

MEMO# 7133

July 24, 1995

DISTRICT COURT DECISION CONCERNING RIGHTS OF ORANGE COUNTY NOTE HOLDERS TO POST-PETITION PROPERTY

1 In re Orange County, Dist. Ct. Case No. SACV 95-341-GLT [AR] (July 12, 1995). 2 See Memorandum to Money Market Funds Ad Hoc Committee No. 3-95, SEC Rules Members No. 31-95, CreditorGs Rights Subcommittee, dated April 27, 1995. July 24, 1995 TO: MONEY MARKET FUNDS AD HOC COMMITTEE No. 8-95 SEC RULES MEMBERS No. 49-95 CREDITOR'S RIGHTS SUBCOMMITTEE RE: DISTRICT COURT DECISION CONCERNING RIGHTS OF ORANGE COUNTY NOTE HOLDERS TO POST-PETITION PROPERTY

The United States District Court for the Central District of California has held that the lien securing certain tax and revenue anticipation notes (TRANS) issued by Orange County is a "statutory lien," which survived the filing of Orange CountyGs bankruptcy petition. The district court reversed a decision regarding the TRANS by the U.S. Bankruptcy Court and remanded its decision to the bankruptcy court for further determination. A copy of the district courtGs decision is attached.¹ As we previously informed you,² the holders of certain TRANS had petitioned the bankruptcy court to lift the automatic stay to permit them to file a complaint in state court to force the County to set aside certain revenues for payment on the notes. The note holders asserted, among other things, that unless the County was required to set aside such funds, it would have insufficient revenues to pay the note holders on the July 1, 1995 maturity date. In denying the note holdersG motion, the bankruptcy court held that the note holders had obtained a security interest rather than a statutory lien, and as such, their interest in revenues collected after December 6, 1995 was cut off as a result of the bankruptcy filing. On appeal from the bankruptcy court, the district court first examined differences between a statutory lien and a security interest under the Bankruptcy Code. It concluded that the distinguishing feature of a statutory lien is that it arises solely by force of a statute. The court then examined the language of the California statute authorizing Orange County to pledge assets to secure the TRANS and determined that the language created a "statutory lien," despite the fact that the decision by the County to borrow on a secured basis was voluntary. The court agreed with the rejection by the bankruptcy court of the note holdersG argument that they have an interest in the CountyGs pre-bankruptcy petition right to collect taxes. According to the court, the lien only gave the note holders an interest in taxes collected, not in the right to collect taxes. Finally, the court did not grant the note holders relief from the automatic stay. Instead, it remanded its decision to the bankruptcy court so that it may "provide [the note holders] with adequate protection of their interests." Alexander C. Gavis Assistant Counsel Attachment Note: Not all recipients of this memo will receive an attachment. If you wish to obtain a copy of the attachment referred to in this memo, please call the Institute's Information Resource Center at

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