo, requiring an independent determination of the legal issues, giving no special weight to the bankruptcy court's decision. 11 U.S.C.A. §§ 707(a)(1), 1307(c).

4 Cases that cite this headnote

[2] **Bankruptcy** Clear error

Bankruptcy Appellate Panel (BAP) reviews bankruptcy court's findings of fact for clear error and disturbs them only when they lack factual support in the record or if BAP is left with the definite and firm conviction that a mistake has been made, focusing on whether the bankruptcy court acted within the bounds of permissible choice in reaching its decision and whether that decision was properly grounded in the law.

5 Cases that cite this headnote

[3] **Bankruptcy** Discretion

Under the abuse of discretion standard, a bankruptcy court's decision will not be disturbed unless the reviewing court has a definite and firm conviction that the lower court made a clear error of judgment or exceeded the bounds of permissible choice in the circumstances.

14 Cases that cite this headnote

[4] **Bankruptcy** Discretion

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Bankruptcy court abuses its discretion when it makes an arbitrary, capricious or whimsical, or manifestly unreasonable judgment.

6 Cases that cite this headnote

[5] **Bankruptcy** Grounds or cause in general; bad faith

Unreasonable delay by debtor that is prejudicial to creditors such as that brought about by inability to confirm a plan, may be cause for dismissal. 11 U.S.C.A. § 1307(c).

[6] **Bankruptcy** Discretion

Bankruptcy court's denial of debtors' motion to convert Chapter 7 case to one under Chapter 13 based on debtors' bad faith due to their inability to propose a confirmable Chapter 13 plan would be reviewed for an abuse of discretion. 11 U.S.C.A. §§ 706(a), 1307(c), 1325(a)(3).

8 Cases that cite this headnote

[7] **Bankruptcy** Particular cases and issues

Bankruptcy court's finding that debtors' conduct showed a lack of good faith would be reviewed for clear error. 11 U.S.C.A. § 1325(a)(3).

2 Cases that cite this headnote

[8] **Bankruptcy** Good faith in general

Courts evaluate a Chapter 13 debtor's good faith case by case, examining the totality of circumstances. 11 U.S.C.A. § 1325(a)(3).

1 Case that cites this headnote

[9] **Bankruptcy** Factors considered in determining presence of good faith

In determining whether Chapter 13 plan has been proposed in good faith, court considers whether debtor has stated his debts and expenses accurately, whether he has made any fraudulent misrepresentation to mislead the court, or whether he has unfairly manipulated the Bankruptcy Code. 11 U.S.C.A. § 1325(a)(3).

1 Case that cites this headnote

[10] **Bankruptcy** Conversion to debt adjustment

Bankruptcy court did not abuse its discretion in denying debtors' motion to convert Chapter 7 case to one under Chapter 13 based on debtors' bad faith due to their inability to propose a confirmable Chapter 13 plan; debtors lacked ability to deal with their reported monthly expenses of $7,000 and to fund plan without using proceeds of marijuana growing operation, and any plan proposed by debtors would require trustee to take possession, sell and distribute marijuana assets in violation of federal criminal law. 11 U.S.C.A. §§ 706(a), 1307(c), 1325(a)(3).

8 Cases that cite this headnote

[11] **Bankruptcy** Cause in general

Determining what amounts to "cause" for dismissal is within the court's discretion. 11 U.S.C.A. § 707(a).

2 Cases that cite this headnote

[12] **Bankruptcy** Cause in general

Factors that are often considered in determining "cause" for dismissal are as follows: the best interests of both debtor and creditors, trustee's consent or objection, potential to delay creditor payments, good or bad faith in seeking dismissal, and the possibility of payment priority becoming reordered outside of bankruptcy; emphasis is typically given to any prejudice that dismissal might cause the estate's creditors. 11 U.S.C.A. § 707(a).

2 Cases that cite this headnote

[13] **Bankruptcy** Bankruptcy

Bankruptcy relief is merely a privilege.

[14] **Bankruptcy** Cause in general

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Bankruptcy court did not abuse its discretion in dismissing Chapter 7 debtors' case "for cause" based on trustee's inability to lawfully administer marijuana assets included in property of the estate; selling the marijuana assets would require the trustee to violate federal law, and if the trustee abandoned the assets, debtors would retain their business after exposing the trustee to grave risk, provide the creditors with little or no recovery, and receive a discharge, protected all the while from their creditors' collection efforts by the automatic stay and then the discharge injunction, which would be the epitome of prejudicial delay. 11 U.S.C.A. §§ 706(a), 1325(a)(3).

8 Cases that cite this headnote

***846** Appeal from the United States Bankruptcy Court for the District of Colorado

Attorneys and Law Firms

Daniel J. Garfield of Foster Graham Milstein & Calisher LLP, Denver, Colorado, for Appellants.

***847** Noah M. Schottenstein, Trial Attorney, Executive Offices of the United States Trustee, Department of Justice (Ramona D. Elliott, Deputy Director/General Counsel and P. Matthew Sutko, Associate General Counsel, Executive Offices of the United States Trustee, Department of Justice, Washington, D.C.; Patrick S. Layng, United States Trustee for Region 19, Gregory Garvin, Assistant United States Trustee, and Alan K. Motes, Trial Attorney, United States Trustee, Department of Justice, Denver, Colorado with him on the brief), Washington, D.C., for Appellee.

Before CORNISH, NUGENT, and SOMERS, Bankruptcy Judges.

OPINION

NUGENT, Bankruptcy Judge.

Possessing, growing, and dispensing marijuana and assisting others to do that are federal offenses. But like several other states, Colorado has legalized these acts and heavily regulates them, triggering a flourishing marijuana industry there. Can a debtor in the marijuana business obtain relief in the federal bankruptcy court? No.

In the *Marrama* case, the United States Supreme Court held that a debtor who is involved in unlawful or deceitful conduct may not convert his Chapter 7 case to Chapter 13 because the conduct betrays a lack of good faith that would bar confirmation under 11 U.S.C. § 1325(a)(3).[1] Section 707(a)(1) allows a Chapter 7 case to be dismissed for cause, including unreasonable prejudicial delay to creditors. A debtor's conduct may demonstrate a lack of good faith that amounts to such cause.

Frank Arenas is licensed in Colorado to grow and dispense medical marijuana. He and Sarah Arenas leased a building to third parties who dispense medical marijuana from it. After litigation with the renters resulted in a state court judgment against them, the Arenases filed a Chapter 7 petition that they later attempted to convert to Chapter 13. The United States Trustee ("UST") objected to the conversion motion and instead asked that the case be dismissed. The bankruptcy court found that even though the debtors' conduct was legal under Colorado law, it violated the federal Controlled Substances Act, 21 U.S.C. § 801 et seq. (the "CSA"). For that reason, the bankruptcy court not only denied the debtors' motion to convert their Chapter 7 case to Chapter 13, but also concluded that the debtors could not receive Chapter 7 relief because engaging in federal criminal conduct demonstrated a lack of good faith that would bar confirmation of their Chapter 13 plan and was cause to dismiss their Chapter 7 case, too. We affirm.

I. Factual Background

The debtors jointly own a commercial building in Denver that consists of two units (the "Property"). Mr. Arenas grows and wholesales marijuana in one unit.[2] He and Sarah Arenas lease the other unit to Denver Patients Group, LLC ("DPG"), a marijuana dispensary. While Mr. Arenas' cultivation and sale of marijuana, and the debtors' leasing of space to a marijuana dispensary are lawful activities under Colorado state law, they violate the CSA.[3]

The debtors filed their Chapter 7 bankruptcy petition after they brought an eviction action against DPG in state court that resulted in a $40,000 attorney's fees award ***848** against them even before the state court addressed DPG's counterclaims against them for $120,000 in damages.

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Lacking the resources to pay the $40,000 judgment or defend the counterclaims, the debtors filed a Chapter 7 petition on February 12, 2014.[4] According to their schedules, Mrs. Arenas is disabled and receives monthly pension benefits and social security totaling $2,977.[5] The family's remaining monthly income of $4,265 stems from rental income and Mr. Arenas' marijuana business.[6] Their monthly expenses are approximately $7,235, making their monthly net income $7.[7] Their nonexempt assets are 25 marijuana plants (valued at $6,250)[8] and the Property[9] (collectively the "Assets").

