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EXPERT ANALYSIS

The Impact of Prime Contractor Bankruptcy On U.S. Government Contracts

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In recent years, the U.S. defense industry has seen a decline in revenues and a general deterioration in the financial condition of contractors. These problems, which have resulted from, among other things, the defense drawdown, layoffs and plant closures, have led to a number of contractor bankruptcies, and this trend may well continue. Performance of many defense contracts involves a prime contract, pursuant to which a prime contractor undertakes responsibility to perform the terms of an agreement with the U.S. government. These contracts also involve one or more subcontracts, under which a subcontractor will contract with the prime contractor to perform specific parts of the prime contractor's agreement with the U.S. government. In this article, we explore how the venue of a prime contractor's bankruptcy proceeding can affect the contractor's ability to retain the benefits under its valuable government contracts.

The ability to "cure" defaults and to "assume" and "assign" executory contracts[1] and unexpired leases are among the most significant powers[2] afforded a debtor in its bankruptcy proceeding. Ordinarily, a debtor has the power to override contractual provisions that would otherwise prohibit or restrict the assignment of agreements (anti-assignment provisions), or permit ter-mination or modification of an agreement on the basis of the debtor's bankruptcy filing or financial condition (*ipso facto* provisions). Here we address certain restrictions on the ability of a bankrupt prime defense contractor to override anti-assignment provisions and *ipso facto* provisions in U.S. government defense contracts.

ASSUMPTION, ASSIGNMENT AND REJECTION

"Assumption" is a technical term under the Bankruptcy Code. It does not refer to a debtor's mere continuation of performance under an agreement subsequent to a bankruptcy filing. Rather, assumption is the mechanism by which a debtor, upon notice to creditors, seeks authorization from the bankruptcy court to reaffirm its obligations under an agreement. It requires the debtor to cure monetary and other defaults and prove that it has the wherewithal to continue to honor its contractual obligations on a going-forward basis.[3] The formal assumption of an agreement by a debtor during its bankruptcy proceeding is essentially equivalent to the debtor entering into a new agreement subsequent to the bankruptcy filing.[4]

Damages resulting from a breach of an assumed agreement are administrative obligations (*i.e.*, expenses incurred in connection with the administration of the bankruptcy proceeding), are given priority over the payment of pre-petition general unsecured claims and must be paid in full, in cash, as a condition in confirmation of a plan of reorganization.[5]

As a result, debtors frequently defer decisions regarding the assumption of contracts and leases until they are compelled to decide, ordinarily at the end of the bankruptcy proceeding, upon plan confirmation.[6] When an agreement provides a debtor with goods, services or leased property at a below-market rate, but the debtor will have no use for the subject property on a going-forward basis, the debtor may ordinarily assign the agreement to a third party for a profit, notwithstanding

a contractual provision prohibiting the assignment of the agreement.[7] If an agreement is not valuable to the debtor or to a third party willing to pay to become an assignee, the debtor will ordinarily reject the agreement.[8]

DEBTOR'S ABILITY TO OVERRIDE ANTI-ASSIGNMENT AND *IPSO FACTO* PROVISIONS

With respect to contractual restrictions on assignment, Section 365(f) of the Bankruptcy Code sets forth the general rule that a debtor may assume and assign an executory contract or unexpired lease, notwithstanding a contractual provision to the contrary that prohibits, restricts or conditions such assignment. The *exception* to this rule is contained in Section 365(c) of the Bankruptcy Code. Section 365(c) provides that a counterparty may enforce a prohibition or restriction on assignment in cases in which an applicable non-bankruptcy law (statutory or case law) exists that would excuse the counterparty from accepting performance from, or rendering performance to, an entity other than the debtor or debtor-in-possession, and the counterparty does not consent to such assumption or assignment.

