Plenary Session

Consumer Law Update 2009

Hon. William H. Brown

U.S. Bankruptcy Court (W.D. Tenn.) (ret.); Carbondale, Colo.

Prof. Jeffrey W. Morris

University of Dayton School of Law and Counsel, Porter Wright, Morris & Arthur; Dayton, Ohio

2009 Educational Materials

CONSUMER LAW UPDATE

Cases reported from September 1, 2008 through May 20, 2009

Prepared for American Bankruptcy Institute

Hilton Head, S.C. July 29-August 1, 2009

United States Bankruptcy Judge Retired

williamhoustonbr@comcast.net

Table of Contents

Prefiling Issues

Empirical Study of BAPCPA. The first report of the effects of BAPCPA, based on data from a random national sampling of debtors, has been published. R.M. Lawless, et al., *Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors,* 82 AM. BANKR. L. J. 349 (2008). A summary of the article is found in Melanie Sonnenborn & John A.E. Pottow, *2009 Consumer Bankruptcy Project—Empirical Analysis Suggests Initial Failure of BAPCPA to Produce Intended Results,* NORTON BANKR. LAW ADVISER (Feb. 2009).

Credit Briefing

Briefing on same calendar day as filing case satisfies § 109(h). Reversing the bankruptcy court and acknowledging split of authority, the BAP holds that briefing may occur on the same calendar day as the filing; "a debtor qualifies as a debtor under § 109(h) so long as he or she completes the required credit counseling at any time between 180 days before, and the moment of, filing of the petition." *In re Francisco,* 386 B.R. 700, 705 (B.A.P. 10th Cir. 2008).

Prebankruptcy credit briefing doesn't apply in involuntary case. After filing of an involuntary Chapter 7, which was not contested, the debtor moved for an extension of time to obtain the § 109(h) credit briefing. The motion was moot, concluding that § 109(h) doesn't apply to involuntary debtors. *In re Sims,* 2009 WL 161343 (Bankr. D. Kan. Jan. 7, 2009).

Debtor's inability to pay for briefing is no excuse. Recognizing that counseling agencies are statutorily required to provide services without regard to ability to pay, financial difficulty is not an exigent circumstance justifying waiver. *In re Sherry,* 2008 WL 3876595 (Bankr. N.D. Ohio Aug. 20, 2008); *see also In re Palacios,* 2008 WL 700968 (Bankr. E.D. Va. Mar. 13, 2008).

Debt Relief Agency

Section 527(b)'s application of "debt relief agency" status to attorneys is constitutional, reversing district court's holding that § 526(a)(4) is facially unconstitutional. In appeal from *Hersh v. United States*, 347 B.R. 19 (N.D. Tex. 2006), the Fifth Circuit held on Dec. 18, 2008, that bankruptcy attorneys do qualify as debt relief agencies under § 101(12A) and for the application of that agency status under § 526(b), agreeing with *Milavetz, Gallop & Milavetz, P.A., et al. v. United States*, 541 F.3d 785, 792 (8th Cir. 2008), that "attorneys that provide 'bankruptcy assistance' to 'assisted persons' are 'debt relief agencies." Section 101(12A) does not specifically include attorneys but neither does it

exclude them. As to § 526(a)(4)'s prohibition against advising an "assisted person" to "incur more debt in contemplation of such person filing a case under" Title 11, the Fifth Circuit holds that the provision is not facially unconstitutional, here disagreeing with the *Milavetz* panel. Applying the "doctrine of constitutional avoidance," the Fifth Circuit "construes the statute to prevent only a debt relief agency's advice to a debtor to incur debt in contemplation of bankruptcy when doing so would be an abuse of the bankruptcy system[,]" basing its conclusion on numerous portions of BAPCPA that discourage bankruptcy abuse, including expanded case dismissal and means testing provisions; "placement of section 526(a)(4) among three provisions meant to curb abuse of the bankruptcy system by debt relief agencies likewise suggests that the statute was only intended to curb abuse." By reversing the district court's holding that § 526(a)(4) was facially unconstitutional, the panel also dissolved the injunction against enforcement. Finally, § 526(b) does not violate the bankruptcy attorney's "First Amendment rights because it does not unduly burden her or her clients, and is narrowly tailored to promote the government's compelling interest in ensuring that consumer debtors are aware of basic bankruptcy information." *Hersh v. United States,* 553 F.3d 743 (5th Cir. 2008).