After the meeting of creditors, the Chapter 7 trustee (the "Trustee") filed a Notice of No Distribution.[10] The Trustee subsequently withdrew the notice when DPG expressed an interest in purchasing the Property. The Trustee then sought guidance from the UST about whether he could administer the Property and whether Mr. Arenas' marijuana-related activities precluded the debtors from proceeding in Chapter 7.

The UST filed a motion to dismiss for cause under § 707(a). The UST alleged that it would be impossible for a Chapter 7 trustee to administer the Assets without violating federal law.[11] In response, the Arenases moved to convert their case to Chapter 13 and objected to the motion to dismiss. After an evidentiary hearing on both motions, the bankruptcy court issued a written order denying the debtors' motion to convert and granting the UST's motion to dismiss on August 28, 2014.[12] This appeal followed.

***849 II. Appellate Jurisdiction and Standard of Review**

This Court has jurisdiction to hear timely filed appeals from "final judgments, orders, and decrees" of bankruptcy courts within the Tenth Circuit, unless one of the parties elects to have the district court hear the appeal.[13] The Arenases timely filed their notice of appeal from the Appealed Order, and the parties have consented to this Court's jurisdiction by not electing to have this appeal heard by the United States District Court for the District of Colorado. We have jurisdiction of this appeal.

[1] [2] [3] [4] An order granting or denying a motion to convert under § 1307(c) is reviewed for abuse of discretion as is an order dismissing a Chapter 7 petition for cause under § 707(a)(1).[14] If in making those orders, the trial court makes conclusions of law, those are reviewable *de novo,* requiring an independent determination of the legal issues, giving no special weight to the bankruptcy court's decision.[15] We review findings of fact for clear error and disturb them only when they lack factual support in the record or if we are "left with the definite and firm conviction that a mistake has been made."[16] We focus on whether the bankruptcy court acted within the bounds of permissible choice in reaching its decision and whether that decision was properly grounded in the law. "Under the abuse of discretion standard: 'a trial court's decision will not be disturbed unless the appellate court has a definite and firm conviction that the lower court made a clear error of judgment or exceeded the bounds of permissible choice in the circumstances.' "[17] A trial court abuses its discretion when it makes an "arbitrary, capricious or whimsical," or "manifestly unreasonable judgment."[18]

III. Analysis

The pivotal issue here is whether engaging in the marijuana trade, which is legal under Colorado law but a crime under federal law, amounts to "cause" including a "lack of good faith" that effectively disqualifies these otherwise eligible debtors from bankruptcy relief. We agree with the bankruptcy court that while the debtors have not engaged in intrinsically evil conduct, the debtors cannot obtain bankruptcy ***850** relief because their marijuana business activities are federal crimes.

A. No abuse of discretion to deny motion to convert to Chapter 13, §§ 706, 1307, and 1325.

While a Chapter 7 debtor may convert his case to Chapter 13 "at any time," § 706 requires that the debtor not have previously converted the case to Chapter 7 and that the debtor be eligible for Chapter 13 relief. Section 706 provides in part:

> (a) The debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time, if the case has not been converted under section 1112, 1208, or 1307 of this title....
>
> ....
>
> (d) Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter.[19]

Because the Arenases originally filed their case in Chapter 7, only the subsection (d) eligibility prong applies. Section

109(e) provides that only individuals with regular income may be Chapter 13 debtors.[20] Many courts consider a debtor's good faith to be a condition of Chapter 13 eligibility.[21]

In *Marrama v. Citizens Bank of Mass.*, the United States Supreme Court held that a Chapter 7 debtor who had made pre-petition false statements and concealed assets from the trustee could not exercise his right to convert his case to Chapter 13 "at any time" because his pre- and post-petition lack of good faith rendered him ineligible for Chapter 13 relief.[22] Because of the debtor's lack of good faith, the court could dismiss his potential Chapter 13 case for cause under § 1307(c). In addition, the debtor's bad conduct prevented confirmation of any plan because good faith is an affirmative confirmation requirement under § 1325(a)(3). The Supreme Court equated "a ruling that an individual's Chapter 13 case should be dismissed or converted to Chapter 7 because of prepetition bad faith" with a "ruling that the individual does not qualify as a Chapter 13 debtor."[23]

[5] The bankruptcy court may dismiss a Chapter 13 case for cause. Section 1307(c) defines "cause" with a nonexclusive list of eleven examples.[24] One nonenumerated cause and one enumerated cause are important in this case. First, this Court has previously held that a debtor's lack of good faith —although not explicitly included in § 1307(c)—amounts to cause for dismissal under § 1307.[25] Second, "unreasonable ***851** delay by the debtor that is prejudicial to creditors,"[26] such as that brought about by inability to confirm a plan, may be cause for dismissal.[27] Had the debtors filed their original case as a Chapter 13, it would have been susceptible to dismissal for either reason.

[6] The bankruptcy court denied the Arenases' motion to convert their Chapter 7 case to Chapter 13 because it concluded that "their reorganization would be funded from profits of an ongoing criminal activity under federal law and would necessarily involve the Chapter 13 Trustee in administering and distributing funds derived from the Debtors' violation of the CSA."[28] Because "[a]ny plan proposed by the Debtors would necessarily be executed by unlawful means ... [the court was] unable to find, under § 1325(a)(3), that their plan [was] 'proposed in good faith *and not by any means forbidden by law*.' "[29] That was "cause for dismissal [under] § 1307(c) on account of the Debtors' bad faith due to their inability to propose a confirmable Chapter 13 plan."[30] On appeal, that conclusion is entitled to the most deferential standard of review, whether denial of the conversion motion was an abuse of discretion.[31]

[7] **[8]** **[9]** We review the bankruptcy court's finding that the debtors' conduct showed a lack of good faith for clear error.[32] Courts evaluate a debtor's good faith case by case, examining the totality of circumstances.[33] Courts in the Tenth Circuit look to the eleven factors set forth in *Flygare v. Boulden.*[34] Courts should also consider "whether the debtor has stated his debts and expenses accurately; ***852** whether he has made any fraudulent misrepresentation to mislead the bankruptcy court; or whether he has unfairly manipulated the Bankruptcy Code."[35]

Only a few of the eleven *Flygare* factors are in play here. They include (1) the debtor's employment history, ability to earn and likelihood of future increases in income; (2) the burden the plan's administration would place on the trustee; and (3) the debtor's motivation and sincerity in seeking Chapter 13 relief.[36]

[10] The debtors contend that when the bankruptcy court held that they could not propose a Chapter 13 plan in good faith, it erred by adopting a per se rule that debtors who are engaged in the marijuana business are not eligible for bankruptcy relief.[37] This oversimplifies the court's reasoning. The bankruptcy court applied the *Flygare* factors and concluded that the debtors couldn't propose a feasible plan. First, the Arenases' monthly income from sources other than marijuana was not enough to fund their plan. Even the debtors agree that the only way they can fund a plan is with the rental income from the marijuana dispensary. Without the rental income, their monthly expenses of $7,000 exceed their non-marijuana income by $4,000 a month. Even with the rental income, the plan is barely feasible because their Schedule I reflects a surplus of less than $8 a month, yielding at best, a nominal dividend.[38] Sarah Arenas is disabled and unable to work. That, combined with Frank Arenas' age and employment history, amply supports a finding that the debtors' income is unlikely to increase during the plan term. The court considered the debtors' "ability to earn and likelihood of future increases in income" and concluded that their plan is not likely confirmable because it is not feasible.[39]

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Second, short of exposing him to physical harm, nothing could be more burdensome to the Trustee's administration than requiring him to take possession, sell and distribute marijuana Assets in violation of federal criminal law. There is no way the Trustee could administer the plan without committing one or more federal crimes. [40]

Finally, as for the debtors' "motivation and sincerity," the bankruptcy court found the debtors to be sincere and credible and took pains to emphasize that their motives in seeking bankruptcy relief were not improper. [41] That said, the court also recognized that lack of good faith carries an objective rather than a subjective meaning. If the debtors are incapable of proposing a confirmable plan, it is objectively unreasonable for them to seek Chapter 13 relief ***853** whether their intentions are kindly or not. We concur in this view.