With respect to *ipso facto* provisions, Section 365(e)(1) of the Bankruptcy Code sets forth the general rule that a provision that would otherwise call for the termination or modification of an executory contract or unexpired lease because of a debtor's bankruptcy filing or financial condition is unenforceable. The *exception* to this rule is contained in Section 365(e)(2) of the Bankruptcy Code. Section 365(e)(2) provides that a counterparty may enforce an *ipso facto* provision, if an applicable non-bankruptcy law (statutory or case law) would excuse the counterparty from accepting performance from or rendering performance to the trustee or an assignee, and the counterparty does not consent to such assumption or assignment.[9]

Assumption is the mechanism by which a debtor, upon notice to creditors, seeks authorization from the bankruptcy court to reaffirm its obligations under an agreement.

The opaque language in the Bankruptcy Code's statutory exceptions to the general rules overriding anti-assignment and *ipso facto* provisions has resulted in a split among the circuits regarding the implications of these exceptions on a debtor's rights to *assume* an agreement or to avoid the immediate termination of an agreement upon a bankruptcy filing — even in circumstances in which the debtor has no intention of *assigning* the agreement to a third party.

IMPACT OF THE HYPOTHETICAL TEST ON ANTI-ASSIGNMENT PROVISIONS

Most circuit courts of appeal that have interpreted Section 365(c) of the Bankruptcy Code, including the 3rd, 4th, 9th and 11th circuits, have construed that provision to impose what is known as the "hypothetical test." These courts have held that if an applicable non-bankruptcy law would prohibit or restrict assignment, then the debtor can neither assume nor assign the agreement. These courts focus on the following language in Section 365(c):

> The trustee may not assume *or* assign any executory contract ... if ... (1)(A) applicable law excuses [the counterparty] from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession ...; and (B) [the counterparty] does not consent to such assumption or assignment.[10]

The hypothetical test is premised on the proscription against assumption *or* assignment. These courts conclude that so long as an applicable law prohibits or restricts assignment to a third party, the agreement may be neither *assumed* nor *assigned* by the debtor in its bankruptcy proceeding absent the counterparty's consent, even if the debtor has no intention of assigning the agreement to any such third party.[11]

Application of the hypothetical test to an anti-assignment provision ordinarily will not interfere with a debtor's enjoyment of the benefits of an agreement *prior* to the time when the debtor is compelled to make a determination regarding assumption or rejection,[12] although the inability of the debtor to assume an agreement unilaterally may provide the counterparty with significant leverage in the bankruptcy proceeding.

In some cases, however, courts in hypothetical test jurisdictions have granted a counterparty's request for relief from the automatic stay to terminate its agreement *before* the debtor has moved

to assume or reject, reasoning that the debtor did not have a legally cognizable interest in the agreement.[13] This result is unusual, however, and invariably occurs only in situations in which there has been some question of the debtor's ability to perform under the agreement during the bankruptcy proceeding.[14]

In cases in which a debtor remains ready, willing and able to perform, it is highly unlikely that a court would conclude that a debtor has no legally cognizable interest in an agreement merely because the agreement is not susceptible to unilateral assumption by the debtor. In fact, in some instances, the issue of assumption may never arise, since the underlying agreement may be fully performed during the administration of the bankruptcy proceeding, prior to the date when the debtor would be compelled to make an assumption determination.

In other instances, the debtor may be able to avoid the assumption issue under an existing agreement with an uncooperative counterparty entirely by transitioning to a new provider of goods and services during the bankruptcy proceeding. Even if there is no viable replacement for essential goods or services provided by an uncooperative counterparty, the bankruptcy estate may benefit from a debtor's continued performance under an agreement during a wind-down process. If any of these factors exist, the debtor's economic interest in the agreement will be obvious, and it is highly unlikely that a court would grant stay relief to allow a counterparty to terminate an agreement prior to the time when the debtor would be compelled to make an assumption determination.

Thus, although a debtor in a hypothetical test jurisdiction must proceed with caution, it will ordinarily be permitted to continue to perform under an agreement during the course of a bankruptcy proceeding, even in cases in which applicable law would prohibit the debtor from assigning the agreement to a third party.

