Pratt's
Journal of Bankruptcy Law

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JULY-AUGUST 2025

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Library of Congress Card Number: 80-68780

ISBN: 978-0-7698-7846-1 (print)
ISBN: 978-0-7698-7988-8 (eBook)
ISSN: 1931-6992

Cite this publication as:

[author name], [*article title*], [vol. no.] PRATT'S JOURNAL OF BANKRUPTCY LAW [page number] ([year])

Example: Patrick E. Mears, *The Winds of Change Intensify over Europe: Recent European Union Actions Firmly Embrace the "Rescue and Recovery" Culture for Business Recovery*, 10 PRATT'S JOURNAL OF BANKRUPTCY LAW 47 (2025)

Editorial Office
230 Park Ave., 7th Floor, New York, NY 10169 (800) 543-6862
www.lexisnexis.com

MATTHEW BENDER

(2025–Pub.4789)

Editor-in-Chief, Editor & Board of Editors

POSTMASTER: Send address changes to *Pratt's Journal of Bankruptcy Law*, LexisNexis Matthew Bender, 230 Park Ave. 7th Floor, New York NY 10169.

The Impact of *In re 301 W N. Ave., LLC*, on the Enforcement of Bankruptcy-Remote Protections

By Steven M. Herman, Kathryn M. Borgeson and Sara Markov*

In this article, the authors discuss a recent bankruptcy court decision that represents a significant development at the intersection of corporate governance, commercial real estate, and bankruptcy law.

A bankruptcy court in Illinois recently issued a decision upholding the enforceability of provisions requiring an independent manager's consent prior to a borrower filing for bankruptcy. The ruling in, *In re 301 W N. Ave., LLC,*[1] represents a significant development at the intersection of corporate governance, commercial real estate, and bankruptcy law and reinforces the role of structured corporate governance mechanisms in protecting lenders from undesired bankruptcy filings.

BACKGROUND

301 W North Avenue, LLC, a Delaware limited liability company (the Debtor), owns North Park Pointe Apartments, a mixed-use development at 301 West North Avenue in Chicago, Illinois (the Property). On September 23, 2020, BDS III Mortgage Capital G, LLC (the Lender) provided a $26 million loan to the Debtor secured by the Property. Martin Paris, Jr. (Paris), acting as president of the Debtor's manager, executed these loan documents.

Prior to making the loan, the Lender required the Debtor to be a bankruptcy-remote entity and to have one acceptable independent manager. To meet these requirements, the Debtor entered into an agreement (the CTCS Agreement) with CT Corporation Staffing, Inc. (CTCS), which specializes in providing independent managers. Lisa M. Pierro (Pierro), an independent manager for over 500 corporate entities, was designated as the independent manager for the Debtor "unless and until she is removed, resigns or is replaced" in accordance with the Debtor's LLC Agreement (the LLCA).

Under the CTCS Agreement, Pierro would be given reasonable time to investigate matters before the board and may engage independent legal counsel if necessary. Pierro's appointment would be automatically renewed unless either

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[1] In re 301 W N. Ave., LLC, 666 B.R. 583 (Bankr. N.D. Ill. 2025).

party provided 30 days' notice to terminate. The CTCS Agreement also provided that both CTCS and Pierro would be indemnified against claims, except in cases of willful misconduct.

The loan agreement further reinforced Pierro's role and required that the Debtor could not file for bankruptcy without Pierro's approval. It also required that there must be at least one independent manager who is reasonably satisfactory to the Lender at all times. Any removal or replacement of the independent manager required at least two business days' prior written notice to the Lender, along with evidence that the replacement independent manager satisfied the Debtor's organizational documents.

On October 1, 2023, the Debtor defaulted on the loan, and in response, the Lender initiated foreclosure proceedings. On February 27, 2024, just before a scheduled foreclosure hearing, the Debtor filed for bankruptcy. The Debtor, its members and the Debtor's manager executed a Consent in Lieu of Meeting of the Members and Manager of 301 W North Avenue, LLC (the Consent in Lieu) to authorize the bankruptcy filing and Paris, acting on behalf of the Debtor's manager, signed the bankruptcy petition, declaring under penalty of perjury that he was authorized to do so. The bankruptcy petition was filed without Pierro's consent, and the Consent in Lieu did not include a signature block for Pierro.

During a creditors' meeting on March 27, 2024, Paris testified that:

(1) He was unaware of any independent manager's consent requirement;

(2) He did not recall any individual needing to approve the bankruptcy filing; and

(3) He did not recognize Pierro's name.

However, Pierro was listed as the manager in the Debtor's annual filings with the Illinois Secretary of State from 2020 to 2023, further evidencing her role as the Debtor's independent manager.

In April 2024, Pierro resigned, citing concerns over unpaid invoices from CTCS and the bankruptcy filing. However, she backdated her resignation to August 31, 2022 – the last date CTCS received payment.