Plenty of evidence supports the bankruptcy court's finding of lack of good faith. We affirm that finding and need not address whether the debtors' plan was "proposed by any means forbidden by law." Instead, we turn to the fate of the Arenases' Chapter 7 petition.

B. No abuse of discretion to dismiss debtors' Chapter 7 case, § 707(a)(1).

[11] **[12]** **[13]** After it concluded that the debtors could not convert their case to Chapter 13, the bankruptcy court granted the UST's motion to dismiss their Chapter 7 case for "cause" under § 707(a). Section 707(a) provides "[t]he court may dismiss a case under this chapter only after notice and a hearing and only for cause, including—(1) unreasonable delay by the debtor that is prejudicial to creditors." "Cause" is not defined in the Code. Determining what amounts to cause for dismissal under § 707(a) is within the court's discretion. [42] As we have previously held:

> Dismissal factors that are often considered are: the best interests of both debtor and creditors; trustee's consent or objection; potential to delay creditor payments; good or bad faith in seeking dismissal; and the possibility of payment priority becoming reordered outside of bankruptcy. Emphasis is typically given to any prejudice that dismissal might cause the estate's creditors. [43]

The Supreme Court has held that "[t]here is no constitutional right to obtain a discharge of one's debts in bankruptcy." [44] Bankruptcy relief is merely a privilege. [45]

The bankruptcy court concluded that it would be impossible for the Chapter 7 Trustee to administer the Arenases' estate because selling and distributing the proceeds of the marijuana assets would constitute federal offenses. Because of that, the creditors had no expectation of receiving any dividend while the debtors would receive a discharge. Meanwhile, the creditors are stayed from enforcing their state law rights. The impossibility of lawfully administering the estate constituted cause for dismissal under § 707(a). [46] The debtors argue here that the Trustee could have abandoned the marijuana assets. They say that § 707(a) "cause" should be limited to circumstances where the debtor's actions have frustrated the administration of the estate or a bankruptcy purpose and that they have not engaged in such conduct. [47]

[14] In fact, the debtors have violated federal law and apparently intend to continue to do so. [48] Selling the plants and the building would require the Trustee to violate federal law. If the Trustee abandoned the Assets, the debtors would retain their business after exposing the Trustee to grave risk, provide the creditors with little or no recovery, and receive a discharge, protected all the while from their creditors' collection efforts by the automatic stay and then the discharge injunction. ***854** That is the epitome of prejudicial delay. The bankruptcy court did not abuse its discretion by dismissing the debtor's Chapter 7 case. [49]

As for the debtors' claim that the bankruptcy court should have required the Trustee to abandon the marijuana assets if he couldn't administer them, they never raised that in the bankruptcy court. [50] It is not clear that a bankruptcy court may order a trustee to abandon assets *sua sponte*. [51] And even if the court can do that, this bankruptcy estate, shorn of its marijuana assets, would likely yield no dividend to the creditors. The debtors would get a discharge and get to keep (via abandonment) their marijuana assets while being

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protected from collection activities. This also strikes us as prejudicial delay that amounts to cause for dismissal.

IV. Conclusion

In this case, the debtors are unfortunately caught between pursuing a business that the people of Colorado have declared to be legal and beneficial, but which the laws of the United States—laws that every United States Judge swears to uphold–proscribe and subject to criminal sanction. Because of that, neither a Chapter 7 nor 13 trustee can administer the most valuable assets in this estate. Without those assets or the marijuana based income stream, the debtors cannot fund a plan without breaking the law, and are therefore ineligible for relief under Chapter 13. In reaching that conclusion, the bankruptcy court stayed well within the bounds of permissible choice and in no way abused its discretion in denying the debtors' motion to convert.

Administering the debtors' Chapter 7 estate would require the Trustee to either violate federal law by possessing and selling the marijuana assets or abandon them. If he did the former, the Trustee would be at risk of prosecution; if he did the latter, the creditors would receive nothing while the debtors would retain all of their assets and receive a discharge as well. Either amounts to prejudicial delay that is sufficient to demonstrate cause to dismiss their Chapter 7 case under § 707(a). The bankruptcy court did not abuse its discretion in granting the UST's motion to dismiss. Accordingly, we AFFIRM the bankruptcy court's order.

All Citations

535 B.R. 845, 74 Collier Bankr.Cas.2d 171, Bankr. L. Rep. P 82,870

Footnotes

1 All future references to “Code,” “Section,” and “§” are to the Bankruptcy Code, Title 11 of the United States Code, unless otherwise indicated.

2 There is no evidence that Mrs. Arenas participates in the growing business. Mr. Arenas possesses all of the required licenses and permits necessary to legally engage in his business under Colorado law.

3 21 U.S.C. § 856(a) makes it unlawful to—

> (1) knowingly open, lease, rent, use, or maintain any place, whether permanently or temporarily, for the purpose of manufacturing, distributing, or using any controlled substance;
>
> (2) manage or control any place, whether permanently or temporarily, either as an owner, lessee, agent, employee, occupant, or mortgagee, and knowingly and intentionally rent, lease, profit from, or make available for use, with or without compensation, the place for the purpose of unlawfully manufacturing, storing, distributing, or using a controlled substance.

21 U.S.C. § 841(a)(1) makes it unlawful for any person knowingly or intentionally to manufacture, distribute, or dispense, or possess with intent to manufacture, distribute, or dispense, a controlled substance.

4 Voluntary Petition, *in* Appellants' Appendix (“App.”) at 17–20.

5 Schedule I at 2, *in* App. at 40; Statement of Financial Affairs, *in* App. at 46.

6 Schedule I at 2, *in* App. at 40.

7 Schedule J at 3, *in* App. at 43.

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8 Arenas Dep. 20:9–13, June 19, 2014, *in* App. at 341. The plants were not listed in the debtors' Schedule B.

9 The value of the Property is unclear. Although the debtors' schedules indicate that the Property was heavily encumbered, some evidence indicated that the Property had value to the estate. *See* Schedule A, *in* App. at 25 (debtors listed the Property's value at $262,725 with secured claims against it of $295,957.51); Schedule D, *in* App. at 30 (same); Statement of Financial Affairs, *in* App. at 46 (Property generated rental income of $52,920 in 2012 and $41,008 in 2013); United States Trustee's Motion to Dismiss Debtors' Case Under 11 U.S.C. § 707(a) (the "Motion to Dismiss") ¶ 7, at 2, *in* App. at 71 ("[T]he Trustee has received preliminary communications concerning a potential purchase of the building by [DPG] ... "). The bankruptcy court did not determine either the value of the Property or whether the debtors had any equity in the Property.

10 *See* Bankruptcy Dkt. Entry No. 16, *in* App. at 4. The Notice of No Distribution effectively abandons all nonadministered assets and closes the case.

11 Motion to Dismiss, *in* App. at 70–73. *See In re Rent–Rite Super Kegs West Ltd.,* 484 B.R. 799 (Bankr.D.Colo.2012).

12 Order on the United States Trustee's Motion to Dismiss and the Debtors' Motion to Convert (the "Appealed Order"), *in* App. at 229–37.

13 28 U.S.C. § 158(a)(1), (b)(1), and (c)(1); Fed. R. Bankr.P. 8001(e) (*now at* Fed. R. Bankr.P. 8005, effective Dec. 1, 2014); 10th Cir. BAP L.R. 8001–3 (*now at* 10th Cir. BAP L.R. 8005–1, effective Dec. 1, 2014).