Automatic Stay

Creditor's state court suit exceeds relief from stay order. Affirming the BAP, the Ninth Circuit restates that actions taken by state court in violation of the stay are void ab initio, with the bankruptcy court not obligated to give full faith and credit to such orders. The motion seeking stay relief was directed toward the creditor's pursuit of the debtor's bonding company, and the BAP and Circuit noted that the stay relief order could be no broader than the relief sought in the motion. If in the course of a state court proceeding after stay relief is granted, it is found that broader relief is needed, the creditor should move for such relief from the bankruptcy court. Another remedy may be to seek retroactive stay relief. But, proceeding to a state court order that exceeds the relief granted by the bankruptcy court is not the appropriate creditor course. *Griffin v. Wardrobe (In re Wardrobe),* 559 F.3d 932 (9th Cir. 2009).

Debtor's former spouse's attorney violates stay. Attorney for debtor's former spouse willfully violated the stay by collection efforts, aggravated by attorney's refusal to release debtor from jail, adopting "egregious conduct" as an element of circumstances that may justify punitive damages under § 362(k). *Young v. Repine (In re Repine),* 536 F.3d 512 (5th Cir. 2008).

IRS is entitled to stay relief for setoff. The bankruptcy court denied a motion by IRS for stay relief to permit setoff against prepetition tax refunds, and by administrative mistake IRS paid the refunds to the debtor, but the BAP holds that this payment did not make IRS's appeal constitutionally or equitably moot. **See discussion under Appeal.** IRS established that it had right of setoff under 26 U.S.C. § 6402(a), which permits credit of any overpayment by the taxpayer against any liability owed by the taxpayer, with "overpayment" being a different concept from "refund" under authority of *IRS v. Luongo (In re Luongo),* 259 F.3d 323 (5th Cir. 2001). When it filed its motion for stay relief to permit setoff, IRS made a prima facie showing of its right to setoff, shifting the burden to the debtor to demonstrate that stay relief was inappropriate. Under its prior authority, *Pieri v. Lysenko (In re Pieri),* 86 B.R. 208 (B.A.P. 9th Cir. 1988), the BAP held that if any conflict existed, § 553 would control over § 522(c). Since the debtor presented no evidence that the tax refunds at issue were necessary for effective reorganization in Chapter 13, it was error to deny IRS stay relief under § 362(d)(2). *United States v. Gould (In re Gould),* 401 B.R. 415 (B.A.P. 9th Cir. 2009).

Award of debtor's attorney fees for stay violation should be under lodestar method. The Chapter 13 debtor who prevailed on a complaint for willful violation of the automatic stay was awarded attorney fees, but the bankruptcy court reduced the requested fee by 2/3. The First Circuit BAP remanded, holding that under former §362(h) [now (k)] the lodestar method is the first step in determination of an appropriate fee. Although the bankruptcy court may make adjustments to the lodestar amount, any reduction must be adequately supported. The bankruptcy court's reduction of the $26,680 requested fee to $7,500 based only on the request being "extremely high in view of the minimal damages" awarded to the debtor for emotional distress was an abuse of discretion. Deference must be given to the § 330(a)(3) and (4) factors. *Lopez v. Consejo de Titulares del Condominio Carolina Court Apartments (In re Lopez),* ___ B.R. ___, 2009 WL 1259377 (B.A.P. 1st Cir. May 7, 2009).

Criminal prosecution exception from stay is absolute. Recognizing §362(b)(1)'s exception from the automatic stay as an absolute exception, the good or bad faith of the law enforcement authority's criminal prosecution is not an issue, and the search warrant and seizure of the debtor's financial records as part of the prosecution did not violate the stay. Upon finding that the criminal prosecution exception applied, the debtor could not argue in the bankruptcy court any violation of property of the estate, civil rights or abuse of process. The court also noted that §105(a) gives no basis for enjoining the criminal

prosecution. *Bartel v. Walsh (In re Bartel),* ___ B.R. ___, 2009 WL 1219941 (B.A.P. 1st Cir. May 4, 2009).