Some Chapter 11 debtors in hypothetical test jurisdictions have attempted to avoid the prohibition on unilateral assumption of an agreement subject to applicable non-bankruptcy law that would restrict assignment. These debtors did so by essentially ignoring the issue and by allowing the agreements to "ride through" the bankruptcy proceedings without ever making a determination regarding assumption or rejection. Under the ride-through doctrine, an agreement may pass through a bankruptcy proceeding without being either assumed or rejected. Essentially, the counterparty's claim survives the bankruptcy proceeding. Although some courts in hypothetical test jurisdictions have permitted ride-through, the ultimate efficacy of such approach is uncertain.

At least one court has noted that although an agreement not formally assumed under Section 365(a) of the Bankruptcy Code may ride through the bankruptcy proceedings, the debtor will not be entitled to the benefits of the exceptions to cure contained in Section 365(b)(2), which excuses a debtor from curing certain types of defaults in connection with assumption.[15] As a result, a counterparty to an agreement that has ridden through bankruptcy may be able to terminate the agreement as soon as the debtor emerges from bankruptcy.

In the bankruptcy proceeding of a prime contractor, a question may arise regarding the debtor's ability to assume a valuable government contract in light of the federal Anti-Assignment Act. The Anti-Assignment Act restricts the transfer of any right or interest in a government contract and operates to annul a contract purportedly assigned by a defense contractor to a third party.[16]

The Anti-Assignment Act is not an absolute proscription, however, since there are exceptions under which a government contract can be assigned to a third party.[17] For example, transfers or assignments occurring by "operation of law" are exempt from the Anti-Assignment Act's application, including transfers occurring incidental to corporate mergers, consolidations or reorganizations, assignments by judicial order, transfers by will and intestacy, bankruptcy transfers and assignments for the benefit of creditors.[18]

The Anti-Assignment Act also includes an exception for assignment of the right to payment under a government contract to a financing institution[19] and, of course, the government may consent to assignment, either under what courts have termed the waiver exception[20] or as implemented in the Federal Acquisition Regulation in the case of acquisitions structured as asset purchases, which require a formal novation.[21] Thus, although the Anti-Assignment Act may not be an

Section 365(f) of the Bankruptcy Code sets forth the general rule that a debtor may assume and assign an executory contract or unexpired lease, notwithstanding a contractual provision to the contrary that prohibits, restricts or conditions such assignment.

outright prohibition on assignment given its various exceptions, it clearly restricts a contractor's ability to freely assign a government contract.

Most courts that have considered the issue have concluded that the Anti-Assignment Act is an applicable law prohibiting or restricting assignment[22]; this has resulted in rulings in hypothetical test jurisdictions prohibiting defense contractor debtors from assuming government contracts in bankruptcy.[23]

However, as previously noted, the application of the hypothetical test to an anti-assignment provision in a government contract should not interfere with a prime contractor debtor's ability to perform under the agreement during the administration of the bankruptcy proceeding. Every effort should be made during the bankruptcy proceeding to obtain the government's consent to assumption of the agreement, although it may be necessary to re-negotiate pricing if the market has moved in the prime contractor debtor's favor since the effective date of the agreement.

IMPACT OF THE ACTUAL TEST ON ANTI-ASSIGNMENT PROVISIONS

Not all courts that have construed Sections 365(c) and 365(e)(2) have agreed that the provisions impose a "hypothetical test" prohibiting the assumption of an agreement in cases in which the agreement could not be assigned to a third party on a non-consensual basis because of an applicable non-bankruptcy law prohibiting or restricting assignment. These courts, including the 1st and 5th circuits and a majority of lower courts, have adopted what has come to be known as the "actual test." These courts have concluded that the exception to the general rule allowing assignment of agreements notwithstanding anti-assignment provisions is only triggered when the debtor *actually* seeks to assign the agreement and is not implicated by an assumption of the agreement by the debtor. These courts focus on the following language in Section 365(c) of the Bankruptcy Code:

> The trustee may not assume or assign any executory contract ... if ... (1)(A) applicable law excuses [the counterparty] from accepting performance from or rendering performance to an entity *other than the debtor or the debtor in possession* ... and (B) [the counterparty] does not consent to *such* assumption or assignment.[24]

The opaque language in the Bankruptcy Code's statutory exceptions to the general rules overriding anti-assignment and ipso facto provisions has resulted in a split among the circuits.

