Secured Property in Chapter 7
(In Which the Secured Creditor Says, "Get Me Outa Here!")

- Modification of Stay and Abandonment of Collateral
  David R. Shook
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- Reaffirmation, Avoidance, Redemption, Surrender
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- Marshaling of Assets
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  Bay City MI

- Selected Provisions of the Bankruptcy Abuse Prevention And Consumer Protection Act of 2005 For Secured Creditors in Chapter 7 Cases
  Honorable Susan V. Kelley
  U.S. Bankruptcy Court, E.D. of WI

REAFFIRMATION, AVOIDANCE, REDEMPTION, SURRENDER

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DEBTOR'S DUTIES:

Pursuant to 11 U.S.C. §521, "The debtor shall — ... (2) if an individual debtor's schedule of assets and liabilities includes consumer debts which are secured by property of the estate – (A) within thirty days after the date of the filing of a petition under chapter 7 ... or on or before the date of the meeting of creditors, whichever is earlier, or within such additional time as the court, for cause, within such period fixes, the debtor shall file with the clerk a statement of his intention with respect to the retention or surrender of such property and, if applicable, specifying that such property is claimed as exempt, that the debtor intends to redeem such property, or that the debtor intends to reaffirm debts secured by such property; (B) within forty-five days after the filing of a notice of intent under this section, or within such additional time as the court, for cause, within such forty-five day period fixes, the debtor shall perform his intention with respect to such property, as specified by sub-paragraph (A) ..."

Accordingly, within forty-five days after the filing of the notice of intent, the debtor must perform that intention. If the debtor fails to perform, what is the remedy to the secured creditor"? Unfortunately, current §521 is silent as to what a remedy might be for the debtor's failure to perform his stated intention. Obviously, however, the most appropriate remedy would be simply to file a motion to modify stay pursuant to 11 U.S.C. §362, and retake possession of the collateral. But, see Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, discussed hereafter.

AVOIDANCE OF LIEN

Pursuant to 11 U.S.C. §522(f), the debtor may avoid the fixing of a lien on the debtor's interest in property to the extent that the lien impairs the debtor's exemption if the lien is either a judicial lien (with certain exceptions) or a nonpossessory, nonpurchase money security interest in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry held primarily for the personal, family or household use of the debtor or a dependent; implements, professional books, or tools of the trade of the debtor or the

trade of a dependent of the debtor; or professionally prescribed health aids for the debtor or a dependent of the debtor.

In order for the debtor to avoid the fixing of a lien, the court must determine the exemption to which the debtor is entitled and must value the property upon which the lien is claimed. In addition, the court must value any other liens on the said property.

REAFFIRMATION AGREEMENT

Pursuant to 11 U.S.C. §524(c), the debtor and secured creditor may enter into a reaffirmation agreement which will reinstate personal liability of the debtor only if (1) the agreement is entered into prior to the granting of the discharge, (2)(A) the agreement contains a clear and conspicuous statement which advises the debtor that the agreement may be rescinded at any time prior to discharge or within sixty (60) days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission; and (B) such agreement contains a clear and conspicuous statement which advises the debtor that such agreement is not required under Title 11, under non-bankruptcy law or under any agreement not in accordance with the provisions of §524(c); (3) such agreement has been filed with the court and, if applicable, accompanied by a declaration or an affidavit of the attorney that represented the debtor during the course of negotiating the reaffirmation agreement that (A) the agreement represents a fully informed involuntary agreement by the debtor; (B) the agreement does not impose an undue hardship on the debtor or a dependent of the debtor; and (C) the attorney fully advised the debtor of the legal effects and consequences of entering into the agreement and any default under the said agreement; (4) the debtor has not rescinded such agreement in accordance with the time provisions contained herein; (5) the provisions of subsection (d) have been complied with (which requires the appearance of a non-represented debtor in open court to be examined by the court as to the provisions of sub-section (c)).

REDEMPTION:

Pursuant to 11 U.S.C. §722, an individual debtor may redeem tangible personal property intended primarily for personal, family or household use, from a lien securing a dischargeable consumer debt if such property is exempted under §522 or has been abandoned under §554 by paying the holder of such lien the amount of the allowed secured claim of such holder that is secured by such lien.

