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Buying Debt? Make Sure You "Buy" It Rather Than Take It By "Assignment"

If you are considering buying a loan - whether distressed or non-distressed - real estate or corporate in nature -- it is important to structure the transaction as a "sale/purchase" rather than an "assignment."

Borrowers in distress routinely threaten or assert "lender liability" claims against their lenders arising from allegedly inappropriate conduct. Suppose the lender engages in such inappropriate conduct, and then transfers the loan. If the borrower files for bankruptcy, who will the borrower (or bankruptcy trustee) be able to sue for lender liability claims? Can a court impose "lender liability" on the transferee of the loan based upon the transferor's conduct?

In the recent case of *In re Enron Corp. v. Springfield Assocs. L.L.C.*, No. 07 Civ. 1957, 2007 U.S. Dist. LEXIS 63129 (S.D.N.Y. Aug. 27, 2007), the U.S. District Court for the Southern District of New York ruled that the *sale* of a bankruptcy claim to a good faith purchaser would eliminate the risk that the claim could be disallowed or subordinated based upon certain conduct of the transferor. The Court also ruled, however, that the *assignment* of a claim would not eliminate such risk of disallowance or subordination. The Court's distinction between a "sale" and an "assignment" - terms which are typically used interchangeably -- has caused much criticism among bankruptcy practitioners. Indeed, all parties to the litigation, and interested third parties such as the Loan Syndications and Trading Association (LSTA) criticized the distinction as "not legally relevant to the analysis."

It is possible, if not likely, that a higher-level court will eliminate the distinction between a sale and an assignment as it relates to the effect of loan acquisitions. In the meantime, however, each loan acquisition should be structured as a purchase and sale to the greatest extent possible. All parties should also recognize that the law in this area is murky and developing, and that each transaction is unique. Accordingly, rather than relying upon this short summary, you should consult with bankruptcy/insolvency counsel in connection with any loan acquisition.

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Firm Facts

On October 13, 2007, Bruce Stachenfeld completed the **Ford Ironman World Championship Triathlon** in Kona, Hawaii.

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