Presentment and honoring prepetition check don't violate the stay. Reversing the bankruptcy court's determination that a check cashing entity willfully violated the stay by presenting the debtor's prepetition check for payment, the BAP held that the presentment of the check after receiving notice of the bankruptcy filing didn't violate the stay; also, when the check was honored the stay wasn't violated by retention of the funds. The transfer is avoidable as a postpetition transfer under § 549, but the debtor's complaint for willful violation damages fails. The debtor had received a "payday" loan prepetition, giving his postdated check for $460 to the check cashing entity. A few days later, Chapter 13 was filed, with notice of filing served on the holder of the check; despite this notice, the check was presented for payment and payment was made. The recipient of the funds refused to turn over the $460 to the debtor unless it received a general release and withdrawal of the debtor's stay violation motion. Although the BAP concedes that the funds in the debtor's checking account became property of the bankruptcy estate upon filing, presentment is permitted under § 362(b)(11), and when the bank honored the check, the transfer of funds took them out of the bankruptcy estate. The next step in the analysis is that upon the transfer, albeit unauthorized, the recipient could not have violated the stay by retaining the funds. "It would be illogical to interpret § 362(b)(11) to mean that the holder of a check can hand the check to a bank teller but cannot take the cash the teller hands over the counter without violating the stay, or that the holder of a check may accept the funds but must immediately return them to the drawer. Such an interpretation would render the exception essentially meaningless, because the purpose of presenting a check is to receive payment." *Buckeye Check Cashing, Inc. v. Meadows (In re Meadows),* 396 B.R. 485, 495 (B.A.P. 6th Cir. 2008). The panel then points out that Buckeye had resisted the turnover simply because of its fight over stay violation and resistance to paying the debtor's attorney fees, all the time willing to return the funds since they were obviously subject to recovery under § 549. The concurring judge points out that while the parties were willing for the money to be turned over to the debtor, had that result been contested, it would have been necessary for the debtor to show that the original giving of the check was an involuntary act, in order to satisfy the debtor's standing to pursue avoidance under § 522(h). *Buckeye Check Cashing, Inc. v. Meadows (In re Meadows),* 396 B.R. 485 (B.A.P. 6th Cir. 2008).

Stay doesn't arise under § 362(c)(4). Distinguishing § 363(c)(3) and (4), no stay comes into effect in third case filed within one year; creditor's actions

postpetition could not violate stay. *Nelson v. Wong Pension Trust (In re Nelson),* 319 B.R. 437 (B.A.P. 9th Cir. 2008).

Limited "ride through" option survives BAPCPA, at least for pro se debtors attempting reaffirmation. Affirming the bankruptcy court's opinion, the district court for the Eastern District of North Carolina interpreted BAPCPA's amendments to reaffirmation and stay relief, concluding that when the pro se debtors' attempts to reaffirm a car loan were denied by the bankruptcy court, the debtors were permitted to retain the car and maintain payments. At the reaffirmation hearing, the bankruptcy judge found that the debtors had negative income over expenses, that the vehicle was worth far less than the loan balance, and that the proposed reaffirmation must be rejected as undue hardship. The debtors testified of their family's need for the vehicle, and the bankruptcy court held that the automatic stay still applied, so long as the debtors remained current on payments and other contractual obligations. Under §§ 362(h)(1) and 521(a)(2), approval of the reaffirmation is not an element for maintaining the stay, and the debtors fulfilled their statutory duty of timely filing their intention to reaffirm; under a plain meaning of those statutes, the bankruptcy court held that the stay remained in effect, and the district court agreed, concluding that the "absurdity" and "drafters' intent" exceptions to plain meaning did not apply. The district court opinion reviews the history of "ride through" and the legislative efforts to restrict it, as well as judicial interpretations of pre-BAPCPA § 521(a)(2). As a result of BAPCPA amendments, "termination of the automatic stay may occur through either of two independent provisions: section 521(a)(6) or the combination of section 521(a)(2)(C) and 362(h)….Section 521(a)(6) makes three things clear. First, it applied when the creditor has an 'allowed claim' for the 'purchase price' of an individual debtor's personal property. Second, if it applies, and if the debtor does not redeem the encumbered personal property, but desires to retain the encumbered personal property, the debtor must timely 'enter[ ] into an agreement…pursuant to section 524(c)'….Finally, if section 521(a)(6) applies and the debtor does not obey it, the automatic stay is terminated, [and] the property is no longer part of the estate." *Coastal Federal Credit Union v. Hardiman*, 398 B.R. 161 (E.D. N.C. 2008). Under a combination of §§ 521(a)(2)(C) and 362(h), "three things [are] clear. First the debtor must timely enter into an agreement 'of the kind specified in section 524(c)….Second, the debtor must timely take the action that the debtor specified in the required statement of intentions. Third, if the debtor does not obey these provisions, then the automatic stay is terminated with respect to the encumbered personal property and the property is no longer part of the estate." *Id.* at * 8. Since this case involved debtors not represented by counsel for the reaffirmation process,

the bankruptcy court was required to hold a hearing and determine if the reaffirmation agreement is approved.