RELEVANT CASE LAW AS TO REDEMPTION

In re Smith, 307 B.R. 912 (B.C.N.D. Ill. 2004) Honorable Jack B. Schmetterer held, for purposes of redemption under §722, the replacement value as provided in Associates Commercial Corp. V. Rash 520 U.S. 953 (1997) is controlling, discounted to eliminate inapplicable elements of value, which discount shall be 10% below established retail value absent contrary evidence.

On appeal to the United States District Court, Northern District of Illinois, Eastern Division, Honorable Ruben Castillo, District Judge, in Smith v. Household Automotive Finance Corp. held that Rash does not require the debtor to pay the property's replacement value in a redemption proceeding inasmuch as Rash dealt with the cram down provisions of a Chapter 13 plan. Judge Castillo remanded the case to Judge Schmetterer.

In re Tripplett, 256 B.R. 594 (B.C., N.D. Illinois 2000), Honorable Eugene Wedoff, presiding, held that Rash's replacement value is not applicable since Rash was a cram down case under Chapter 13 and redemption involves immediate payment. Held that wholesale or liquidation value of the collateral is the appropriate price at which a debtor can redeem the property.

In re Stark, 311 B.R. 750 (B.C.,N.D. Illinois 2004), Honorable John H. Squires, presiding, held that a balancing approach is appropriate and absent other persuasive evidence the average of wholesale and retail values will be the value at which the debtor may redeem property from a lien.

In re Smith, 313 B.R. 785 (B.C.,N.D. Indiana 2004), Judge Klingeberger held that valuation standard for §722 will be the average trade in value of the Official Used Car Guide of the NADA, subject to two exceptions, i.e. adjustments of value in the NADA guide for condition, accessories, or mileage and testimony of expert witnesses as qualified under the Federal Rules of Evidence. In addition, the court held that the relevant date for determining the value is the date of filing of the petition.

In re Edwards, 901 F.2d 1383 (7th Cir. 1990) requires Chapter 7 debtors in the Seventh Circuit to perform one of three options regarding personal property: surrender, reaffirm under §524(c) or redeem under §722.

Unlike the Seventh Circuit, a fourth option, i.e. retaining the collateral and keeping current on all loan payments has been permitted in the Second Circuit, In re Boodrow, 126 F.3d 43 (2d Cir. 1997) the Third Circuit, In re Price 370 F.3d 362 (3rd Cir. 2004) and the Ninth Circuit, In re Parker 139 F. 3d 668 (9th Cir. 1998).

SELECTED PROVISIONS OF THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005 (S.256)

SEC 203. DISCOURAGING ABUSE OF REAFFIRMATION AGREEMENT PRACTICES

Amends Section 524 to provide more extensive disclosures to the debtor including clear and conspicuous written terms identifying Amount Reaffirmed and Annual Percentage Rate and providing a Summary of Reaffirmation Agreement. Also includes advising the debtor that reaffirming an obligation is a "serious financial decision". Also requires advising the debtor that even if the debt is discharged and the debtor does not reaffirm the debt, any lien on property survives the discharge. Section 203 also adds section 158 to Chapter 9 of Title 18, authorizing FBI agents and United States Attorneys to address abusive reaffirmations of debt and materially fraudulent statements in bankruptcy schedules.

SEC 304. DEBTOR RETENTION OF PERSONAL PROPERTY SECURITY

Amends section 521(a) to provide that in a Chapter 7, the debtor must, within 45 days after the first meeting of creditors, either reaffirm the debt pursuant to sec 524(c) with respect to secured property or redeem the property from lien pursuant to sec 722. If the debtor fails to do so, the automatic stay is terminated as to the property of the debtor and the property is no longer property of the estate and the creditor may take whatever action under nonbankruptcy law available, unless the court determines upon motion of the trustee before the expiration of the 45 day period that the property is of consequential value to the estate.

SEC 305. RELIEF FROM THE AUTOMATIC STAY WHEN THE DEBTOR DOES NOT COMPLETE INTENDED SURRENDER OF CONSUMER DEBT COLLATERAL.

Amends sec 362 by terminating stay as to property of the debtor and the property is no longer property of the estate if the debtor does not timely file statement of intent and timely perform the stated intention, unless court determines upon motion of trustee that property is of consequential value to the estate.

