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The Delaware Bankruptcy Court Grapples With Section 546(e) Post-Merit Management

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In its ruling in *FTI Consulting, Inc. v. Sweeney (In re Centaur, LLC)*, the United States Bankruptcy Court for the District of Delaware addressed the Supreme Court's recent clarification of the scope of Bankruptcy Code Section 546(e)'s "safe harbor" provision, affirming a more narrow interpretation of Section 546(e).

Section 546(e) limits a bankruptcy trustee's power to avoid transfers made by, to, or for the benefit of certain entities, including financial institutions. A split of authority arose in the lower courts concerning the scope of Section 546(e). A number of courts, including the Third Circuit, took an expansive view that the safe harbor applies to transfers involving financial institutions at any point in the transaction. The Seventh and Eleventh Circuits have held that the safe harbor does not apply to transactions in which financial institutions acted only as intermediaries. This split of authority triggered the Supreme Court's review of the issue.

FTI Consulting arises from the bankruptcy case of Valley View Downs, L.P. ("VVD"). Prior to its bankruptcy filing, VVD acquired the membership interests of certain of its minority partners for cash and a promissory note (collectively, the "Transfers"). The parties used Credit Suisse to finance the Transfers.

During VVD's bankruptcy case, the trustee sought to avoid the Transfers as constructive fraudulent transfers. The payment recipients opposed avoidance on the grounds that the Transfers fell within the scope of Section 546(e)'s safe harbor because the Transfers involved a financial institution, Credit Suisse. The Bankruptcy Court suspended consideration of the issue pending the Supreme Court's consideration of the scope of Section 546(e) in *Merit Management Group, LP v. FTI Consulting, Inc.*

In early 2018, the Supreme Court issued its ruling in *Merit Management*. Focusing on the language of the statute and statutory context, the Supreme Court held that Section 546(e) only applies to the contested transfer (e.g., from the debtor to the ultimate recipient) and not to intermediary transactions within the contested transfer. Accordingly, Section 546(e) does not protect a transfer that was routed through a financial institution if neither the debtor nor the ultimate beneficiary of the transfer are protected entities under Section 546(e).

Following the Supreme Court's ruling, the Bankruptcy Court in *FTI Consulting* held that the participation of a financial institution intermediary, such as Credit Suisse, was irrelevant to the Section 546(e) analysis of the Transfers. As neither VVD nor the recipients of the Transfers are financial institutions, and the transactions involving Credit Suisse were only component parts of the Transfers, Section 546(e) cannot apply to the Transfers.

FTI Consulting provides a glimpse into Section 546(e)'s application post-*Merit Management*— parties who are not financial institutions may be unable to rely on the safe harbor to protect transactions from the avoidance powers of bankruptcy trustees

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