Although § 521(d), added by BAPCPA, makes ipso facto clauses enforceable, that is only true upon a debtor's failure to take the action required by §§ 521(a)(6) and 362(h). The district court then looked at § 521(a)(6)'s requirement that the creditor have an "allowed claim for the purchase price…," noting that this creditor did not have an "allowed claim"; to read the statute literally is not absurd, with the court finding plausible reasons why Congress may have included "allowed claim" in the statute. The same is true for the inclusion of "for the purchase price" in the statute. Even though the bankruptcy court didn't approve the reaffirmation, it was nevertheless an "agreement" entered into by the pro se debtors. The fact that §§ 521(a) and 362(h) don't give the creditor relief does not leave it without potential relief for "cause" under § 362(d). "[U]nder the governing principles of statutory construction, this court must analyze whether it is plausible that Congress could have chosen to spare uncounseled debtors whose reaffirmation agreements were not approved by the bankruptcy court from automatically losing the protection of the automatic stay, becoming subject to any applicable ipso facto clause, and becoming subject to both repossession and a personal deficiency judgment….Congress could plausibly have chosen the result that flows from BAPCPA's plain language."

The results are that the stay remains in place for the pro se debtors whose reaffirmation agreement was not approved by the bankruptcy court, the car remains property of the estate, and the debtors may maintain possession so long as they stay current on payments and other contractual obligations; the creditor retains only in rem rights and remedies in the event of default. *Coastal Federal Credit Union v. Hardiman*, 398 B.R. 161 (E.D. N.C. 2008).

Another district court in the Fourth Circuit concludes "ride through" no longer available and ipso facto clauses are valid. Reversing the bankruptcy court's finding that the car lender violated the automatic stay by repossession without giving notice of cure opportunity, the district court for the Southern District of West Virginia held that BAPCPA abolished the "ride through" option. The debtor filed a statement of intention to "continue payments" on a vehicle jointly owned with his nondebtor spouse, and the parties were current on installment payments and insurance maintenance. The statement did not indicate whether the debtor intended to redeem or reaffirm, and DaimlerChrysler moved to confirm termination of the stay, which motion was granted by the bankruptcy court; however, after DaimlerChrysler repossessed without giving

notice of an opportunity to cure, the spouses filed a motion for injunctive relief, which was also granted by the bankruptcy court, and the creditor returned possession to the debtor and spouse. After reviewing pre-BAPCPA split of authority on the ride through option, the district court held that the option was eliminated by BAPCPA's amendments and additions of §§ 521(a)(2), 521(a)(6) and 362(h), "at least insofar as applied to this debtor who failed to redeem, reaffirm, or surrender….The BAPCPA changes to the Code require the debtor to redeem, reaffirm or surrender the property, or the automatic stay will be lifted and the property will not be part of the estate….The cases holding that the 'ride through' option is still viable after BAPCPA are limited in their applicability." *DaimlerChrysler Financial Services Americas LLC v. Jones (In re Jones),* 397 B.R. 775 (S.D. W.Va. 2008) (citing and distinguishing cases). Since the "ride through" option doesn't exist, for a debtor who doesn't comply with § 521(a)(6) and 362(h), ipso facto clauses in contracts are valid; the filing of bankruptcy in itself may be a contractual default permitting repossession even when the debtor is current. Moreover, the creditor's acceptance of payments while the dispute was ongoing did not act as waiver or estoppel, since § 521(f) gives the debtor a right to make voluntary payments, while § 521(*l*) permits the creditor to accept payments before and after the filing of a reaffirmation agreement. Under West Virginia law, the creditor was not required to give notice of a right to cure default, since the bankruptcy filing triggered the default, with the district court holding that a cure opportunity applies only to default in payments under the contract. *DaimlerChrysler Financial Services Americas LLC v. Jones (In re Jones),* 397 B.R. 775 (S.D. W.Va. 2008)