SEC 306. GIVING SECURED CREDITORS FAIR TREATMENT IN CHAPTER 13

Amends sec 1325(a)(5)(B)(i) to provide that the holder of lien claim retains the lien until the earlier of payment of the underlying debt determined under nonbankruptcy law or discharge under sec 1328. Also provides that if the case is dismissed or converted the creditor retains the lien as recognized under nonbankruptcy law. Also prohibits use of sec 506 to strip the lien of a purchase money security interest in a motor vehicle if purchased within 910 days of the petition or one year for other personal property.

SEC 309. PROTECTING SECURED CREDITORS IN CHAPTER 13 CASES

This provision is intended to stop abusive conversions and amends sec 348 by providing that lien survives the conversion unless the full amount of the debt under nonbankruptcy law has been paid. Also amends sec 365 by providing that if a lease of personal property is not timely assumed or is rejected, the stay is automatically terminated. If lease is not assumed in Chapter 13 plan, the lease is deemed rejected at conclusion of hearing on confirmation. In Chapter 7, debtor may notify creditor in writing that debtor desires to assume lease at which time creditor may notify debtor that it is willing to have lease assumed and may condition assumption on cure of default. Secs 362 and 524 are not violated by notification to debtor and negotiation of cure. Also amends sec 1326 by providing adequate protection payments to secured creditor within 30 days after filing of plan and/or payments to a lessor of leased property. Any payments so made shall be deducted from the payments necessary to Chapter 13 trustee and evidence of payment to secured creditor and/or lessor must be provided to trustee. Also requires debtor to provide evidence of insurance to secured creditor and/or lessor within 60 days after the date of filing of case.

SEC 313. DEFINITION OF HOUSEHOLD GOODS AND ANTIQUES

Amends sec 522(f) by defining household goods to include:

clothing, furniture, appliances, 1 radio, 1 television, 1 VCR, linens, china, crockery, kitchenware, education materials and equipment primarily for use of minor dependent children of debtor, medical equipment and supplies, furniture exclusively for use of minor children, or elderly or disabled dependents of debtor, personal effects (including toys and hobby equipment of minor dependent children and wedding rings) of debtor and dependents of debtor, and 1 personal computer and related equipment.

Definition of household goods does not include works of art (unless by debtor or dependent of debtor), electronic entertainment equipment worth more than $500 (except 1 t.v., 1 radio, and 1 VCR), items acquired as antiques worth more than $500, jewelry worth more than $500 (except wedding rings), and a computer, motor vehicle, boat, or motorized recreational device, conveyance, vehicle, watercraft, or aircraft.

SEC. 327. FAIR VALUATION OF COLLATERAL

Amends sec 506(a) by providing in a Chapter 7 or 13, the value of personal property securing an allowed secured claim shall be determined based upon replacement value as of the petition date without deduction for costs of sale or marketing. As to property acquired for personal, family or household purposes, replacement value shall mean the price a retail merchant would charge for property of that kind considering age and condition at time value is determined.

MARSHALING OF ASSETS

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I. WHAT IS MARSHALING?

A. Doctrine Based on Equity

The doctrine of marshaling of assets is based upon equity and traditionally benefits junior secured creditors. Generally, marshaling is applied when two or more secured creditors make claims against a debtor and the senior secured creditor can satisfy its claim from two or more of the debtor's assets, while the junior secured creditor can only reach one asset to satisfy its claim. In re Vermont Toy Works, Inc., 82 B.R. 258 (Bankr. D. Vt. 1987), reversed on other grounds. Federal Courts trace this principle from the seminal case of Meyer v United States, 375 U.S. 233, 11 L.E.D. 2d 293, 84 St. Ct. 318 (1963) and early English common law. Bankruptcy Courts have authority to order the marshaling of funds under their equity jurisdiction, pursuant to 28 U.S.C. §1781. The Supreme Court in Meyer

stated that the doctrine was to be used to prevent "arbitrary action" by a senior creditor who has the potential to destroy the rights of junior lien holders.

B. Setting

Most often, marshaling is found in a setting where one creditor has a senior lien in all the debtor's assets and other creditors exist who have liens subordinate to the senior liens on some, but not all, of the debtor's property. In that instance, junior lien holders may demand that the senior lien holder resort first to collateral it holds exclusively to satisfy its claims in order to protect the junior lien holder's interest.

