

Lehman Bankruptcy Court Holds Contractual Right to Triangular Setoff Unenforceable in Bankruptcy and Not Protected by Safe Harbors

October 6, 2011 | Articles & Books

In a recent decision issued in the Lehman Brothers Inc. SIPA proceeding in the Southern District of New York, *In re Lehman Brothers Inc.*, Case No. 08-01420 (JMP) (SIPA), slip op. (Bankr. S.D.N.Y. Oct. 4, 2011), Bankruptcy Judge James M. Peck held that a contractual right to effect a cross-affiliate setoff is unenforceable in bankruptcy. The court found that mutuality is a requirement for both common law and contractual setoff under Section 553 of the Bankruptcy Code, and that the contract did not create mutuality for purposes of Section 553. The court further held that the safe harbor provisions for swaps and other derivatives contracts in the Bankruptcy Code do not permit a party to exercise a contractual right to setoff where there is no mutuality.

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