1994 addition of exception for creation or perfection of statutory lien for ad valorem taxes doesn't apply retroactively. Concerning property with a long history of bankruptcies, alleged by the tax authority to have been designed to avoid property tax sales, the district court affirms the bankruptcy court's holding that § 362(b)(18)'s exception, which was added in the Bankruptcy Reform Act of 1994, doesn't contain a clear expression of retroactive application. As a result, the exception doesn't apply to a case filed in 1992 and terminated in 1997, and the tax lien imposed during the pendency of that case is void under authority of *In re Meyers*, 491 F.3d 120 (3d Cir. 2007) ("actions in violation of the stay are void but retroactively ratifiable if the stay is annulled."). *Keuller v. Monroe County Tax Claim Bureau (In re Keuller),* 399 B.R. 782 (M.D. Pa. 2009).

Section 362(c) (3)'s "with respect to the debtor" interpreted as referring to spousal filings. In a Chapter 7 case where the debtor was a repeat filer, after the 30 days expired, the mortgage creditor moved for an order confirming that

the stay had terminated under §362(c)(3). The debtor argued that the statute's language "with respect to the debtor" meant that the stay terminated only with respect to him personally but that the stay remained in effect as to property of the estate. The court concluded that §362(c) (3) applied to both the debtor and property of the estate, construing the "with respect to the debtor" phrase in the context of the entire §362(c) as "referring to the serially-filing spouse, making the debtor subject to collection actions, both *in personam* and *in rem* (against estate and non-estate property) while leaving the stay in effect as to the newly-filing spouse's person and property." In reaching this conclusion, the court reviews three other interpretations of the phrase. *In re Daniel,* 404 B.R. 318 (Bankr. N.D. Ill. 2009).

Section 362(*l*) not applied when residential eviction is based on nonmonetary default. When the landlord had obtained a prebankruptcy eviction based on excessive accumulated debris that endangered the property, the Chapter 13 debtor's certification and tender of rent to the clerk under §362(*l*) didn't reinstate the automatic stay because the default was not monetary. The nonmonetary default could not be cured under §362(*l*), and the debtor's motion to reinstate the stay was denied. *In re Griggsby,* 404 B.R. 83 (Bankr. S.D. N.Y. 2009).

Mortgage refinancing scam violates stay. Finding that the Chapter 13 debtor was tricked into signing deeds that she believed were part of mortgage refinancing, the scam violated the automatic stay as attempts to exercise control over property of the estate, and the deeds were void. *Walker v. Creative Loans, LLC (In re Walker),* ___B.R.____, 2009 WL 1064355 (Bankr. E.D. Wis. Apr. 16, 2009).

Stay relief denied when servicer fails to demonstrate standing. The motion for stay relief was supported by a declaration of "bankruptcy specialist" that movant had "possession" of original note, but the motion failed to show that movant had authority to act for note holder beyond merely stating it was servicer. The servicer doesn't assert a beneficial interest in the note nor does it establish a right to enforce the note. "The real party in interest in relief from stay is whoever is entitled to enforce the obligation sought to be enforced. Even if a servicer or agent has authority to bring the motion on behalf of the holder, it is the holder, rather than the servicer, which must be the moving party, and so identified in the papers and in the electronic docketing done by the moving party's counsel….To have standing, [the servicer] must establish its authority to act for the holder of the Debtors' note." No business records were offered to

support that authority, and the declaration of the bankruptcy specialist was unclear about authority. *In re Jacobson,* 2009 WL 567188 (Bankr. W.D. Wash. Mar. 6, 2009).

Assignee of mortgage fails to have standing for stay relief. Discussing the "serial assignments" of mortgages that have "complicated what was previously a generally straight-forward standing analysis," the Chapter 7 trustee's objection to stay relief was sustained, when the motion was filed by MERS as "nominee" for the mortgagee, and the motion provided no documentation or evidence that the party for whom MERS was acting had any interest in the note or mortgage. *In re Sheridan,* 2009 WL _____, Case No. 08-20381-TLM (Bankr. D. Idaho, March 12, 2009).