II. HOW IS MARSHALING APPLIED?

A. General Application

Generally speaking, the Courts will allow application of the doctrine where multiple secured creditors claim against a common debtor; the senior creditor can reach two or more funds/interests held by this debtor; and where the junior creditors can only reach one fund and/or interest of this debtor. If marshaling is ordered, it requires that the senior creditor first work to satisfy its claim from the fund that the junior creditor cannot access before the senior creditor is allowed to satisfy the claim from the common fund and/or interest of this debtor. Obviously, marshaling is most commonly utilized in those instances which involve collateral issues under 11 U.S.C. §363.

B. Three Elements Must Be Present

1. The existence of two or more creditors;

2. The existence of two funds belonging to a debtor; and

3. Only one of the creditors having access to both funds/interests. Imperial House Motel of Canton, Ltd. v. Trident Fin Corp., (In re Parks Imperial Canton, Ltd.), No. 93-61004, 95-6084, 1997 W.L. 391478, at *7, (Bankr. N.D. Ohio 1987); In re C&B Oil Co., 72 B.R. 228, 230 (Bankr. N.D. Ohio 1987).

C. Possible Fourth Element, No Injustice

"The power to compel a party who has two funds to resort to the one on which others have no claim will only be exercised when it will work no injustice to any party connected with the litigation." In re Gibson Group, Inc., 151 B.R. 133, 134 (Bankr. S.D. Ohio 1993) (quoting Century Trust Co., N.A. v. Burchett (In re Willson Dairy Co.), 30 B.R. 67 (Bankr. S.D. Ohio 1983). Marshaling of property does not occur where equity would consider the marshaling unjust. Francis v Herren, 101 N.C. 497, 8 S.E. 353 (1888).

D. What Law Governs the Order of Marshaling

Bankruptcy Courts have authority to order the marshaling of funds under their equity jurisdiction, 28 U.S.C. §1781, anytime the three criteria articulated in Imperial House, supra are present. Some authority exists which indicates that state law may control as to the application of doctrine of marshaling. (See In re Robert E. Derecktor of R.I., Inc., 150 B.R. 296 (Bankr. D.R.I. 1993); In re Gibson Group, Inc., 151 B.R. 134, citing Ohio v. Collins (In re Madeline Marie Nursing Homes, 694 F. 2d 433, 438-39 (6th Cir. 1982). Also see Butner v. United States, 440 U.S.

48, 55, 99 S. Ct. 914, 918, 59 L.Ed. 2d 136 (1979) (stating that unless federal interest requires otherwise, state law governs property interest).

E. Elements Established by Clear and Convincing

The party requesting marshaling must establish the elements by clear and convincing evidence. In re United Retail Corp., 33 B.R. 150, 154 (Bankr. D.H.A.W. 1983).

F. Common Debtor Examined

1. In re C&B Oil Co., the court found that the trustee had standing to seek a marshaling order, but the trustee's request was denied for lack of common debtor. The court would not allow the trustee to compel the bank to look to personal assets of a corporate guarantor before proceeding against corporate debtors. Lack of the common debtor element has given cause to deny marshaling In re San Jacinto Glass Indus., 93 B.R. 934, 941 (Bankr. S.D. Tex. 1988) (bankruptcy court should adhere to common debtor requirement except in extraordinary cases); Cullen v. Revere Copper & Brass, Inc. (In re John I. Paulding, Inc.), 76 B.R. 7 (Bankr. D. Mass. 1987) (marshaling is only proper where both funds are held by debtor); In re Dealer Support Servs. Int'l, 73 B.R. 763, 764-65 (Bankr. E.D. Mich. 1897) (marshaling not allowed where funds held separately by debtor and guarantor).

2. The Bankruptcy Court in South Carolina declined to issue its order for marshaling of assets of a Chapter 7 non-debtor spouse to pay federal and

state tax claims noting that the creditor failed to satisfy the "common debtor" requirement for marshaling in addition to the fact that the marshaling of the non-debtor spouse's assets would not have been equitable. In re Field, 1998 WL 690026 (Bankr. D.S.C., Judge Wm. Thurmond Bishop).