The court found no evidence that the Debtor was aware of Pierro's resignation before the bankruptcy filing, noting Paris's testimony that he did not even recognize the name Lisa Pierro. Furthermore, the Debtor failed to notify the Lender of Pierro's resignation or appoint a replacement independent manager, as required under the loan documents.

The Lender subsequently filed a motion to dismiss the bankruptcy case and to bar the Debtor from refiling (the Motion to Dismiss).

LEGAL DISCUSSION AND RULING

Under 11 U.S.C. § 1112(b), a bankruptcy court must dismiss a bankruptcy case if there is "cause" to do so. One such cause is when an entity lacks the legal authority to file for bankruptcy. The U.S. Supreme Court has ruled that if those acting on behalf of an entity are not legally authorized to file for bankruptcy, the court has no choice but to dismiss the case. Federal bankruptcy courts have previously upheld this principle, holding that a case must be dismissed if the individuals filing on behalf of an entity lack proper authority.

The Motion to Dismiss raised two key questions:

(1) Was the Debtor properly authorized to file for bankruptcy?

(2) If not, did the Debtor's LLCA unlawfully restrict its ability to do so?

WAS THE DEBTOR PROPERLY AUTHORIZED TO FILE FOR BANKRUPTCY?

The Debtor is governed by Delaware law and its LLCA, which required the unanimous written consent from its members and managers (including the independent manager) for the Debtor to file for bankruptcy. Therefore, the consent of Pierro was required to authorize the Debtor's bankruptcy filing.

Paris previously testified that he did not confer with Pierro to obtain her consent to the filing and that he did not "believe there was an independent manager." Paris further testified that he did not even recognize the name "Lisa Pierro."

Additionally, the Consent in Lieu did not have a signature block for Pierro to sign. In light of this evidence, the court found that the LLCA clearly designated Pierro in this role, and that the Debtor failed to obtain Pierro's consent to authorize the filing.

In response, the Debtor argued that Paris believed that Pierro had resigned prior to the filing, and therefore, her consent would not have been required to authorize the filing. The Debtor also argued that Pierro's resignation amounted to ratification of the bankruptcy filing.

The court recognized the confusion surrounding the timing of Pierro's resignation but found it evident that she signed and submitted her resignation on April 30, 2024 – two months after the Debtor filed for bankruptcy. Pierro testified that her resignation was prompted not only by the Debtor's failure to pay the CTCS, but also by the bankruptcy filing itself, which she first learned about in April, 2024 when contacted by the Lender's counsel regarding a subpoena. Based on this, the court found that Pierro was still the independent manager at the time of the bankruptcy filing, and her consent was required to authorize the filing.

The next question was whether Pierro's resignation amounted to a ratification of the bankruptcy filing. Under Delaware law, implied ratification requires that a party, with full knowledge of the relevant facts, either remains inactive for a significant period, takes actions that acknowledge the disputed act, or behaves in a way that implies approval. However, the evidence showed that Pierro only became aware of the bankruptcy in April – more than a month after the petition was filed –and resigned shortly thereafter. The court found that this did not demonstrate that Pierro had prior knowledge of the filing or took any steps to affirm it, but instead that Pierro's prompt resignation suggests that she rejected the bankruptcy. The court concluded that the Debtor failed to prove that Pierro ratified the filing and therefore, the filing was unauthorized.

DID THE DEBTOR'S LLCA UNLAWFULLY RESTRICT ITS ABILITY TO DO SO?

Even though the Debtor was not authorized to file for bankruptcy, the question remained whether the LLCA imposed impermissible restrictions on the Debtor's ability to access bankruptcy relief. Typically, corporate governance provisions that overly restrict an entity's ability to file for bankruptcy are void as against public policy. Here, the Debtor argued that the provisions requiring Pierro's consent fall into this category. If this was the case, then even if the LLCA required Pierro's consent, the bankruptcy petition would have been properly filed, because the provisions requiring Pierro's consent were unenforceable. However, provisions requiring an independent manager to participate in key decisions, including bankruptcy filings, are not inherently void as long as they create a structure where fiduciary duties are respected and the provisions otherwise comply with applicable law.

Court decisions from *In re Lake Michigan Beach Pottawattamie Resort LLC* and *In re Intervention Energy Holdings, LLC,* set important precedents, establishing that corporate governance provisions which overly restrict a debtor's ability to exercise its bankruptcy rights are unenforceable. In *Lake Michigan Beach*, the court ruled that provisions requiring the lender's consent as a "Special Member" before the borrower could file for bankruptcy were invalid because they eliminated the Special Member's fiduciary duties to the borrower. Similarly, in *Intervention Energy Holdings*, the court found that creditor consent provisions, often referred to as a "golden share" or "creditor blocking vote" effectively eliminated the debtor's right to seek federal bankruptcy relief, describing them as an "absolute waiver" of that right and therefore contrary to public policy.