Creditor seeking in rem relief and ban against future filings must proceed in adversary proceeding. A creditor's motion seeking in rem relief outside what is authorized under § 362(d) and seeking a ban against future bankruptcy filings is treated by the court as a complaint for which the creditor must pay the adversary proceeding fee, and the creditor's "election to combine injunctive relief with stay relief operates to waive the automatic termination provision of § 362(e)." Section 362(d)(4), added by the 2005 Act, requires a finding that the petition was filed as part of a scheme to delay, hinder and defraud creditors, and the order making such a finding must be recorded as to the property at issue. The present motion doesn't contend that the Chapter 7 case is a part of the necessary scheme; therefore, § 362(d) (4) is not applicable. The request for in rem relief as to particular property seeks injunctive relief, going to the court's equitable authority, thus triggering a due process requirement of an adversary proceeding. Rather than denying the motion as seeking relief beyond what may be granted in a contested matter, the court treats the motion as one triggering an adversary proceeding, for which the creditor must pay the difference between a stay relief motion and a complaint. *In re Van Ness,* 399 B.R. 897 (Bankr. E.D. Cal. 2009).

Debtors must exhaust administrative remedy before seeking sanctions against IRS. Section 362(d) (9) provides an exception from stay for IRS investigation, audit and assessment, and 26 U.S.C. § 7433(e) (1) requires debtors to exhaust administrative remedies before seeking stay violation sanctions. *In re Douglas,* 2009 WL 168703 (Bankr. D. Kan. Jan. 23, 2009).

Reinstatement of Chapter 13 case doesn't retroactively reinstate stay. Section 362(c)(2)(B) is unambiguous, terminating the automatic stay upon dismissal of a case, and reinstatement of the dismissed case doesn't

retroactively put the stay back into effect during the gap period. When the debtor moved to reinstate the case after the sheriff's sale, no stay was in effect to void the sale. *Gargani v. Wells Fargo Bank, N.A. (In re Gargani),* 398 B.R. 839 (Bankr. W.D. Pa. 2009); *accord Smith v. Oak Grove Utility Co. (In re Smith),* 2009 WL 115293 (Bankr. D. Md. Jan. 16, 2009).

Contrasting views of trustee as individual for recovery under § 362(k). In cases reported in late 2008, involving attempted recovery by the Chapter 7 trustee for stay violations, the court in *Campbell v. Ledyard Nat'l Bank (In re Ledyard),* 398 B.R. 799 (Bankr. D. Vt. 2008), held that the trustee, although a natural person, represented the estate, which is not an individual, and the trustee had not personally been harmed by a stay violation. Although the trustee could not recover under § 362(k), the trustee could seek sanctions under § 105(a). In *Moser v. Mullican (In re Mullican),* 2008 WL 5191196 (Bankr. E.D. Tex. Sept. 30, 2008), the court discusses the split of authority on whether a trustee for a corporate debtor could recover under former § 362(h), concluding that a Chapter 7 trustee for individual consumer debtors had standing to pursue stay violation damages, here against the debtors.

Cause of action filed by unscheduled creditor is void while stay in effect, but after entry of discharge action may be pursued. Although the Chapter 7 debtor did not schedule the creditor who filed a state court suit for violations of the Fair Debt Collections Practices Act, the filing of the suit was a violation of the automatic stay and commencement of that suit is void ab initio; however, the plaintiff may proceed with the suit once the stay was terminated by entry of discharge. *See* discussion of the case concerning determination of discharge under **Jurisdiction**. *Johnson v. JP Morgan Chase Bank, et al.,* 395 B.R. 442 (E.D. Cal. 2008).

Motion to extend stay not necessary for debtor who received prior Chapter 7 discharge. Section 363(c)(3)'s limitation on the stay applies only to debtors with cases pending with the prior 1-year period and whose cases were dismissed; for a Chapter 13 debtor who received a discharge in a prior Chapter 7 case within the 1-year of filing the Chapter 13, no motion to extend the stay under § 363(c)(3)(B) is needed. *In re Forletta,* 397 B.R. 242 (Bankr. E.D. N.Y. 2008).

Avoiding Powers

Standing of Debtor

Necessary elements for Chapter 13 debtor's standing. In a concurring opinion, one judge on the Sixth Circuit BAP has reviewed the necessary elements for the debtor's bringing an avoidance action under § 522(h), citing *DeMarah v. United States (In re DeMarah),* 62 F.3d 1248, 1250 (9th Cir. 1995). The case involves the issue of whether the automatic stay was violated by a check cashing entity presenting the debtor's prepetition check, receiving the funds and refusing to turn them over to the debtor. *See* discussion of the case for that issue under **Automatic Stay**. In the concurring opinion, the issue of standing is discussed, had the debtor filed an avoidance action under § 549, with the focus being on whether the presentment was a voluntary transfer for purposes of § 522(g) and (h); the giving of the check originally was voluntary, but the presentment was "a creditor-initiated involuntary transfer under § 101(54)(D)." *Buckeye Check Cashing, Inc. v. Meadows (In re Meadows),* 396 B.R. 485, 495 (B.A.P. 6th Cir. 2008).