The actual test is premised on the interrelation between subparagraphs (A) and (B). In the circuits adopting this test, the courts conclude that the reference to the counterparty's lack of consent to *such* assumption or assignment in subpara-graph (B) refers only to an assumption by, or assignment to, an entity *other than the debtor or debtor-in-possession* (as specified in subparagraph (A)).

Since an assumption in and of itself does not involve a transfer to a third party, courts in actual test jurisdictions conclude that the trustee may assume an agreement, as long as the trustee does not *actually* seek to assign that agreement to a third party (*i.e.*, a party other than the debtor or debtor-in-possession) over the objection of the counterparty and in contravention of an applicable non-bankruptcy law prohibiting assignment.[25]

IMPACT OF THE HYPOTHETICAL TEST ON *IPSO FACTO* PROVISIONS

Courts within jurisdictions that have adopted the hypothetical test have concluded that if an applicable non-bankruptcy law would excuse a counterparty from accepting performance from, or rendering performance to, the trustee or an assignee under the agreement, the debtor cannot override a contractual *ipso facto* provision. This is the case even if the debtor has no intention of assigning the agreement to any such third party. These courts focus on the following language in Section 365(e)(2)(A) of the Bankruptcy Code:

> [The debtor's ability to override an *ipso facto* provision] does not apply to an executory contract ... of the debtor, ... if ... applicable law excuses [the counterparty] from accepting performance from or rendering performance to the trustee or to an assignee of such contract ...; and ... [the counterparty] does not consent to such assumption or assignment.[26]

Defense supply and services contracts are governed by the FAR and do not contain *ipso facto* provisions, although such provisions may be included in other government contracts.[27] We are aware of no published decisions in which a court in a hypothetical test jurisdiction has considered the Anti-Assignment Act in determining the enforceability of an *ipso facto* provision against a bankrupt prime defense contractor.

However, those cases analyzing the statute in the context of the anti-assignment provision of Section 365(c) of the Bankruptcy Code leave little doubt that a court would conclude that the Anti-Assignment Act is an applicable law prohibiting or restricting assignment. Therefore, in the event that a particular government contract contained an *ipso facto* provision, this could lead to a draconian result in a case in which a government contract provided for the termination of the agreement upon the prime contractor's bankruptcy filing. Unlike the case of an anti-assignment provision (in which the existence of the Anti-Assignment Act should not interfere with a debtor's enjoyment of the benefits of the agreement prior to assumption), application of the hypothetical test to a properly drafted *ipso facto* provision could well result in the termination of the agreement immediately upon a filing of a voluntary bankruptcy case by a prime contractor.

If an *ipso facto* provision requires the counterparty to issue a notice of termination to the debtor, the counterparty will be required to file a motion seeking authority to lift the automatic stay in order to issue the notice. In such cases, a debtor may be able to persuade the court to deny the counterparty's motion on the grounds that "cause" does not exist to grant relief from the stay, since the debtor stands ready, willing and able to perform under the agreement, and the counterparty's interests thereunder will remain adequately protected. However, in cases in which the parties have drafted an *ipso facto* provision to be self-executing upon the bankruptcy filing (without requiring the issuance of notice of the termination), a court in a hypothetical jurisdiction would probably conclude that the agreement automatically terminated immediately upon the bankruptcy filing.

The hypothetical test is premised on the proscription against assumption or assignment.

IMPACT OF THE ACTUAL TEST ON *IPSO FACTO* PROVISIONS

Courts within jurisdictions that have adopted the actual test have concluded that the exception to the general rule allowing debtors to override contractual *ipso facto* provisions does not apply unless and until the debtor, acting through a trustee, *actually* seeks to assume the agreement, or the debtor *actually* seeks to assign the agreement to a third party. These courts focus on the following language in Section 365(e)(2)(A) of the Bankruptcy Code:

> [The debtor's ability to override an *ipso facto* provision] does not apply to an executory contract ... of the debtor, ... if ... applicable law excuses [the counterparty] from accepting performance from or rendering performance to the trustee or to an assignee of such contract ...; *and* ... [the counterparty] *does not consent* to such assumption or assignment.[28]

Emphasizing the language in the statute referring to the counterparty's lack of consent to assignment, courts in actual test jurisdictions have found that the *ipso facto* provision exception is not triggered, unless a trustee is appointed to displace the debtor-in-possession and actually proposes to assume the agreement, or the debtor actually proposes to assume and assign the agreement to a third party over the objection of the counterparty.

