



ANALYSIS: Where Have All the Preference Lawsuits Gone?

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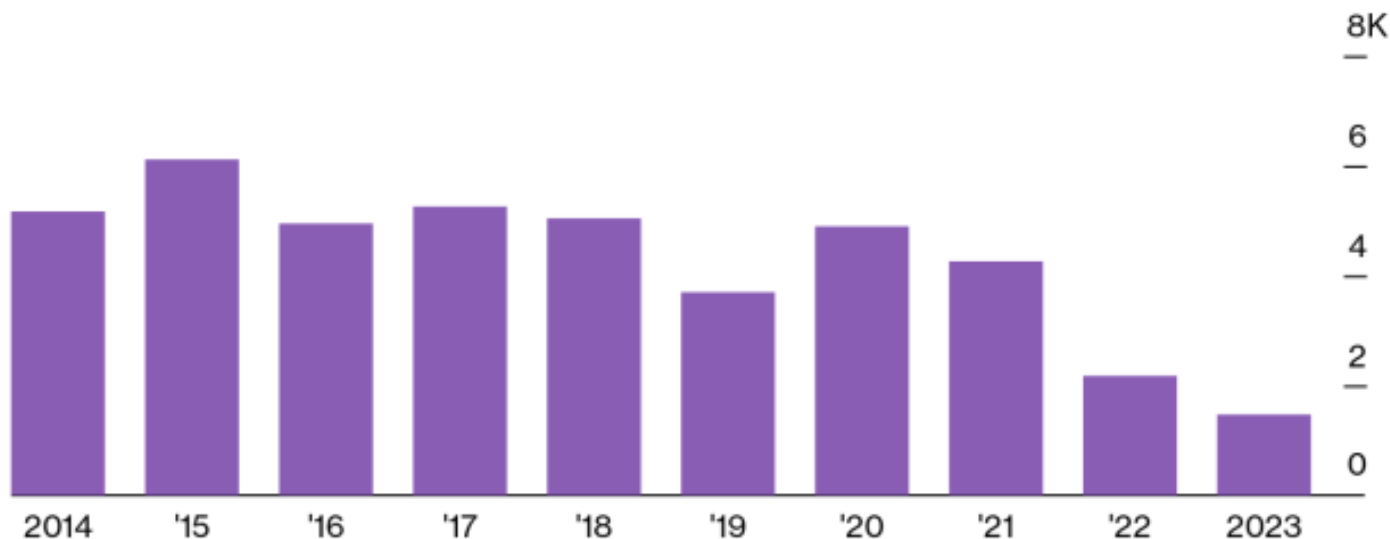
By Jeffrey P. Fuller 2024-02-20T10:56:27000-05:00

While 2023 was one of the busiest of recent years for Chapter 11 bankruptcy filings, last year was the quietest year for preference lawsuits in the past decade.

Since 2014, there's been a 72% drop in these lawsuits, which allow a debtor or trustee to claw back money paid to creditors within a certain time period prior to the bankruptcy petition date. And the number of preference lawsuits filed last year (1,470) is down from 2015's high of 6,112, according to a Bloomberg Law dockets search.

In 2023, Preference Lawsuits Dwindled to Lowest Volume in a Decade

Preference complaints filed in bankruptcy courts, 2014-2023



Source: Bloomberg Law Dockets. Yearly case totals include adversary proceedings using NOS code for preference.

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So what are the reasons for the decline of preference litigation?

Effect of Bankruptcy Reform or Bankruptcy Bust?

Last year, I [identified this decline](#) in preference adversary proceeding filings and speculated that one possible reason might have been the amendments to [section 547 of the Bankruptcy Code](#) in the Small Business Reorganization Act of 2019. These changes require preference plaintiffs to take a defendant's potential affirmative defense into account.

However, I no longer believe that the section 547 amendments are what drove the totals downward. Taking a look at the past decade of preference lawsuit data, the totals during 2020 and 2021—the first two years that the amendments were in effect—weren't dramatically lower than the yearly preference totals from 2014 to 2019.

Instead, the decline could be related to the pandemic-related “bankruptcy bust” of 2021 and 2022. Preference cases owe their existence primarily to Chapter 11 and Chapter 7 cases. If these cases are few and far between, it follows that there will be far fewer preference cases.

In the Chapter 11 context, there will often be some lag time between the petition date and the filing of preference lawsuits. Chapter 11 debtors ordinarily want to avoid suing their creditors while simultaneously building support for a plan. Pursuit of preference claims is often left to a post-confirmation [liquidating trustee](#).

Because of this, preference cases have often been filed shortly before the expiration of the [two-year statute of limitation](#) that runs from the petition date. But this period appears to be shortening in recent years.

Kara Casteel, an attorney with ASK LLP, which represents plaintiffs in avoidance action litigation (which includes preferences), said that the period from petition date to preference case filing has shrunk to anywhere from 90 days to six months into a case. “People want to see money right away,” Casteel said when I spoke with her recently about preference litigation.

According to [data from US Courts](#), 2020 had the highest yearly total (7,786) in the past decade for business-related Chapter 11 cases, but this didn't seem to help drive up the 2022 preference total—likely because most of the potential cases were already filed by 2021. Also, the number of Chapter 7 business cases wasn't especially high in 2020 (it was the third lowest total of the decade), which also might have helped influence the low number of preference cases in 2022.

It will be interesting to see if preference lawsuits in 2024 and 2025 climb back up, due to 2023 being a somewhat busier year for bankruptcy (the second busiest for Chapter 11 business cases in the last

decade, though it was still the third slowest year of the last decade for business bankruptcies overall).

Business Bankruptcies Were Busier in 2023 After Two Slow Years



Source: U.S. Courts

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To Sue or Not to Sue

Factors other than the volume of Chapter 7 and Chapter 11 cases may be at play as well. Casteel and Joseph Steinfeld, another attorney with ASK LLP, noted the dynamics that a [creditors' committee](#) can have on whether or not preference litigation is pursued. Because preference litigation is ordinarily pursued after confirmation of a plan, and the debtor is often no longer in the picture, it's typically the committee that makes decisions about this litigation.

Some committee members may raise concerns about the potential impact of preference litigation on a reorganized debtor or a purchaser of assets who assumes the debtor's name should vendors be targeted with these lawsuits. However, other members may argue that these claims are assets of the estate that should be pursued in order to increase creditor recoveries.

While litigation can be costly to the bankruptcy estate, preference litigation can be [managed efficiently](#) and some firms can even handle it on a contingency fee basis. It doesn't ordinarily require substantial discovery or evidentiary hearings, and usually is resolved with an early-stage settlement. In any case,

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it's a "good idea to look at the value of the preference claims," even if the ultimate decision is that the "juice is not worth the squeeze," Steinfeld said.

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