14 *Marrama v. Citizens Bank of Mass.,* 549 U.S. 365, 375, 127 S.Ct. 1105, 166 L.Ed.2d 956 (2007) (bankruptcy court has authority to immediately deny a motion to convert a Chapter 7 case to a Chapter 13 in lieu of a conversion order that postpones the allowance of equivalent relief and may provide a debtor with an opportunity to take action prejudicial to creditors); S. REP. NO. 95–989, at 94 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5880 ("The decision whether to convert is left in the sound discretion of the court, based on what will most inure to the benefit of all parties in interest."); *In re Isho,* Nos. UT–12–090, 11–30284, 2013 WL 1386208, *3 (10th Cir. BAP April 5, 2013) (determination of cause for dismissal pursuant to § 707(a) is within the discretion of the bankruptcy court).

15 *Salve Regina Coll. v. Russell,* 499 U.S. 225, 238, 111 S.Ct. 1217, 113 L.Ed.2d 190 (1991).

16 *Las Vegas Ice & Cold Storage Co. v. Far W. Bank,* 893 F.2d 1182, 1185 (10th Cir.1990) (quoting *LeMaire ex rel. LeMaire v. United States,* 826 F.2d 949, 953 (10th Cir.1987)).

17 *Moothart v. Bell,* 21 F.3d 1499, 1504 (10th Cir.1994) (quoting *McEwen v. City of Norman,* 926 F.2d 1539, 1553–54 (10th Cir.1991)).

18 *Id.* at 1504–05 (internal quotation marks omitted).

19 11 U.S.C. §§ 706(a) and (d).

20 Section 101(30) defines "individual with regular income" as "[an] individual whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13 of this title, other than a stockbroker or a commodity broker." The regular income requirement anticipates that the income is

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sufficient to fund the debtor's living expenses and the plan payments. The debt limitation is not an issue in this appeal.

21 Keith M. Lundin & William H. Brown, Chapter 13 Bankruptcy, 4th Edition, § 5.1 at ¶ 5, Sec. Rev. Apr. 19, 2011, www.Ch13**o**nline.com. ("Although not mentioned in the Code as a condition for eligibility for Chapter 13, many reported decisions have considered a debtor's 'good faith' at the threshold of a Chapter 13 case, typically in the context of a motion to dismiss.").

22 549 U.S. 365, 127 S.Ct. 1105, 166 L.Ed.2d 956 (2007).

23 *Marrama,* 549 U.S. at 375, 127 S.Ct. 1105.

24 11 U.S.C. § 1307(c)(1)-(11).

25 *In re Armstrong,* 303 B.R. 213, 218 (10th Cir. BAP 2004) (egregious prepetition conduct and other actions constituted bad faith, warranting dismissal of Chapter 13); *In re Davis,* 239 B.R. 573, 578–79 (10th Cir. BAP 1999) (cause for dismissal of Chapter 13 existed based on debtor's lack of good faith in filing bankruptcy, inability to propose a feasible amendment to unconfirmable plan, debtor's lack of good faith in filing plan, and debtor's ineligibility for Chapter 7 based on a prior discharge) (citing *In re Love,* 957 F.2d 1350, 1354 (7th Cir.1992)).

26 11 U.S.C. § 1307(c)(1).

27 *In re Paulson,* 477 B.R. 740, 745–46 (8th Cir. BAP 2012) (cause for dismissal under § 1307 due to unreasonable delay stemming from the debtor's inability to get a plan confirmed); *In re Merhi,* 518 B.R. 705, 719–20 (Bankr.E.D.N.Y.2014) (continuation of case when debtor cannot propose a confirmable debt adjustment plan constituted prejudicial delay to creditors under 11 U.S.C. § 1307(c)(1)); *In re Yarborough,* Case No. 12–30549, 2012 WL 4434053, *2 (Bankr.E.D.Tenn. Sept. 24, 2012) ("The right to convert [from chapter 7] to Chapter 13, however, is not absolute, and conversion may be denied where 'cause' would exist to convert or dismiss the debtor's Chapter 13 case under 11 U.S.C. § 1307(c), including inability to propose a confirmable plan and bad faith.") (footnote and citations omitted). *See also* *In re Ames,* 973 F.2d 849, 851–52 (10th Cir.1992) (Chapter 12 bankruptcy may be dismissed due to failure to propose a confirmable plan).

28 Appealed Order at 5–6, *in* App. at 233–34.

29 *Id.* at 6–7, *in* App. at 234–35.

30 *Id.* at 6, *in* App. at 234.

31 *Marrama,* 549 U.S. at 375, 127 S.Ct. 1105 (bankruptcy court has authority to immediately deny a motion to convert a Chapter 7 case to a Chapter 13 in lieu of a conversion order that postpones the allowance of equivalent relief and may provide a debtor with an opportunity to take action prejudicial to creditors); S. REP. NO. 95–989, at 94 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5880 ("The decision whether to convert is left in the sound discretion of the court, based on what will most inure to the benefit of all parties in interest.").

32 *In re Davis,* 239 B.R. 573, 576 (10th Cir. BAP 1999) ("Whether a Chapter 13 plan has been proposed in good faith is a question of fact subject to the clearly erroneous standard of review.").

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33 *Id.* at 577.

34 709 F.2d 1344 (10th Cir.1983).

35 *In re Cranmer,* 697 F.3d 1314, 1319 n.5 (10th Cir.2012).

36 *Id.* at 1347–48.

37 Appellants' Opening Brief at 9, 29–30.

38 We recognize that nominal repayments alone do not violate the good-faith standard of § 1325(a)(3). Other factors, however, weigh against a good-faith finding.

39 The debtors' suggestion that the United States Government's decision not to prosecute Colorado participants in the marijuana business somehow addresses the feasibility and good-faith question fails to account for the possibility that subsequent Administrations and Attorneys General could exercise their prosecutorial discretion to take a different approach. As long as marijuana remains a controlled substance, a matter left entirely to Congress, people who engage in the Colorado marijuana trade remain at risk of federal criminal prosecution, regardless of the Department of Justice's current posture.

40 The CSA criminalizes virtually every aspect of selling, manufacturing, distributing and profiting from the use of controlled substances. *See* 21 U.S.C. §§ 841(a)(1) and 856(a).

41 Appealed Order at 6, n.8, *in* App. at 234.

42 *In re Isho,* Nos. UT–12–090, 11–30284, 2013 WL 1386208, at *3 (10th Cir. BAP April 5, 2013).

43 *Id.* (citations omitted).

44 *United States v. Kras,* 409 U.S. 434, 446, 93 S.Ct. 631, 34 L.Ed.2d 626 (1973).

45 *In re Michael,* 285 B.R. 553, 556 (Bankr.S.D.Ga.2002) (citing *In re Sochia,* 231 B.R. 158, 160 (Bankr.W.D.N.Y.1999); *In re Khan,* 35 B.R. 718, 719 (Bankr.W.D.Ky.1984)).

46 Appealed Order at 5, *in* App. at 233.

47 Appellants' Opening Brief at 23.

48 July 30, 2014 Hrg Tr. at 18, *in* App. at 198.

49 *In re Medpoint Mgmt.,* LLC, 528 B.R. 178, 184–86 (Bankr.D.Ariz.2015) (finding reasoning in *Arenas* and *Rent Rite* persuasive; dual risks of forfeiture of assets and a trustee's inevitable violation of CSA constitute cause to dismiss involuntary petition under § 707(a)).

50 *Walker v. Mather (In re Walker),* 959 F.2d 894, 896 (10th Cir.1992) (appellate court will not consider issues not raised below); *Pritner v. COFCO Credit Co., LLC (In re Pritner),* Nos. WO–040–080, 99–16898–BH, 03–1371–BH, 2005 WL 705363, at *5 (10th Cir. BAP 2005) (refusing to consider argument not raised below).

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51 Section 554(b) states: "(b) *On request of a party in interest and after notice* and a hearing, the court may order the trustee to abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate." 11 U.S.C. § 554(b) (emphasis added).

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KeyCite Yellow Flag
Distinguished by In re Callaway, Bankr.N.D.Cal., June 26, 2024

647 B.R. 748
United States Bankruptcy Court, C.D. California.

IN RE: The HACIENDA COMPANY, LLC, Debtor.