G. Exceptions to Common Debtor Element

1. Based on equitable principals, the courts have recognized exceptions to the "common debtor" element in marshaling cases. (See Telefest Inc. v. VU-TV, 591 F. Supp. 1368, 1382 (D. N.J. 1984) (citing Mastan Co. v. S.S. Sapphire Sandy, 293 F. Supp. 68, 74 (D. N.J. 1968), aff'd., 418 F. 2d 177 (3d Cir. 1969), cert. denied, 397 U.S. 1009 (1970).

2. The courts have also expanded the common debtor element by recognizing when a non-debtor's property was pledged to secure the debtor's obligation as a capital contribution to the debtor, In re Wm. Pietsch Co., 200 B.R. 207, 210-11 (Bankr. E.D. Wis. 1996) (citing in Multiple Servs. Indus. Inc. 18 B.R. 635, 636 (Bankr. E.D. Wis. 1982)).

3. Marshaling also invoked in absence of the traditional "common debtor" where the non-debtor engaged in fraudulent conduct and/or was unjustly enriched. See In re Field, 226 B.R. 178, 183 (Bankr. D. S.C. 1998); Fundex Capital Corp. v. Balaber-Strauss (In re Tampa Chain Co.), 53 B.R. 772, 778-79 (Bankr. S.D.N.Y. 1985).

4. Marshaling has been applied against non-debtor shareholders in order to preserve distribution to the unsecureds. In re Jack Green's Fashions for Men Big & Tall, Inc., 597 F.2d 130, 133 (8th Cir. 1979).

III. WHO MAY INVOKE MARSHALING?

A. Junior Lien Holders

Marshaling is most commonly invoked by junior secured creditors.

B. Bankruptcy Trustees

1. Courts have not been in agreement as to whether the bankruptcy trustee has a right to seek an order compelling a senior secured creditor to marshal its collateral so as to benefit the bankruptcy estate. See In First Nat. Mercantile Bank & Trust Co. v. Hazen, 96 B.R. 924 (W.D. Mo. 1988), where the bankruptcy trustee used a marshaling order against a senior lien holder who had a lien against the estate's inventory and a second mortgage on other property for which the estate had no interest. The senior creditor was compelled to pursue the second mortgage interest rather than the inventory. Compare First Nat. Mercantile Bank with matter of McElwaney, 40 B.R. 66, 70 (Bankr. M.D. Ga. 1984) where trustee was not provided with the power to invoke marshaling of assets, stating that the Bankruptcy Code does not vest the trustee with better rights than those belonging to the debtor. In the case of In re Jack Green's Fashions for Men

Big and Tall, Inc., 597 F. 2d 130 (8th Cir. 1979), the trustee was allowed to assert marshaling against a senior creditor in a manner that expands the doctrine and its traditional application. In re Vermont Toy Works, Inc., 82 B.R. 258 (Bankr. D. Vt. 1987), the court relied on the Uniform Commercial Code to show that a judicial lien creditor may be considered a secured party under state law, thereby finding that the trustee had authority to invoke the marshaling of assets doctrine. Yet, In the Matter of Dealer Support Services Intern, Inc., 73 B.R. 673 (Bankr. E.D. Mich. 1987), the trustee was not provided with an order to compel secured lender to proceed first against guarantors. Seventh Circuit granted the trustee standing in In re Koch Refining v. Farmer's Union Central Exchange, Inc., 831 F. 2d. 1339 (7th Cir. 1987), cert. denied, 108 Sup. Ct. 1077 (1988), while the Eighth Circuit denied the trustee standing to assert same In re Ozark Restaurant Equipment Co., Inc., 816 F. 2d. 1222 (8th Cir. 1987), cert. denied, 108 Sup. Ct. 147 (1987). More recently, the bankruptcy trustee, as a hypothetical lien holder under 11 U.S.C. §544(a), had standing to seek marshaling for the benefit of the estate, Official Comm. of Unsecured Creditors v. Lozinski (In re High Strength Steel Inc.), 269 B.R. 560, 573-74 (Bankr. D. Del. 2001).