Value for avoidance

Value of debtors' interests determined when they obtained fee simple interests. Debtors, who held remainder interests in residence when Chapter 13 filed but then obtained and recorded fee simple interests, moved to avoid judgment lien two years after confirmation of their plan. In that interval, Indiana's homestead exemption had increased to $15,000, but with the increase in value for fee simple interests, the value exceeded the total liens plus exemptions. The Seventh Circuit held that under § 541(a)(7), the bankruptcy estate included the estate's interest acquired after commencement of the case, and that § 1306(a)(1) includes the interests the debtors acquired, while § 522 requires value for property acquired by the estate to be determined "as of the date such property becomes property of the estate." Increase in value of the residential interest, under the after-acquired statutes, is included in the calculation of value for lien avoidance purposes under § 522(f), and the value here is determined when the debtors acquired and recorded their fee simple interests. *(In re Willett,* 544 F.3d 787 (7th Cir. 2008).

Fraudulent transfer

Mortgage fails to provide constructive notice due to defective acknowledgement. Affirming the BAP in one of a series of avoidance attacks by Chapter 7 and 13 trustees, based on failure of the mortgage acknowledgement to properly follow applicable state law, the Sixth Circuit

provides an examination of when the trustee may successfully avoid such mortgages under § 544. There is a dissent taking the position that the alleged discrepancy does not amount to a failure to comply with state law. *Burden v. CIT Group/Consumer Fin., Inc. (In re Wilson),* 2009 WL 723197 (6th Cir. Mar. 19, 2009).

Debtor, victim of mortgage refinancing scam, did not voluntarily transfer. When the Chapter 13 debtor had been tricked into signing deeds, thinking they were mortgage refinancing, the executions of deeds were not voluntary transfers, and the debtor was able to use §§522(g) and 549 to avoid postpetition transfers. *Walker v. Creative Loans, LLC (In re Walker),* ___B.R.____, 2009 WL 1064355 (Bankr. E.D. Wis. Apr. 16, 2009).

Postpetition transfers

California's protection of bona fide purchasers from debtor is not preempted by Bankruptcy Code. Affirming the BAP, the Ninth Circuit held that when the Chapter 7 debtors sold their residence postpetition without authorization from the court, when the petition had not been recorded to give notice, and when the trustee had not abandoned the estate's interest in the residence, California's statute protecting bona fide purchasers from unrecorded conveyances was effective to protect those purchasers from the trustee's avoidance attack, which was based not on § 549(a) but on the transfer being void (§ 549(c) provides a defense to the purchasers if the attack was under § 549(a)). The panel also held that under *Schwartz v. United States (In re Schwartz,* 954 F.2d 569 (9th Cir. 1992), the automatic stay of § 362 protects the debtor from creditors, and a postpetition transfer by the debtor is not void as in violation of the stay. *Burkart v. Coleman (In re Tippett),* 542 F.3d 684 (9th Cir. 2008).

Preference

Debtors' use of credit card to transfer balances is preferential transfer of interest. When the debtors used one credit card within preference period to pay off balances on other cards, a transfer of the "interest of the debtors in property" occurred for § 547 purposes, with the Tenth Circuit agreeing with the majority view that the debtors had control over the disposition of the new funds and reversing the lower courts. Earmarking doctrine does not protect the transfer. *Parks v. FIA Card Servs. (In re Marshall),* 550 F.3d 1251 (10th Cir. 2008).

Property of estate

Chapter 7 property of estate

Section 363(o) interpreted by Eleventh Circuit. In a Chapter 7 case, after conversion from 13, the debtor attempted to exempt claims raised in an adversary proceeding against his mortgage company under the Truth in Lending Act, but the bankruptcy court held that the TILA claims were "independent rights under federal law," not subject to homestead exemption. The claims were property of the bankruptcy estate, and the Chapter 7 trustee settled the adversary proceeding by selling the claims to the mortgagee. The Circuit court held that § 363(o), added by BAPCPA, did not apply; the sale was of the debtor's claims under the TILA rather than of an underlying credit transaction. The debtor and counsel were also sanctioned by the bankruptcy court for discovery violations, in the amount of the mortgagee's attorney fees and costs, and the sanction was affirmed. *MacNeal v. Equinamics, Corp. (In re MacNeal),* 2009 WL 97559 (11th Cir. Jan. 15, 2009) (unpublished).