Case No.: 2:22-bk-15163-NB
|
Signed January 20, 2023

Synopsis
Background: United States Trustee (UST) filed motion to dismiss Chapter 11 case of debtor that, prepetition, manufactured and packaged cannabis products before ceasing operations and transferring its value to Canadian company and selling vacant land that debtor had intended for use as cannabis cultivation center.

Holdings: The Bankruptcy Court, Neil W. Bason, J., held that:

[1] fact that UST filed notice of appeal did not divest Bankruptcy Court of jurisdiction to issue opinion following denial of UST's motion to dismiss;

[2] UST failed to establish "cause" to dismiss case based on any violations of Controlled Substances Act (CSA); and

[3] unusual circumstances precluded dismissal under Bankruptcy Code's "for cause" provision.

Motion denied.

Procedural Posture(s): Motion to Convert or Dismiss Case.

West Headnotes (15)

[1] Bankruptcy Effect of Transfer

Fact that United States Trustee (UST) filed notice of appeal did not divest Bankruptcy Court of jurisdiction to issue opinion following denial of UST's motion to dismiss Chapter 11 case of debtor that, prepetition, manufactured and packaged cannabis products before ceasing operations and transferring its value to Canadian company, because no appellate court had yet granted the UST's motion for leave to appeal, and Bankruptcy Court's opinion did not alter or expand any prior rulings, but rather, merely provided further explanation, as anticipated on the record at hearing on dismissal motion.

[2] Bankruptcy Proceedings

Burden of establishing "cause" for dismissal of Chapter 11 case rests with party seeking dismissal. 11 U.S.C.A. § 1112(b)(1).

[3] Bankruptcy Proceedings

Movant must show "cause" for dismissal of Chapter 11 case by preponderance of evidence. 11 U.S.C.A. § 1112(b)(1).

[4] Bankruptcy Proceedings

If party moving to dismiss or convert a Chapter 11 case under Bankruptcy Code's "for cause" provision demonstrates the requisite "cause," burden shifts to debtor to make the statutorily required four-part showing for an "unusual circumstances" defense. 11 U.S.C.A. § 1112(b)(2).

[5] Bankruptcy In General; Grounds in General

If debtor cannot satisfy "unusual circumstances" defense to dismissal or conversion of Chapter 11 case under Bankruptcy Code's "for cause" provision, then the bankruptcy court must choose between conversion or dismissal based on the best interests of the creditors and the estate. 11 U.S.C.A. § 1112(b).

1 Case that cites this headnote

[6] Bankruptcy Dismissal or suspension

Violations of nonbankruptcy law can be "cause" for dismissal of Chapter 11 case; that said, there

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are many remedies for debtor's violations of law, rule, or procedure, and dismissal is one of the more extreme remedies. 11 U.S.C.A. § 1112(b)(1).

[7] **Bankruptcy** Dismissal or suspension

Violations of nonbankruptcy law might establish "cause" for dismissal for Chapter 11 case because such violations might establish a lack of good faith. 11 U.S.C.A. § 1112(b)(1).

2 Cases that cite this headnote

[8] **Bankruptcy** Dismissal or suspension

Violations of nonbankruptcy law might constitute "gross mismanagement" of Chapter 11 estate, within meaning of "for cause" dismissal provision of Bankruptcy Code, because violations of nonbankruptcy law might expose the estate to financial losses and criminal sanctions, and violating the law might constitute "mismanagement" per se. 11 U.S.C.A. § 1112(b)(4)(B).

[9] **Bankruptcy** Dismissal or suspension

Violations of nonbankruptcy law might warrant dismissal under general principles applicable to a bankruptcy court as a court of equity, pursuant to bankruptcy judges' oath of office to uphold the law, or on other theories.

[10] **Bankruptcy** Dismissal or suspension

Ongoing postpetition violations of nonbankruptcy law are far more problematic than prepetition violations, in deciding whether to dismiss Chapter 11 case.

[11] **Bankruptcy** Dismissal or suspension

United States Trustee (UST) failed to establish "cause" to dismiss Chapter 11 case of debtor that, prepetition, manufactured and packaged cannabis products before ceasing operations and transferring its value to Canadian company and selling vacant land that debtor had intended for use as cannabis cultivation center, based on any violations of Controlled Substances Act (CSA); UST did not demonstrate any ongoing violation of the CSA by debtor, as distinguished from any prepetition violations, either by any connection to distributing cannabis or by stock ownership in a cannabis-related enterprise, nor did the UST demonstrate that if the case were converted to Chapter 7 liquidation, any trustee would have to engage in violation of CSA. 11 U.S.C.A. § 1112(b)(1); Comprehensive Drug Abuse Prevention and Control Act of 1970 § 101, 21 U.S.C.A. § 801 et seq.

[12] **Bankruptcy** Sale or Assignment of Property

Orderly liquidation in bankruptcy typically maximizes the value of debtor's assets; bankruptcy can preserve going concern value, or can authorize a sale of assets free and clear of liens and other interests, thereby obtaining higher bids than outside of bankruptcy. 11 U.S.C.A. §§ 363(f), 1129(b)(2)(A)(ii).

[13] **Bankruptcy** Discretion

Bankruptcy Code's mandate that court "shall" dismiss or convert bankruptcy case for "cause" does not mean that any violation of criminal law requires dismissal, but rather, court has discretion to determine whether dismissal is warranted based on all the facts and circumstances. 11 U.S.C.A. § 1112(b)(1).

2 Cases that cite this headnote

[14] **Bankruptcy** Dismissal or suspension

Unusual circumstances precluded dismissal under Bankruptcy Code's "for cause" provision in Chapter 11 case of debtor that, prepetition, manufactured and packaged cannabis products before ceasing operations and transferring its value to Canadian company and selling vacant land that debtor had intended for use as cannabis cultivation center; debtor had divested itself,

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prepetition, of any direct involvement in the cannabis business, and any dismissal would undermine a very realistic possibility of a substantial payment to creditors, as the only thing for debtor to do was to sell its stock in the Canadian company, which appeared to be legal and feasible under Canadian law, and then to use the proceeds to pay creditors, or alternatively to distribute the stock to creditors. 11 U.S.C.A. § 1112(b)(2).

[15] Bankruptcy Frivolity or bad faith; sanctions

In general, bankruptcy court should defer to prosecutors to use their discretion about whether and how to address any violations of nonbankruptcy law.

Attorneys and Law Firms

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David L. Neale, Juliet Y. Oh, Lindsey L. Smith, Levene, Neale, Bender, Yoo & Golubchik L.L.P., Los Angeles, CA, for Debtor.

OPINION ON MOTION TO DISMISS CANNABIS-RELATED CASE

Neil W. Bason, United States Bankruptcy Judge

This Bankruptcy Court has already issued an order (docket no. 71) denying the motion of the United States Trustee's ("UST") to dismiss this case (docket no. 53, the "MTD"). This Opinion memorializes and further explains this Court's reasoning. [1]

1. BACKGROUND

The above-captioned Debtor was in the business of wholesale manufacturing and packaging cannabis products under the "Lowell Herb Co." brand, a/k/a "Lowell Farms," and it ceased operations on February 25, 2021. At one time, Debtor owned land that was intended for use as a cannabis cultivation center, but Debtor did not achieve this goal and the vacant land was sold in 2020 to pay creditors.

After Debtor ceased operations, it transferred its value to a publicly traded Canadian company – allegedly by structuring the sale as one of intellectual property, not the sale of an operating cannabis business. The acquirer's sole business is cannabis growth and sales, which apparently are legal under Canadian law. In return, Debtor received a roughly 9.4% share of the equity shares of the acquiring entity. The acquiring entity changed its name to Lowell Farms, Inc.

On September 21, 2022, Debtor filed this bankruptcy case. In Debtor's initial status report, Debtor stated that it intended "to propose a plan of reorganization that provides for Debtor to sell off the shares of [Lowell Farms, Inc. that] it owns in an orderly fashion and use the proceeds from the stock to pay creditors [or] ... Debtor may elect to distribute the shares it owns to its creditors directly." At oral argument, Debtor's counsel elaborated that the stock of Lowell Farms, Inc. is thinly traded and therefore, to avoid flooding the market and depressing the return to creditors, "we're talking about selling it off in chunks [over time] ...." Tr. 12/20/23 (docket no. 76), p. 16:19.