For example, in *In re Mirant Corp.*, the 5th Circuit considered the Anti-Assignment Act in the context of an *ipso facto* provision in a government contract (albeit not a defense contract and one not governed by the FAR). The 5th Circuit adopted the actual test and concluded that a counterparty could not terminate an executory contract on the grounds that applicable law would prohibit assignment in cases in which the debtor had not actually proposed to assign the agreement to another party.[29]

Thus, in cases in which the actual test applies, so long as a trustee has not been appointed to displace the debtor's management, a debtor will ordinarily be able to stave off the enforcement of *ipso facto* provisions and assume agreements notwithstanding the existence of *ipso facto* provisions and applicable laws prohibiting or restricting assignment.

Unlike in a hypothetical test jurisdiction, where a self-executing *ipso facto* provision calling for the automatic termination of the agreement upon a bankruptcy filing is likely to be deemed effective, a debtor in an actual test jurisdiction should be able to enjoy the benefits of the agreement. The debtor should be able to circumvent enforcement of an *ipso facto* provision so long as a trustee (rather than a debtor-in-possession) is not seeking to assume the agreement and the debtor does not seek to assign the agreement to a third party.

TERMINATION-FOR-CONVENIENCE PROVISIONS

Another issue that may affect a prime defense contractor's ability to enjoy the benefits of an agreement is the existence of a "termination for convenience" provision. Defense contracts — including those for procurement, construction and research and development — are generally governed by the FAR, which provides that the government can terminate an agreement for convenience.

Although the Bankruptcy Code does not expressly invalidate termination-for-convenience provisions, courts have held that a counterparty may not send a notice of termination without first seeking relief from the automatic stay in the bankruptcy court.[30]

A debtor in a hypothetical test jurisdiction must proceed with caution.

Some courts have held that a provision allowing a party to terminate a contract for convenience is not in itself sufficient cause to grant stay relief and that a counter-party must still meet the requirements of Section 362(d)(1) of the Bankruptcy Code, which requires a movant to establish "cause" to grant relief from the automatic stay.[31] As a result, debtors in both hypothetical and actual test jurisdictions have often been able to persuade the court to deny a counterparty's request to modify the automatic stay to permit the counterparty to terminate the agreement.

Further, debtors in actual test jurisdictions sometimes have been able to preclude a counterparty from enforcing a termination-for-convenience provision on the basis that the counterparty's real reason for termination was the debtor's bankruptcy filing, which runs afoul of Section 365(e)(1) of the Bankruptcy Code.[32] For this reason, it is not unusual for a debtor in an actual test jurisdiction to attempt to draw a counterparty out to explain why it is exercising a termination-for-convenience provision. The debtor may do so on the chance that the counterparty will reveal that its real motivation for exercising the provision is the bankruptcy filing or the debtor's financial condition generally, in violation of Section 365(e)(1).

CONCLUSION

Although debtors ordinarily have the power to override contractual prohibitions on assignment and to block the enforcement of *ipso facto* provisions, such power is limited in cases in which there exists an applicable non-bankruptcy law prohibiting or restricting assignment. In the case of the bankruptcy of a prime defense contractor, the federal Anti-Assignment Act will generally serve as such an applicable non-bankruptcy law.

In jurisdictions that have adopted the actual test, the existence of the Anti-Assignment Act will serve only to limit the debtor's ability to assign a government contract to third parties, but it will not impair the debtor's ability to enjoy the benefits of the agreement during the bankruptcy proceeding or to assume the agreement in connection with a plan of reorganization.

