

No Equitable Tolling of Section 548 “Look-Back” Period

March/April 2012

Haben Goitom

In *Industrial Enterprises of America v. Burtis (In re Pitt Penn Holding Co., Inc.)*, 2012 WL 204095 (Bankr. D. Del. Jan. 24, 2012), a Delaware bankruptcy court held that the two-year statutory “look-back” period with respect to which a fraudulent transfer may be avoided pursuant to section 548 of the Bankruptcy Code cannot be “equitably tolled.” Previously, the bankruptcy court had issued inconsistent orders in various adversary proceedings in the case providing that the two-year look-back period could be equitably tolled, allowing transfers that occurred outside that window of time to be avoided. *Pitt Penn* clarifies that, in the view of this Delaware bankruptcy court, the look-back period cannot be tolled for equitable reasons because it is “a substantive element of a § 548 cause of action” rather than a statute of limitations.

Avoidance of Fraudulent Transfers and Obligations

Section 548(a) of the Bankruptcy Code allows a bankruptcy trustee or chapter 11 debtor in possession (“DIP”) to avoid transfers of a debtor’s property or obligations incurred by a debtor if the transaction involved was either actually or constructively fraudulent and if the transfer or obligation “was made or incurred on or within 2 years before the date of the filing of the petition.”

Transfers may also be avoided under applicable state law by operation of section 544(b) of the Bankruptcy Code. Section 544(b) allows a DIP or trustee to “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” against the debtor. The primary advantage of this provision over section 548 is that many state fraudulent-transfer laws (in most jurisdictions, a

version of the Uniform Fraudulent Transfer Act) provide for a longer statutory look-back period than the two-year period specified in section 548.

Section 546 of the Bankruptcy Code places other limitations on the ability of a trustee or DIP to commence avoidance actions. Section 546(a) provides in relevant part:

An action or proceeding under section 544, 545, 547, 548, or 553 of this title may not be commenced after the earlier of— (1) the later of— (A) 2 years after the entry of the order for relief; or (B) 1 year after the appointment or election of the first trustee . . . ; or (2) the time the case is closed or dismissed.

If a transfer is avoided, the trustee or DIP can recover the property transferred or its value from the transferee(s) (with certain exceptions) pursuant to section 550 of the Bankruptcy Code.

Background

Pittsburgh-based Industrial Enterprises of America (“IEAM”) was a seller of antifreeze and other automotive additives and chemicals until it went out of business in 2009 after two former IEAM senior executives engaged in a massive fraud that ultimately earned them lengthy jail sentences. IEAM filed for chapter 11 protection on May 1, 2009, in Delaware.

Nearly (but not quite) two years after the petition date, IEAM filed adversary proceedings against various defendants (the “Collyers”) seeking to recover property fraudulently transferred by the company prior to its bankruptcy filing. The complaints assert various state- and federal-law claims as well as claims to recover property, pursuant to sections 544, 548, and 550 of the Bankruptcy Code. The Collyers moved to dismiss all of the claims. The court ruled in their favor with respect to the section 548 claims because the transfers occurred “several months outside of the look-back period,” but it denied the motion to dismiss the remaining claims. In doing so, the

court held that, regardless of when IEAM learned of the transfers or the fraudulent circumstances surrounding them, if the transfers occurred more than two years before IEAM's bankruptcy filing, IEAM could not bring the causes of action under section 548.

That ruling, however, was in direct conflict with the court's prior holdings in other adversary proceedings commenced by IEAM, where the court permitted equitable tolling of fraudulent-transfer actions. The bankruptcy court learned of its inconsistent holdings in connection with IEAM's motion to reconsider the court's order dismissing its section 548 claims against the Collyers.

The Bankruptcy Court's Decision

Apologizing to the parties for its oversight, the bankruptcy court brought "its prior inconsistent rulings into alignment." It ruled that "Section 548(a)'s two-year look-back period is a substantive element of a § 548 cause of action, and therefore cannot be equitably tolled."

IEAM argued that equitable tolling has often been applied by bankruptcy courts to allow a claim to be filed outside the statute of limitations, where some action has been taken on the part of the defendant to make the plaintiff unaware that the cause of action existed. IEAM also argued that equity should prevent the Collyers from benefiting from the statute of limitations when they concealed the fraudulent transfers.

The court agreed that typically, statutes of limitations are equitably tolled to prevent "technical forfeitures that would unfairly thwart a trial on the merits, unless tolling would be 'inconsistent with the text of the relevant statute.'" However, the court explained, IEAM's argument fails

because it does not address whether the two-year look-back period is a substantive element of a section 548 claim that, unlike a statute of limitations, cannot be equitably tolled.

Statutes of Limitations v. Section 548 Look-Back Period

Statutes of limitations, the court emphasized, are rules of procedure meant to “regulate secondary conduct,” such as the filing of a suit, but should not affect the actions that gave rise to the suit.

By contrast, although the text of section 548 creates a cause of action based on the transfer of a debtor’s interest in property (the “primary conduct”), the provision does not “regulate” how far into the future the claim can be brought (the “secondary conduct”), which is what a statute of limitations does. According to the court, the two-year period in section 548 simply looks back from the petition date (when the cause of action accrued) to evaluate transfers that occurred during that window of time. The look-back period, the court wrote, is “baked-in to ‘the actual *substance*’ ” of the cause of action, whereas a statute of limitations begins to run when the cause of action accrues, requiring a litigant to assert a claim within a certain time period.

Turning to an examination of section 546 for purposes of comparison, the court described section 546 as “a true statute of limitations,” whereas the two-year time period in section 548 is a substantive element of a fraudulent-transfer claim that cannot be tolled.

The court respectfully declined to follow contrary (but noncontrolling) precedent relied upon by IEAM. See *Official Committee of Unsecured Creditors v. Pardee (In re Stanwich Fin. Servs. Corp.)*, 291 B.R. 25 (Bankr. D. Conn. 2003). Instead, the bankruptcy court in *Pitt Penn* agreed with the reasoning articulated in *In re Maui Indus. Loan & Fin. Co.*, 454 B.R. 133 (Bankr. D.

Haw. 2011), where the court similarly held that the two-year look-back period is a substantive element of section 548.

Conclusion

Pitt Penn clarifies that even in a court of equity and despite colorable claims of concealment on the part of an avoidance-action defendant, there are limitations on the power of a bankruptcy court to invoke the doctrine of equitable tolling. According to *Pitt Penn*, one such impediment is found in section 548, whose two-year look-back period cannot be equitably tolled because it is a substantive element of a fraudulent-transfer cause of action under federal bankruptcy law.

Although this may appear to be a harsh result, especially when the facts regarding the defendants are particularly egregious, in some instances (like *Pitt Penn*), similar claims can be brought under state law that may provide for a longer look-back period or a “discovery rule” tolling an applicable statute of limitations. Such state-law claims, however, may not always be available.

Finally, the concept of equitable tolling should be distinguished from the statutory tolling provision of section 108 of the Bankruptcy Code. Section 108 expressly gives a trustee or DIP additional time to: (i) commence actions on behalf of the estate, provided that the applicable time period did not expire before the filing of the bankruptcy petition; and (ii) file pleadings, cure defaults, and perform other acts on behalf of the debtor.