2. JURISDICTION, AUTHORITY AND VENUE

[1] This Bankruptcy Court has jurisdiction to decide the MTD, and venue is proper, under 28 U.S.C. §§ 1334 and 1408. This is a "core" proceeding in which this Bankruptcy Court has the authority to enter a final judgment or order under 28 U.S.C. § 157(b)(2)(A) and (O). *See also* *Stern v. Marshall*, 564 U.S. 462, 131 S. Ct. 2594, 180 L.Ed.2d 475 (2011). [2]

*751 3. DISCUSSION

a. Legal standards

[2] **[3]** As the parties acknowledge, the burden of establishing "cause" for dismissal under § 1112(b) rests with the party seeking dismissal. *See In re Rosenblum*, 608 B.R. 529, 536 (Bankr. D. Nev. 2019). The movant must show such cause by "a preponderance of the evidence." *In re Woodbrook Assocs.*, 19 F.3d 312, 317 (7th Cir. 1994).

[4] If the movant establishes that "cause" exists under § 1112(b)(1), then the opponent can still prevent conversion or dismissal under § 1112(b)(2) if (1) the court "finds and

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specifically identifies unusual circumstances establishing" that conversion or dismissal is "not in the best interests of creditors"; (2) the opponent shows that "there is a reasonable likelihood" of confirming a plan in a reasonable amount of time; (3) the opponent establishes that the grounds for conversion or dismissal include an act or omission of the debtor for which there is a "reasonable justification"; and (4) the opponent establishes that the act or omission can be "cured within a reasonable time." *See Rosenblum*, 608 B.R. at 536-37 (summarizing § 1112(b)(2)).

[5] If the debtor cannot satisfy the "unusual circumstances" elements under § 1112(b)(2), then the bankruptcy court must choose "between conversion or dismissal based on the best interests of the creditors and the estate." *In re Nelson*, 343 B.R. 671, 675 (9th Cir. BAP 2006) (citation and internal quotation marks omitted).

b. Violations of nonbankruptcy law, generally

[6] A violation of nonbankruptcy law is not expressly listed as "cause" for dismissal under § 1112(b)(1) & (4), but compliance with applicable nonbankruptcy law generally is required both by statute (*e.g.,* 28 U.S.C. § 959) and under the authorities cited by both parties, so it appears to be undisputed that violations of nonbankruptcy law *can* be cause for dismissal. That said, there are many remedies for any debtor's violations of any law, rule, or procedure, and dismissal is one of the more extreme remedies.

[7] There are several alternative reasons why violations of nonbankruptcy law might establish cause for dismissal. First, such violations might establish a lack of "good faith" sufficient to warrant dismissal. *See, e.g., In re Arenas*, 535 B.R. 845 (10th Cir. BAP 2015) (debtors' marijuana business, while legal under state law, was illegal under federal law, and thus the debtors could not propose a confirmable plan in good faith). *See generally In re Leavitt,* 171 F.3d 1219, 1224 (9th Cir. 1999) ("cause" for dismissal not defined by the Code, but can include "bad faith"/lack of "good faith"); *Rosenblum,* 608 B.R. at 537 (listing common considerations in assessing good faith).

[8] Second, violations of nonbankruptcy law might constitute "gross mismanagement" ***752** of the estate, within the meaning of § 1112(b)(4)(B), because violations of nonbankruptcy law might expose the estate to financial losses and criminal sanctions, and violating the law might constitute "mismanagement" *per se*. *See, e.g., In re Rent-Rite Super Kegs West Ltd.,* 484 B.R. 799, 809 (Bankr. D. Colo. 2012) (Debtor's decision to continue leasing warehouse space to tenants engaged in the business of growing marijuana exposed Debtor to criminal liability and the risk of forfeiture which amounted to gross mismanagement).

[9] In addition, violations of nonbankruptcy law might warrant dismissal under general principles applicable to a bankruptcy court as a court of equity, pursuant to bankruptcy judges' oath of office to uphold the law, or on other theories. *See, e.g., In re Johnson*, 532 B.R. 53, 56-58 (Bankr. W.D. Mich. 2015) (suggesting that authorizing debtor to continue generating income from marijuana operations appears inconsistent with judicial oath to uphold the law, but concluding that Debtor could remain in bankruptcy and avoid dismissal of his case if he ceased marijuana operations). *See also* MTD (docket no. 53) pp. 8:18-17:11; Opp. (docket no. 59) pp. 3:6-19:26; *and* Reply (docket no. 63) pp. 7:22-11:14 (discussing authorities).

[10] But the authorities cited by the parties also appear to reflect some degree of discretion. Ongoing postpetition violations are far more problematic than prepetition violations; and although indirect connections with illegal activity might violate nonbankruptcy law, the degree of connection appears to be important to deciding whether to dismiss the case. *See e.g., In re Burton*, 610 B.R. 633, 637-638 (9th Cir. BAP 2020) (affirming dismissal as within bankruptcy court's discretion, but holding that "the mere presence of marijuana near a bankruptcy case does not automatically prohibit a debtor from bankruptcy relief," so a "bankruptcy court must be explicit in articulating its legal and factual bases for dismissal in cases involving marijuana") (citations omitted); *and see also Garvin v. Cook Investments NW, SPNWY, LLC,* 922 F.3d 1031, 1036 (9th Cir. 2019) (bankruptcy judge is not an "ombudsman without portfolio, gratuitously seeking out 'illegalities' ..., a result that would be "inimical to the basic function of bankruptcy judges ...") (footnote, citations, and internal quotation marks omitted).

c. The Controlled Substances Act, 21 U.S.C. § 801 et seq. (the "CSA")

[11] The UST has not established any ongoing violation of the CSA by Debtor, as distinguished from any prepetition violations, either (i) by any connection to distributing

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cannabis or (ii) by stock ownership in a cannabis-related enterprise. Nor has the UST established that, if a chapter 11 trustee were appointed or if this case were to be converted to a chapter 7 liquidation, any trustee would have to engage in a violation of the CSA.

i. No ongoing distribution of cannabis

True, the CSA covers conspiracies with intent to distribute cannabis, and one way to characterize the facts might be that Debtor is effectively conspiring to continue carrying on its California-based cannabis business indirectly, through its ownership interest in a Canadian company operating under Debtor's former name. *See* 21 U.S.C. §§ 846 (conspiracy) *and* 856(a) (illegal to "control any place" or "profit from" a place used to manufacture, store, distribute, or use cannabis), *and* MTD p. 8:1-8. Alternatively, even if (as this Bankruptcy Court finds and concludes) Debtor is *not* effectively carrying on its prepetition cannabis business indirectly, Debtor did structure its own liquidation in a manner designed ***753** to maximize the value derived from its connection with cannabis, which might be characterized as an indirect way to "profit from" the cannabis business.

On the other hand, this interpretation of section 856(a) of the CSA goes too far. Debtor's passive ownership of stock, with intent to liquidate that stock to pay creditors, will *terminate* any connection with cannabis. This appears to be the opposite of an intent to profit from an ongoing scheme to distribute cannabis, at least if Debtor does not maintain its investment in Lowell Farms, Inc. for too long a period of time (which is an issue that can be addressed in connection with confirmation of any chapter 11 plan). Therefore, the UST has not established a violation of section 856(a) of the CSA.

ii. No future investment of profits from cannabis

Similarly, although the UST has shown that Debtor's prepetition receipt of stock in its acquiring entity probably violated section 854 of the CSA, the UST has not established a likelihood of any postpetition violation from use or investment of cannabis proceeds. Section 854 of the CSA makes it illegal for a "person who has received any income derived, directly or indirectly, from [a relevant violation of the CSA]" to "use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise [engaged in or affecting interstate commerce]." *See* MTD p. 11:21-28 at n. 5 (quoting statute). Debtor does not propose, postpetition, to use any of its remaining assets to "invest" in any enterprise (cannabis-related or otherwise). Instead, Debtor proposes to sell the stock and distribute the resulting cash to creditors, or else transfer the stock directly to creditors.

iii. No showing that a future trustee would have to violate the CSA

The UST raises the specter that any future bankruptcy trustee would have to engage in illegal activity. But the UST does not explain how a trustee would have to violate the CSA or any other law.

