

Claim Trading Industry: Pay Attention to Anti-Assignment Provisions!

Article By:

Elliot M. Smith

In a June 20, 2018 opinion, Judge Carey of the United States Bankruptcy Court for the District of Delaware sustained an objection to a proof of claim that had been traded during the bankruptcy case and filed by the claim purchaser. The opinion highlights the importance of being vigilant in conducting diligence before acquiring a claim against a bankruptcy debtor, especially regarding the ability of the original creditor to assign the claim without the debtor's consent.

The claim at issue in [In re Woodbridge Group of Companies, LLC](#) was based on three prepetition promissory notes issued by one of the debtors totaling \$75,000. The notes each contained a provision prohibiting the lender from assigning them without the borrower's consent, and stating that an assignment without consent would be "null and void." This last clause was crucial to the Bankruptcy Court's ruling.

The lesson for claim traders is that there is an important distinction between the *power* to assign and the *right* to assign. Applying Delaware law, which governed the notes, the Bankruptcy Court explained that when a provision restricts the *power* to assign, the assignment itself is void. Such a provision is enforceable against a lender under Delaware law and in the world of bankruptcy. In contrast, when a provision restricts the *right* to assign, an assignment in violation of that provision may breach the terms of the contract (and possibly result in a damages claim), but the assignment itself remains valid and enforceable. This distinction may seem like splitting hairs, but nonetheless reflects what courts describe as the "modern approach" to assignment clauses. The deciding factor as to whether an anti-assignment provision implicates the power to assign is whether the provision has express language saying that an assignment in violation of the provision will be void or invalid. Without this language, the provision will generally be viewed as implicating only the right to assign. The notes at issue in this case contained the necessary "null and void" language. As such, the Bankruptcy Court held that the provision restricted the lender's power to assign, and the assignment was null and void given the failure to obtain the debtor's consent to the assignment.

The Bankruptcy Court also rejected other arguments advanced by the lender, including that the debtor was unable to enforce the anti-assignment provisions because of its prior breach of the notes. Judge Carey explained that it is "axiomatic that a non-breaching party may not emerge post-breach with more rights than it had pre-breach." The lender had a choice to make when the debtor breached its prepetition obligations: stop performance and assume the contract is avoided, or

continue performance and sue for damages. The lender cannot do both. By filing a claim and asserting rights under the notes, the lender was seeking to enforce the terms of the notes and therefore must abide by the restrictions in the notes, including the anti-assignment provisions.

The Bankruptcy Court also rejected an argument that section 9-408 of the Uniform Commercial Code nullifies all contractual provisions that purport to restrict the assignment of a note or require the consent of the maker as a condition for assignment. This section does say that certain kinds of anti-assignment provisions are ineffective in certain scenarios. However, based on the language of the statute and the Official Comments to the statute, and to avoid rendering other sections of the U.C.C. superfluous, the Bankruptcy Court held that section 9-408 applied only to provisions purporting to restrict grants of security interests in promissory notes, and not to the outright transfer of a promissory note itself. The section was therefore inapplicable in this case.

This is not the first time Judge Carey has weighed in on matters affecting the claim trading industry. His opinion in *In re KB Toys, Inc.*, 470 B.R. 331 (Bankr. D. Del. 2012) also discussed the industry and the Judge's view that claim traders "are highly sophisticated entities fully capable of performing due diligence before any acquisition." Claim traders are being held to high standards, and are expected to do their diligence in any claim acquisition. Going forward, this diligence needs to include focusing on any anti-assignment provisions affecting the power to assign without consent of the borrower. The ability to file an allowed proof of claim depends on it.

© Copyright 2025 Squire Patton Boggs (US) LLP

National Law Review, Volume VIII, Number 221

Source URL: <https://natlawreview.com/article/claim-trading-industry-pay-attention-to-anti-assignment-provisions>