Here, the court reviewed specific provisions in the LLCA, noting that the LLCA imposed upon Pierro fiduciary duties to the Debtor as well as its creditors, ensuring that bankruptcy decisions were made with appropriate due diligence. The Debtor argued that Pierro's role served only the Lender's interests since the position remained in place for the duration of the loan. However, the court found that this arrangement was a reasonable and logical requirement, rather than an overly restrictive limitation on the Debtor's access to bankruptcy relief. The Debtor also claimed that Pierro owed no duties to the LLC's members, but the court emphasized that the primary concern is whether Pierro's role unlawfully restricted the Debtor's right to file for bankruptcy, which it found was not the case here.

Furthermore, the Debtor argued that limiting the interests that Pierro must consider to the Debtor's economic interests allowed her to avoid liability for a breach of fiduciary duties. However, the court found it appropriate for an independent manager to assess economic implications when authorizing a bankruptcy filing.

Lastly, the Debtor challenged indemnification provisions in the CTCS Agreement, arguing that they unlawfully shielded Pierro from liability, even for bad faith actions. However, the court noted that the LLCA was the key document at issue – not the CTCS Agreement – and the LLCA explicitly prohibited indemnification in cases of bad faith or willful misconduct, which aligned with Delaware law.

Ultimately, the court determined that the Debtor's LLCA did not unlawfully restrict its right to seek bankruptcy relief and the provisions were therefore valid. Since the provisions of the LLCA were enforceable and Pierro did not consent to the filing, the court found the Debtor lacked the necessary authorization to file the petition. As a result, the Motion to Dismiss was granted. The court did, however, deny the Lender's request to bar Debtor's refiling, stating that to do so would effectively prohibit the Debtor from properly deciding – in compliance with its LLCA – whether it should file for bankruptcy.

LOOKING AHEAD

The ruling in *In re 301 W N. Ave., LLC* has significant implications for commercial real estate transactions, particularly in reinforcing the use of bankruptcy-remote structures, which are widely used in real estate financing to protect lenders by isolating a property's financial obligations from the broader business operations of its owners.

A common mechanism for achieving bankruptcy remoteness is the use of Special Purpose Entities (SPEs), which are designed to limit the risk of insolvency by maintaining strict separateness from affiliated entities. Lenders often impose restrictions, such as independent director or manager provisions, to prevent SPEs from filing for bankruptcy without prior approval. Historically, courts have scrutinized such provisions, particularly when they effectively eliminate a borrower's ability to seek bankruptcy relief. However, this ruling affirms that provisions requiring an independent manager's consent remain enforceable, so long as they do not constitute an outright prohibition on bankruptcy, but rather serve a legitimate governance function.

This decision follows in the wake of the *General Growth Properties* (GGP) bankruptcy, which raised concerns over the effectiveness of SPE structures. In 2009, GGP, a publicly-traded real estate investment trust, filed for bankruptcy along with numerous subsidiary SPEs that were traditionally considered bankruptcy-remote. The lenders to the SPEs had required independent managers who were not insiders of GGP, but they did not have the more robust removal requirements and fiduciary duty provisions that were included in the LLCA in *301 W N. Ave*. On the eve of its bankruptcy filing, GGP removed the independent managers at the SPEs and replaced them with restructuring professionals. Those restructuring professionals took into account the interests of the entire GGP enterprise as a whole and voted to file each of the SPEs for bankruptcy, including those that were solvent and whose properties were performing. Various lenders filed motions to dismiss the SPE bankruptcies as bad faith filings, arguing that they were premature and sought to restructure the debt of solvent SPEs for the benefit of GGP's equity holders.

However, the court allowed the SPEs to proceed with bankruptcy filings, finding that the inclusion of the solvent SPEs in GGP's bankruptcy filing was legitimate because those SPEs were integral to GGP's reorganization. In contrast to *301 W N. Ave.*, the restructuring professionals then serving as independent managers had voted to file the SPEs for bankruptcy, and there was no prohibition on considering the interests of GGP in determining whether to file the SPEs for bankruptcy. The GGP ruling suggested that financial entanglement and operational integration with the parent company could override certain structural safeguards previously relied on by lenders to mitigate the future risk of bankruptcy.

The GGP case weakened the assumption that SPEs could remain insulated from a parent company's financial distress. In response, lenders have since sought to bolster SPE structures through more stringent separateness covenants and the enhanced independent manager provisions that were included in the *301 W N. Ave* LLCA, which are the current market standard.

Following GGP, cases such as *Lake Michigan Beach* and *Intervention Energy* had provided practitioners with guidance as to the types of bankruptcy voting provisions that would not be enforceable. The *301 W N. Ave.* decision, however, provides concrete confirmation that the standard independent manager provisions are enforceable and effective. By upholding the enforceability of independent manager consent provisions, this decision strengthens lenders' ability to protect their financial interests, while also establishing clear legal boundaries around governance structures. As the commercial real estate market continues to evolve, this case will serve as a critical benchmark in structuring bankruptcy-remote entities and balancing the power dynamics between borrowers and lenders in distressed financial situations.