2. In those instances where it appears that the courts may accept the trustee's standing to request marshaling of assets, the courts appear to pull back that right based upon failure of the trustee to establish all the common law

elements for marshaling. In re San Jacinto Glass Indus., 93 B.R. 934, 941 (Bankr. S.D. Tex. 1988) (bankruptcy court should adhere to common debtor requirement except in extraordinary cases); Cullen v. Revere Copper & Brass, Inc. (In re John I. Paulding, Inc.), 76 B.R. 7 (Bankr. D. Mass. 1987) (marshaling is only proper where both funds are held by debtor); In re Dealer Support Servs. Int'l, 73 B.R. 763, 764-65 (Bankr. E.D. Mich. 1987) (marshaling not allowed where funds held separately by debtor and guarantor).

C. Unsecureds Invoke Marshaling

1. While marshaling has most commonly been invoked by junior secured creditors, situations have arisen wherein it has been advantageous for unsecured creditors in bankruptcy to request marshaling and the courts have granted the request. See In re Hale, 141 Bankr. 225 (Bankr. ND Fla. 1992). Although the court in Hale acknowledged that traditionally only junior lienors may compel marshaling, the court held that unsecured creditors have standing to invoke the doctrine of marshaling of assets to compel mortgagees to look first to all their security for full satisfaction of their claim before they receive distribution as unsecured creditors.

2. Other cases have held that unsecured creditors do not have standing to request and subsequently receive a marshaling order. See In re Brazier Forest Prods., Inc., 921 F2d 2221, 223 (9th Cir. 1990) (only secured or lien creditors may assert marshaling, applying Washington state law); In re

Atlas Commercial Floors, Inc., 125 Bankr. 185, 188 (Bankr. ED Mich. 1991) and cases cited therein; In re Packard Properties, Ltd., 112 Bankr. 154, 158 (Bankr. ND Tex. 1990); In re Dealer Support Servs. Int'l, 73 Bankr. 763, 764 (Bankr. Ed Mich. 1987); In re Price, 50 Bankr. 226, 230 (Bankr. Ed Mich. 1985); In re Pittsburgh-Canfield Corp. v. Wheeling-Pittsburgh Steel Corp., 309 B.R. 277, 51 Collier Bankr. Cas. 2d 1873, 42 Bankr. Ct. Dec. 277, Bankr. L. Rep. P. 80,088, 2004 Fed App. 004P.

D. Reverse Marshaling

It may be possible for a bankruptcy trustee, as a hypothetical creditor, to block a junior lien holder's request for marshaling of assets where marshaling would provide the junior lien holder with collateral it never bargained for to the detriment of the general unsecureds. In re Center Wholesale, Inc., 759 F2d. 1440, 13 Bankr. Ct. Dec. (C.R.R. 163, 12 Collier Bankr. Cas. 2d (M.B.) 1107 9th Cir. 1985). However, neither a bankruptcy trustee nor a debtor-in-possession can force "reverse marshaling" of assets by forcing the senior lien holder to satisfy its claim on collateral which also secures the junior lien holder's interest when the senior lien holder has other collateral it may draw from first. In re Borges, 184 B.R. 874, 27 Bankr. Ct. D.E.C. (C.R.R. 701, 34 Collier Bankr. Cas. 2d (M.B.) 281 (Bankr. D. Conn. 1995).

IV. EFFECT OF SUBROGATION AND SUBORDINATION

A. Subrogation

In In re Lomb, 74 B.R. 711 (Bankr. W.D. Pa. 1987), a marshaling order was denied to the bankruptcy trustee because the estate would not benefit from the marshaling order compelling the creditor to proceed against a third party since the third party would be subrogated to creditor's rights against the estate pursuant to 11 U.S.C. §509(a) of the Bankruptcy Code. §509(a) provides:

> An entity that is liable with the debtor on, or that has secured, a claim of a creditor against the debtor, and that pays such claim, is subrogated to the rights of such creditor to the extent of such payment.

See In re Leviton Construction Co., 122 B.R. 530, 532 (Bankr. S.D. Ohio 1991).

B. Subordination

1. 11 U.S.C. §509(b)(1)(C) provides:

> Such entity is not subrogated to the rights of such creditor to the extent that – (1) a claim of such entity for reimbursement of contribution on account of such payment of such creditor's claim is – (C) subordinated under section 510 of this title.

2. 11 U.S.C. §510(c)(1) states:

> Notwithstanding subsections (a) and (b) of this section, after notice and a hearing, the court may – (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed interest to all or part of another allowed interest.