In jurisdictions that have adopted the hypothetical test, however, the Anti-Assignment Act may impose a significant problem that could require a debtor to provide substantial concessions to the United States in order to obtain the government's consent to the assumption of an agreement under the debtor's plan of reorganization (although, in the ordinary case, it should not interfere with the debtor's enjoyment of the benefits of the agreement during the administration of the bankruptcy proceeding).

Further, in the event that a government contract contained a self-executing *ipso facto* provision triggered upon the contractor's bankruptcy filing, the Anti-Assignment Act will probably result in the automatic termination of the contract if a prime contractor has filed for bankruptcy in a hypothetical test jurisdiction. However, in cases in which the *ipso facto* provision is not

self-executing, a prime contractor that files for bankruptcy in a hypothetical test jurisdiction may be able to preclude the government from terminating the agreement. The contractor may do so by persuading the court to deny the government's request to modify the automatic stay (to permit it to issue a notice of termination) on the basis that the debtor stands ready to perform the agreement and because the interests of the government will remain adequately protected while performance is completed.

NOTES

[1] The Bankruptcy Code does not define "executory contract." Although courts have utilized a variety of approaches in determining whether a contract is executory, many courts have adopted the Countryman definition, which defines an executory contract as "a contract under which the obligations of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other." Vern Countryman, *Executory Contracts in Bankruptcy: Part I,* 57 MINN. L. REV. 439, 460 (1973).

[2] The automatic stay, arguably the most significant power, is triggered immediately upon the commencement of the bankruptcy proceeding and is a worldwide injunction barring virtually every action against a debtor and its property. *See* 11 U.S.C. § 362(a).

[3] *See id.* § 365.

[4] *Adamowicz v. Pergament (In re Lamparter Org. Inc.),* 207 B.R. 48, 52 (E.D.N.Y. 1997) ("[T]he power given the debtor in possession or trustee to assume or reject executory contracts is intended to enable him to make a new decision as to the wisdom of the contract in light of the changed circumstances of bankruptcy or conversion, as if he were entering into a new contract.") (quotation omitted).

[5] *Adventure Res. Inc. v. Holland,* 137 F.3d 786, 798-799 (4th Cir. 1998) (breach of an assumed executory contract results in an administrative priority claim). There is, however, a statutory limit on post-assumption rejection damages in the case of non-residential real property leases. *See* 11 U.S.C. § 503(b)(7).

[6] In 2005, Congress amended the Bankruptcy Code to, among other things, require that a debtor make a decision regarding the assumption of non-residential real property leases on the earlier of plan confirmation or 120 days after an order for relief has been entered in the case (with an extension of up to 90 days for cause). *See id.* § 365(d)(4). In connection with the acceleration of the decision-making process in the case of non-residential real property leases, Congress also added a limitation to the amount of the administrative claim resulting from the debtor's rejection of a previously assumed non-residential real property lease. *See id.* § 503(b)(7).

[7] *See id.* § 365(f).

[8] Upon rejection, outstanding amounts owed as of the bankruptcy filing, together with damages resulting from the debtor's breach of its ongoing obligations under the agreement, are treated as prepetition general unsecured claims. *See id.* § 365(g).

[9] The archetypical example of a contract not assignable under applicable non-bankruptcy law is a personal services contract. Because a personal services contract cannot be assigned to a third party outside of bankruptcy, the counterparty can both reject the debtor's proposed assumption and assignment, and enforce any contractual right to terminate based upon the debtor's bankruptcy filing or financial condition. *See In re Antonelli,* 148 B.R. 443, 448 (D. Md. 1992) (noting that "personal services" contracts cannot be assigned under Section 365(c)).

[10] 11 U.S.C. § 365(c) (emphasis added).

[11] *See RCI Tech. Corp. v. Sunterra Corp. (In re Sunterra Corp.),* 361 F.3d 257 (4th Cir. 2004); *Perlman v. Catapult Entm't (In re Catapult Entm't),* 165 F.3d 747 (9th Cir. 1999); *City of Jamestown v. James Cable Partners (In re James Cable Partners),* 27 F.3d 534, 537 (11th Cir. 1994); *In re West Elecs.,* 852 F.2d 79, 83-84 (3d Cir. 1988).