For example, even if Debtor still had possession of any cannabis or marijuana products (which it does not), a trustee could "ask[ ] the responsible federal authorities to dispose of the estate's marijuana" and then fulfill the trustee's statutory duty to "liquidat[e] other estate property for distribution to creditors in accordance with the priorities of [§] 726." Steven J. Boyajian, Just Say No to Drugs? Creditors Not Getting a Fair Shake When Marijuana-Related Cases are Dismissed, 36 Am. Bankr. Inst. J. 24, 75 & n. 21 (Sept. 2017).

Moreover, it is not a foregone conclusion that the rights of any federal governmental unit to seize assets would supersede creditors' rights. *See id.* at 75 (text accompanying nn. 28-32). Therefore, not only has the UST failed to show that a future trustee would have to violate the CSA but, to the contrary, it appears that any future trustee probably might have a duty to administer assets rather than simply turn them over to federal authorities.

In addition, if any future trustee were concerned about any of these issues, the trustee could seek declaratory relief or other protections to assure compliance with the law and protection from liability. Alternatively, the trustee could always seek dismissal of this case at that point.

For all of the foregoing reasons, the UST has not established any ongoing violation of the CSA, nor has the UST established that any future trustee would have to violate the CSA. The lack of any demonstrated illegality, now or in the foreseeable ***754** future, is one ground for denial of the MTD. [3]

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d. Alternatively, Congress did not adopt a "zero tolerance" policy under § 1112(b) for any illegality

Supposing for the sake of discussion that the UST could establish a violation of the CSA (which it has not done), that it not enough. Congress did not adopt a "zero tolerance" policy that requires dismissal of any bankruptcy case involving violation of the CSA (or other activity that might be proven to be illegal). *See* *Burton*, 610 B.R. at 637 (no per se rule requiring dismissal when marijuana is present).

True, Congress has enacted the CSA and this Bankruptcy Court's duty is to follow Congressional directives. On the other hand, Congress has not specified what should be the *bankruptcy-specific* remedy for any violation of the CSA.

Congress could have included within the examples of "cause" in § 1112(b)(4) a violation of the CSA, or any other nonbankruptcy laws, but it chose not to do so. This implies that violations of nonbankruptcy laws do not *necessarily* constitute cause for dismissal or conversion.

In addition, such a broad reading of "cause" for dismissal could be extremely disruptive in other cases before this Bankruptcy Court, perhaps even the vast majority of all bankruptcy cases. *See, e.g., In re CWNevada LLC*, 602 B.R. 717, 728 n. 25 (Bankr. D. Nev. 2019) ("bankruptcy courts have a long history of considering cases whose activities and operations have included past, present and possibly ongoing violations of applicable non-bankruptcy, civil and criminal laws") (citing examples); Hon. Keith M. Lundin (Ret.), Up in Smoke, Bankruptcy Workshop, Season 2, Episode 3, available at https://lundin on chapter13.com/Content/WorkshopVideos (last visited on January 18, 2023) (noting bankruptcy courts' and trustees' statutory mandate to administer assets, and extensive history of doing so notwithstanding some connection to illegal activity).

Dismissing every case that had a connection with illegal activity would be contrary to Congress' directives under the Bankruptcy Code. Consider what would happen if the doors of the bankruptcy courts were closed to any debtor who had crossed the line into illegal activity prepetition, and were attempting to wind up that activity postpetition.

Some of the largest business bankruptcy cases, like those of Pacific Gas & Electric Co. of "Erin Brockovich" *fame*, Enron Corporation, and Bernie Madoff, involve alleged or actual criminal activity. Should those cases have been dismissed? How about cases involving sexual abuse? *See CWNevada,* 602 B.R. at 728 n. 25 (citing, *inter alia,* NCR Staff, Catholic Diocese and Orders that Filed for Bankruptcy and Other Major Settlements, National Catholic Reporter (2018), https://www.ncronline.org/news/catholic-dioceses-and-orders-filed-bankruptcy-and-other-major-settlements (last visited on January 18, 2023) (listing numerous bankruptcy proceedings ***755** to address sexual abuse claims, from July 6, 2004 through approximately February 28, 2018)).

On a smaller scale, this Bankruptcy Court takes judicial notice that many small business bankruptcies involve restaurants or small apartment buildings, and most of those businesses have at least some ongoing level of violations of health and safety regulations. When dealing with food and shelter, although it is important to strive for perfection, realistically that goal can be extremely difficult to achieve.

Likewise, many individual debtors have crossed the line into illegality in ways both large and small, from engaging in criminal gang activity to failing to pay taxes or parking fines. This Bankruptcy Court takes judicial notice that individuals who are struggling financially may have difficulty paying parking fines, for example, and there are societal debates about the criminalization of nonpayment of such fines, so barring such a debtor from bankruptcy would not be a step to take lightly.

If all of the foregoing examples were sufficient "cause" for mandatory dismissal, this Bankruptcy Court might have to dismiss most bankruptcy cases. That would harm the constituencies that Congress attempted to protect using all of the tools of the Bankruptcy Code, including creditors, debtors, employees of debtors, and local governments and communities that depend on debtors' ability to reorganize their finances and resume making contributions to commerce and society.

For example, the automatic stay of § 362(a) protects creditors from a "race to collect": absent that stay the assets go to anyone who is able to seize them before other creditors. Insiders or other favored creditors might have an advantage in doing so, contrary to Congress attempts to prevent such favoritism. *See, e.g.,* § 547(b)(4) (longer "look back" period for preference recipients who are insiders).

[12] In addition, an orderly liquidation in bankruptcy typically maximizes the value of a debtor's assets. Bankruptcy

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can preserve going concern value, or can authorize a sale of assets free and clear of liens and other interests, thereby obtaining higher bids than outside of bankruptcy. *See, e.g.,* §§ 363(f) *and* 1129(b)(2)(A)(ii), *and see also In re Olson,* 2018 WL 989263 at *7 (9th Cir. BAP Feb. 5, 2018) (Tighe, J., concurring) (noting the usefulness of sales free and clear, even in cases connected to marijuana).

In addition, dismissal of bankruptcy cases would shield recipients of avoidable transfers (*e.g.,* §§ 547, 548) and persons whose misdeeds might only come to light in the bankruptcy forum, with all of its mandated disclosures and investigative tools. *See, e.g.,* Rules 1007 & 2004; *see also* Boyajian, Just Say No to Drugs?, *supra,* 36 Am. Bankr. Inst. J. 24 at 75 (text accompanying nn. 22-27) (arguing that dismissal of involuntary chapter 7 petition allowed "the alleged debtor to use its own federally proscribed conduct [running a marijuana business] as a shield to protect it from the collection efforts of creditors holding seemingly undisputed claims"). This Bankruptcy Court doubts that Congress intended to shield recipients of avoidable transfers, and wrongdoers, by mandating dismissal of any bankruptcy case that might be connected to violations of criminal law.

In fact, in many situations the victims of illegal activity are the persons who might be most severely harmed by dismissal of any bankruptcy case. This is true whether that illegal activity involves releasing carcinogens into the water supply, financial fraud, being a "slumlord," causing food poisoning, abusing employees, child sexual abuse, or other criminal activity. The victims ***756** may be the biggest creditors, or those with the most to lose.

One other type of creditor who might well be harmed by any mandated dismissal of any case connected to illegal activity is any government agency charged with enforcing the law, such as the Department of Justice, which encompasses the Office of the UST itself. Such agencies' funding, and their ability to continue policing against criminal activity, might depend in part on the preservation and recovery of assets, including through bankruptcy.