Thus, if misconduct by claimant results in injury to creditors or provides an unfair advantage to the claimant because of the result of misconduct, the

courts may equitably subordinate and allow marshaling despite the possibility of subrogation. See In re Vermont Toy Works, Inc., 82 B.R. 258 (Bankr. D. Vt. 1987). (Also see In re Dealers Support Services Int'l Inc., 73 B.R. 763 (Bankr. E.D. Mich. 1987); Stuhley v. U.S. Small Business Administration (In re United Medical Research, Inc.), 12 B.R. 941, 944 (Bankr. C.D. Cal. 1981).

V. CENTRAL STATES CASES DISCUSSING MARSHALING

In the Matter of Todd Michael Taylor, 289 B.R. 379 (Bankr. N.D. Ind., 2003)
In re Rich Supply House, Inc., 43 B.R. 68 (Bankr. N.D. Ill., 1984)
Herzog v. NBD Bank of Highland Park, 203 B.R. 80 (N.D. Ill., 1996)
In re William Duane Batterton, 2001 WL 34076431 (Bankr.C.D. Ill., 2001)
DuPage Lumber and Home Improvement Center Company v. George Pacific Corporation, 34 B.R. 737 (Bankr. D.C. Ill., 1983)

In re Wm. Pietsch Co., Inc., 200 B.R. 207 (Bankr. E.D. Wis., 1996)
In re Universal Electric Sigh Co., Inc., 255 B.R. 732 (Bankr. E.D. Wis., 2000)
In the Matter of Multiple Services Industries, Inc., 18 B.R. 635 (Bankr. E.D. Wis., 1982)
In re Bay Metro Glass Co., Inc., 101 B.R. 50 (Bankr. E.D. Wis., 1989)
In re C&B Oil Co., 72 B.R. 228, 230 (Bankr. N.D. Ohio 1987)
In re Leviton Construction Co., 122 B.R. 530, 532 (Bankr. S.D. Ohio 1991)
In re Parke Imperial Canton, Ltd., 1997 WL 391478 (Bankr. N.D. Ohio, 1997)
In re the Gibson Group, Inc., 151 B.R. 133 (Bankr. S.D. Ohio, 1993)
In the Matter of Willson Dairy Company, 30 B.R. 67 (Bankr. Ohio, 1981)
In re Atlas Commercial Floors, Inc., 125 B.R. 185 (Bankr. E.D. Mich., 1991)
In the Matter of Dealer Support Services International, Inc., 73 B.R. 763, 764-65 (Bankr. E.D. Mich., 1897)
In re Wilson L. Trickett, 14 B.R. 85 (Bankr. Mich., 1981)
In re Kathleen M. Wheeler, 252 B.R. 420 (Bankr. W.D. Mich., 2000)

SELECTED PROVISIONS OF THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005 FOR SECURED CREDITORS IN CHAPTER 7 CASES

Susan V. Kelley
U.S. Bankruptcy Judge, Eastern District of Wisconsin

1. Effect of Conversion from Chapter 13 to Chapter 7.

Under § 348(f)(1)(c), in a case converted from chapter 13 to chapter 7, a secured creditor retains the security interest until the full amount of the claim (as determined under applicable nonbankruptcy) law is paid in full. Unless a pre-petition default has been fully cured through the plan at the time of conversion, the default has the effect given under applicable nonbankruptcy law.

2. Treatment of Purchase Money Security Interests.

Under § 521(a)(6), in an individual debtor's chapter 7 case, with respect to personal property secured by a PMSI, within 45 days after the first meeting of creditors, the debtor must either reaffirm, redeem or surrender the property. If the debtor does not reaffirm or redeem within 45 days, the property is no longer property of the estate, unless court grants a motion filed by the trustee within the 45 day period stating that the property is of consequential value to the estate.

3. Debtor's Duty to Provide Tax Returns.

Pursuant to § 521(e)(2), not less than 7 days before the first date set for the meeting of creditors, the debtor must provide the trustee, and any creditor who has timely requested a copy, of the federal tax return for the most recent tax year preceding the filing for which a return was filed. The court must dismiss the case for failure to comply unless the debtor shows that the failure to comply was beyond the control of the debtor. Note: Guidelines are supposed to be promulgated to preserve the privacy of the tax returns, including restriction on access by creditors.