[12] *See In re Kazi Foods of Mich.,* 473 B.R. 887 (Bankr. E.D. Mich. 2011) (adopting hypothetical test and denying debtor's assumption motion, which motion was filed nearly four months after the bankruptcy case was first commenced); *In re Access Beyond Techs.,* 237 B.R. 32 (Bankr. D. Del. 1999) (adopting the hypothetical test and denying debtor's assumption motion more than 10 months after the bankruptcy cases were first commenced).

[13] *See West Elecs.,* 852 F.2d at 83-84 (granting stay relief to allow the counterparty to terminate the agreement); *In re Planet Hollywood Int'l,* 2000 WL 36118317, at *10 (D. Del. Nov. 21, 2000) (same); *United States v. TechDyn Sys. Corp. (In re TechDyn Sys. Corp.),* 235 B.R. 857, 864 (Bankr. E.D. Va. 1999) (same).

[14] *See West Elecs.,* 852 F.2d at 80 (counterparty suspended contract because of what it considered to be serious irregularities in debtor's accounting procedures and delivery and payment delinquencies); *Planet Hollywood,* 2000 WL 36118317 at *3 (counterparties asserted that debtors could not cure

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outstanding defaults or provide adequate assurance of future performance); *TechDyn,* 235 B.R. at 859 n.2 (counterparty asserted that debtor was unable to cure the present defaults or provide adequate assurance of future performance).

[15] *See In re Hernandez,* 287 B.R. 795, 800 (Bankr. D. Ariz. 2002) (allowing the contract to ride through the bankruptcy, but noting that a contract that is not assumed is not entitled to certain benefits afforded by Section 365; these benefits include insulation from *ipso facto* provisions or the right to cure defaults).

[16] 41 U.S.C. § 15(a) ("No contract or order, or any interest therein, shall be transferred by the party to whom such contract or order is given to any other party, and any such transfer shall cause the annulment of the contract or order transferred, so far as the United States is concerned."). The statute further provides that "[a]ll rights of action, however, for any breach of such contract by the contracting parties are reserved to the United States." *Id. See also* 48 C.F.R § 42.12.

[17] *Liberty Ammunition Inc. v. United States,* 101 Fed. Cl. 581, 587 (2011) ("courts have recognized a number of exceptions to the Anti-Assignment Act under which a government contract can be validly assigned to another party").

[18] *See Webster v. United States,* 90 Fed. Cl. 107, 116 (2009); *Holland v. United States,* 62 Fed. Cl. 395, 400 (2004); *Johnson Controls World Servs. v. United States,* 44 Fed. Cl. 334, 343 (1999).

[19] 41 U.S.C. § 15(b) (providing an exception where "the moneys due or to become due from the United States ... under a contract providing for payments aggregating $1,000 or more, are assigned to a bank, trust company or other financing institution").

[20] *See Liberty Ammunition,* 101 Fed. Cl. at 588.

[21] *See* 48 C.F.R. § 42.1204(a) (the government "may, when in its interest, recognize a third party as the successor in interest to a government contract when the third party's interest in the contract arises out of the transfer of — (1) All of the contractor's assets; or (2) The entire portion of the assets involved in performing the contract"). The FAR further provides that, in the case of an asset purchase, there may be change-of-ownership issues that the parties should address in a formal novation agreement. *Id.* at § 42.1204(b).

[22] *But see Bonneville Power Admin. v. Mirant Corp. (In re Mirant Corp.),* 440 F.3d 238, 253 (5th Cir. 2006), in which the court adopted the actual test, but noted in dicta that the federal Anti-Assignment Act might not be considered an "applicable law" prohibiting assignment until an actual assignment was proposed that did not fall within the statutory exceptions to the Anti-Assignment Act's general prohibition on the assignment of federal contracts (*e.g.,* the exception for assignment to a financing institution). The 5th Circuit did not consider, however, whether the Anti-Assignment Act might constitute an applicable law restricting assignment. Although the Anti-Assignment Act might not constitute an applicable law prohibiting assignment, given the exceptions to the general prohibition found within the statute and in the case law, the better interpretation of the Anti-Assignment Act is that, at the very least, it constitutes applicable law restricting assignment.