[13] For all of these reasons, this Bankruptcy Court does not interpret Congress' mandate that this Bankruptcy Court "shall" dismiss or convert a bankruptcy case for "cause" under § 1112(b) to mean that any violation of criminal law *requires* dismissal. Rather, this Court interprets the statute as giving discretion to determine whether dismissal is warranted based on all the facts and circumstances. *See generally* *Burton*, 610 B.R. 633, 640 *and passim* (review of various authorities, and referring to bankruptcy courts' "broad discretion in deciding whether to dismiss a case").

Nor does this Bankruptcy Court interpret the UST's MTD to advocate for such an extreme position. *Cf.* Clifford J. White III and John Sheahan, Why Marijuana Assets May Not Be Administered In Bankruptcy, 36 Am. Bankr. Inst. J. 34, 34-35 (Dec. 2017) (contrasting bankruptcy cases "in which the criminal activity has already been terminated and the principal concern of the bankruptcy court is to resolve competing claims by victims for compensation" from a case involving "a company that is not only continuing in its business, but even seeking the affirmative assistance of the bankruptcy court in order to ... facilitate its violations of the law going forward") (the authors are listed, respectively, as the director of the Executive Office for U.S. Trustees and as a trial attorney in the Office of the General Counsel).

In sum, this Bankruptcy Court interprets both § 1112(b) and the UST's MTD as adopting a middle ground, under which this Bankruptcy Court must exercise its discretion to determine whether, given all of the facts and circumstances, a debtor's connection to cannabis profits and any past or future investment in cannabis enterprises warrants dismissal of this bankruptcy case. Under this standard, the UST has not met its burden to establish sufficient cause for dismissal, for the reasons stated above, including (i) Debtor's indirect connection with any violation of the CSA (assuming, contrary to this Court's analysis in the prior section of this Opinion, that such a violation exists), (ii) Debtor's intent to liquidate its assets and pay creditors, and (iii) the benefits of a bankruptcy case for all parties in interest, including creditors.

e. Alternatively, the "unusual circumstances" exception applies

[14] Congress has provided that even when there is "cause" to dismiss or convert a case, this Bankruptcy Court must not to do so under the "unusual circumstances" test described above. *See* § 1112(b)(2). The elements of this test have been satisfied, at least in the absence of evidence that prosecutors intend to single out Debtor for particularly harsh treatment that would undermine any ability to pay creditors and otherwise make appropriate use of the bankruptcy system.

Specifically, the unusual circumstances in this case are as follows. First, Debtor has divested itself, prepetition, of any direct involvement in the cannabis business. Second,

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unlike most dismissals by this Court, which generally involve situations such as a pending foreclosure of fully-encumbered ***757** property and no realistic possibility of a distribution to unsecured creditors, in this case any dismissal would undermine a very realistic possibility of a substantial payment to creditors. That successful outcome appears to be very likely because the only thing for Debtor to do is to sell its stock in the Canadian company, which appears to be legal and feasible under Canadian law, and then to use the proceeds to pay creditors; or alternatively to distribute the stock to creditors.

These facts also establish the other elements of the "unusual circumstances" test: conversion or dismissal is not in the best interests of creditors; there is a reasonable likelihood of confirming a plan in a reasonable amount of time; even if Debtor's acts and omissions in seeking to divest itself of its assets and pay creditors somehow violated the CSA or other law, and would otherwise mandate dismissal, Debtor's attempt to maximize value and pay creditors establishes a "reasonable justification" for such acts and omissions; and, so long as Debtor's process of selling or distributing its stock in the Canadian company does not take too long, any violation of law can be "cured within a reasonable time." *Rosenblum*, 608 B.R. at 536-37 (reviewing elements of § 1112(b)(2)).

In addition, this Bankruptcy Court is mindful of the fact that there are many other tools to address any wrongful or illegal conduct by any debtor in possession of the bankruptcy estate. For example, in appropriate circumstances a trustee or examiner can be appointed (§ 1104), or sanctions can be imposed. *See, e.g.,* Rule 9011. The availability of such alternatives reinforces a more flexible interpretation of § 1112 as just one of many possible tools, not a tool that this Bankruptcy Court has to use regardless of the consequences.

In addition, this Bankruptcy Court notes that there are many non-bankruptcy tools that can be used to address any illegal activity. Remedies can be sought, in appropriate situations, by prosecutors, private attorneys general, class action representatives, individual plaintiffs, and others, such as local, state, and national governments, to address any violations of nonbankruptcy law in a more nuanced and targeted manner than the blunt tool of dismissing bankruptcy cases. Again, the availability of such alternatives reinforces this Bankruptcy Court's interpretation of § 1112(b) as providing some discretion: dismissal is not the only remedy.

f. No intent to condone illegal activity

To be clear, nothing in this Opinion should be interpreted as condoning illegal activity. Illegal activity can be cause for dismissal in appropriate circumstances, both as a matter of interpreting Congress' directives in § 1112(b) and, more generally, to preserve the integrity of the bankruptcy system and the bankruptcy courts that Congress has established. *See, e.g., In re Mattiace Industries, Inc.*, 76 B.R. 44, 47-48 (Bankr. E.D.N.Y. 1987) (dismissing chapter 11 bankruptcy case because debtor's continued violations of state environmental regulations endangered public health and conversion was inappropriate due to difficulties a trustee would face in managing debtor's hazardous waste site with limited estate resources)

[15] But this Bankruptcy Court would be overstepping its role, and acting contrary to Congress' directives within the Bankruptcy Code, if it were to deny creditors, debtors, employees, equity investors, and other constituencies the benefits and protections of bankruptcy based on the facts and circumstances presented. In general this Bankruptcy Court should defer to prosecutors, and all of the other types of persons mentioned above, to use their discretion ***758** about whether and how to address any violations of nonbankruptcy law. *See* *Cook Investments*, 922 F.3d 1031, 1036 (rejecting "ombudsman" role of bankruptcy court). Such parties can pursue remedies in a more nuanced and targeted manner, rather than using the blunt tool of dismissal, which on the record presented is contrary to the best interests of creditors and the estate.

4. CONCLUSION

For all of the foregoing reasons, the MTD has been denied by separate order.

All Citations

647 B.R. 748, 72 Bankr.Ct.Dec. 59

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Footnotes

1 Unless the context suggests otherwise, a “chapter” or “section” (“§”) refers to the United States Bankruptcy Code, 11 U.S.C. § 101 et seq. (the “Code”), a “Rule” means the Federal Rules of Bankruptcy Procedure or other federal or local rule, and other terms have the meanings provided in the Code, Rules, and the parties’ filed papers.

2 Although the UST has filed a notice of appeal, that does not divest this Bankruptcy Court of jurisdiction to issue this Opinion for two alternative reasons. First, so far as this Bankruptcy Court is aware, no appellate court has granted the UST's motion for leave to appeal (docket no. 90). *See* *In re Rains*, 428 F.3d 893, 903-904 (9th Cir. 2005) (“if the order at issue is interlocutory, any appeal ... would not transfer jurisdiction to an appellate court”) (citations omitted); *In re Bertain*, 215 B.R. 438 (9th Cir. BAP 1997) (“The denial of a motion to dismiss is an interlocutory order”) (cleaned up; citations omitted). Second, this Opinion does not alter or expand any prior rulings, and instead merely provides further explanation, as anticipated on the record at the above-captioned hearing. *See* *Rains*, 428 F.3d at 904 (other exceptions to rule that notice of appeal divests lower court of jurisdiction).

3 To be clear, Debtor's apparent ownership of over 9% of the stock of a cannabis business puts it in uncomfortably close proximity to the cannabis industry. Perhaps, if all the facts and circumstances were known to this Bankruptcy Court, and if this Bankruptcy Court were to engage in independent research beyond the authorities cited by the parties, Debtor's proposed liquidation actually would be a violation of the CSA or some other criminal statute. But this Bankruptcy Court has not been asked to render any summary judgment as to purported violations of criminal law, and this Bankruptcy Court's rulings above should not be interpreted as any such summary judgment. Rather, on the present record and solely for purposes of the UST's MTD, no violation of the CSA has been established.

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