4. Dismissal for Failure to provide information.

According to § 521(l), the debtor's failure to provide any information required under § 521(a) within 45 days of the date of the petition results in automatic dismissal on the 46th day unless, a motion is filed within the 45 days by the debtor or the trustee.

5. Lien Avoidance on Exempt property.

The classification of household goods for purposes of avoiding liens that impair exemptions under § 522(f) has been severely restricted, e.g., one television, one vcr, one computer.

6. Collateral Valuation.

Under § 506(a), in an individual debtor's chapter 7 or 13 case, value is determined as the replacement value, disregarding costs of sale. For consumer goods, value is the price a retail merchant would charge considering the age and condition.

7. Reaffirmation.

Section 524(k) requires detailed disclosures to be made by a creditor before a reaffirmation agreement may be signed by the debtor, including the language that must be used. Debtor must state the amount of monthly take home pay and other income, current monthly expenses, and the amount available to make the payments on the debt being reaffirmed. There is a presumption of undue hardship under § 524(m) if the debtor's expenses plus the payment on the reaffirmed debt exceeds the income. This may be rebutted if the debtor identifies additional sources of funds to make the payment. This section does not apply where the creditor is a credit union.

8. Redemption.

Under § 722, the redemption price must be paid at the time of redemption.

9. Termination of Automatic Stay if Prior Case Dismissed.

Under § 362(c)(3) and (i), the stay is terminated 30 days after a petition is filed in a case filed by an individual under chapter 7, 11 or 13, if a case pending within one year prior to the petition was dismissed, other than a case refiled after dismissal under § 707(b). The stay may be continued if the court finds after a hearing upon motion of a party in interest that refiling was in good faith. However, the case is presumed not to be in good faith, rebuttable only by clear and convincing evidence. The presumption against good faith applies to all creditors if: more than one case under any chapter in the previous year, and the previous case was dismissed because the debtor failed amend schedules or petition when ordered by the court, or failed to provide adequate protection ordered by the court, or there has not been a substantial change in the debtor's financial condition or personal affairs or any other reason to conclude that the later case will not be concluded if a chapter 7, with a discharge, or if a chapter 11 or 13, with a confirmed plan that will be fully performed. The presumption against good faith applies to any creditor who: filed a motion under § 362(d) and at the time of dismissal the motion was pending or had been resolved by the termination, modification or conditioning of the stay in the prior case.

10. No Stay for Serial Filers.

Under § 362(c)(4), no stay goes into effect if 2 or more cases pending within the one-year prior to an individual's chapter 7, 11 or 13 case, were dismissed other than a case refiled after dismissal under § 707(b). The court may impose the stay upon request of a party in interest, but the motion must be filed within 30 days of the date of the petition, the stay will not take effect until the order is entered, the movant must establish the good faith of the later filing, and the presumption of lack of good faith is identical to § 362(c)(3). Upon request, the court may enter an order confirming that no stay was in effect.

11. In Rem Stay Relief for Real Property.

Pursuant to § 362(d)(4), the stay may be terminated as to real property securing an obligation if the court finds that the filing was part of a scheme to hinder, delay or defraud the creditor involving: (a) transfer of an ownership interest without creditor approval or a consent order; or (b) multiple bankruptcy filings involving the property. A § 362(d)(4) in rem order recorded in accordance with state law is binding in any other bankruptcy case filed within 2 years of the entry of the order.

12. Termination of the Stay for Personal Property.

According to § 362(h), the stay is terminated as to personal property (secured or leased), if the individual debtor fails to timely file a statement of intentions indicating that the debtor will surrender, retain and redeem or reaffirm, or assume the lease or if the debtor fails to timely perform the intentions. This section does not apply if the upon motion of the trustee, the court determines that the property is of consequential value to the estate, if the court orders adequate protection for the creditor/lessor or if the court orders the debtor to deliver the personal property to the trustee.

13. Assumption of Personal Property Leases.

Under § 365(p), the individual chapter 7 debtor may assume a lease of personal property by providing written notification to the lessor of the desire to assume; the creditor, at the creditor's option, may consent to the assumption, and may require the debtor to cure any arrearage as a condition of assumption. Within 30 days, the debtor must notify the creditor that the lease is assumed. The stay is not violated by notice to the debtor and negotiation of the cure.