[23] *See, e.g., West Elecs.,* 852 F.2d 79 (adopting the hypothetical test and concluding that a contract could not be assumed because the Anti-Assignment Act as "applicable law" made assignment impermissible if it would foreclose assignment by the prepetition debtor to another defense contractor); *TechDyn,* 235 B.R. 857; *In re Plum Run Serv. Corp.,* 159 B.R. 496 (Bankr. S.D. Ohio 1993); *United States v. Carolina Parachute Corp. (In re Carolina Parachute Corp.),* 108 B.R. 100 (M.D.N.C. 1989), *aff'd in part and vacated in part on other grounds,* 907 F.2d 1469 (4th Cir. 1990).

[24] 11 U.S.C. § 365(c) (emphasis added).

[25] *See Institut Pasteur v. Cambridge Biotech Corp.,* 104 F.3d 489, 493 (1st Cir. 1997).

[26] 11 U.S.C. § 365(e)(2)(A).

[27] *See infra,* n.30.

[28] 11 U.S.C. § 365(e)(2)(A).

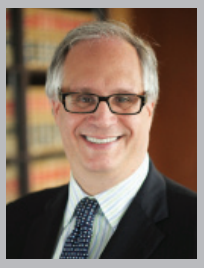
[29] *See In re Mirant Corp.,* 440 F.3d at 247–51 (5th Cir. Feb. 13, 2006). *See also In re Hartec Enters.,* 117 B.R. 865, 872 (Bankr. W.D. Tex. 1990), *vacated by settlement,* 130 B.R. 929 (W.D. Tex. 1991) (adopting the "actual test" because it "better fulfills the purposes" of the Anti-Assignment Act, under which the "prohibition on a transfer is not triggered so long as it is basically the same entity performing under the contract").

[30] *See, e.g., In re Enron Corp.,* 300 B.R. 201, 211-212 (Bankr. S.D.N.Y. 2003) (holding that a contract cannot be terminated without first seeking stay relief, regardless of the existence of a provision in the contract allowing for termination); *In re Redpath Computer Servs.,* 181 B.R. 975, 978 (Bankr. D. Ariz. 1995) (finding that "the Bankruptcy Code neither enlarges the contract rights of a debtor, nor prevents termination of a contract by its own terms," but "[a]n executory contract that is property of the estate can only be terminated after a grant of relief from the stay"). *But see Valley Forge Plaza Assocs. v. Schwartz,*

114 B.R. 60 (E.D. Pa. 1990) (holding that the Bankruptcy Code does not prevent termination of a contract by its own terms, and "the ability to terminate a contract on its terms survives bankruptcy").

[31] *See In re The Elder-Beerman Stores Corp.*, 195 B.R. 1012, 1018 (Bankr. S.D. Ohio 1996) ("The conditions under Section 362(d) govern relief from the stay, and when those conditions are not met, courts have not hesitated to leave the stay intact, even in the presence of 'at will' termination clauses."); *Coaldale Energy LP v. Lehigh Coal & Navigation Co.* (*In re Lehigh Coal & Navigation Co.*), 2009 WL 1657096, at *3-4 (Bankr. M.D. Pa. June 12, 2009) (holding that the debtor's ability to terminate the agreement at will "may not be sufficient to constitute cause to grant relief," but finding that cause existed to grant stay relief on other grounds).

[32] *See In re Nat'l Hydro-Vac Indus. Servs.*, 262 B.R. 781, 786 (Bankr. E.D. Ark. 2001) (holding that a contract termination clause did not enable a bank to terminate on the basis of the debtor's Chapter 11 filing, and noting that "[i]n a commercial contractual relationship, terminable-at-will provisions must be exercised in good faith"); *In re B. Siegel Co.*, 51 B.R. 159, 163 (Bankr. E.D. Mich. 1985) (convenience termination clause does not confer an unrestricted right to cancel a contract, when the only reason for its invocation is the debtor's bankruptcy filing, because this would nullify the remedial policy of Section 365(e)(1)).



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