Under New York law, spouse's beneficiary interest in life insurance not property of estate. In Chapter 7 trustee's objection to debtor's exemption claim for cash surrender value of life insurance, spouses in jointly-filed case had two separate bankruptcy estates, unless substantively consolidated, and trustee could not reach cash surrender values of reciprocal life insurance policies that each debtor had, with the other spouse named as beneficiary. Under New York law, the beneficiary has no vested interest in the policy subject to trustee's administration. The court discusses effect of § 302 joint filings on separate estates. *Wornick v. Gaffney,* 544 F.3d 486 (2d Cir. 2008).

Debtor's beneficial interest in self-settled spendthrift trust reachable by trustee. Under California law, Chapter 7 debtor's beneficial interest in self-settled spendthrift trust was not protected from the trustee or hypothetical lien creditors; since the debtor had power to invade the trust corpus, under state law, "any spendthrift provisions are invalid when the settler is a beneficiary." *Cutter v. Vujic (In re Cutter),* 398 B.R. 6 (B.A.P. 9th Cir. 2008).

Economic stimulus payment is property of estate. Economic stimulus payment received by the Chapter 7 debtor postpetition is property of the estate without need for proration between pre- and postpetition periods. Since stimulus payment is federal, court looks to federal rather than state law. The trustee argued that the stimulus was tied to a prebankruptcy tax filing, which triggered the debtors' eligibility for stimulus, while the debtors argued that the payment

was an advance on their postpetition tax refund. Without specifically deciding that issue, the court holds that the estate is entitled to the entire stimulus, noting that after the debtors filed their prebankruptcy 2007 tax return they had a contingent interest as of the bankruptcy filing in the entire stimulus payment. The court doesn't apply the typical proration theory for a tax refund to see how much of the refund is related to the tax year that expired before the bankruptcy filing, since the stimulus payment has no relationship to the timing of the bankruptcy filing. *In re Schwinn,* 400 B.R. 295 (Bankr. D. Kan. 2009).

Settlement of prepetition cause of action by attorney not employed by trustee is void. The Chapter 7 debtor had been injured prepetition in an automobile accident, and the attorney representing the debtor in that action settled the cause of action without moving to be employed to represent the trustee. The bankruptcy estate was never that attorney's client. Under Rule 9019, court approval of a settlement involving property of the estate is necessary, and no approval was sought. The Chapter 7 trustee was not a party to the settlement. The settlement by the attorney acting without authority and employment is void ab initio. Since the settlement funds had been paid, they must be turned over to the trustee, who must then return the funds to the party that paid. *Nickless v. McGrail & McGrail (In re Dooley),* 399 B.R. 340 (Bankr. D. Mass. 2009).

Disability credit insurance is not property of estate. Until entire balance of debt is paid by credit insurance payable on disability, that insurance doesn't vest in debtor and debtor's estate has no claim to insurance on theory that debt is bifurcated. *In re Gladwell,* 2009 WL 140098 (Bankr. C.D. Ill. Jan. 21, 2009).

Chapter 13 property of estate

Assets acquired postconfirmation and before termination of case are property of estate. Under confirmed plan, debtors chose option that upon confirmation all property of estate vested in them, and after confirmation, debtors inherited two parcels of real estate. Judgment was taken against debtors for postconfirmation business debt, and judgment was recorded as lien. Debtors moved to avoid lien. Court reviews three basic approaches to reconciliation of §§ 1306(a) and 1327(b), adopting "growing majority" view that all postpetition acquired property is property of estate. Under this plan's revesting provision, the only property that vested in the debtors upon confirmation was the property in existence at confirmation. The parcels inherited by the debtors postconfirmation could not revest in them; therefore, while the postpetition creditor did not violate the stay by suing the debtors, there was a violation of § 362(a)(4) in the

creditor's judgment lien against the inherited property of the estate. As to the debtors' home that did revest at confirmation, the judgment lien could properly attach without violating the stay. *In re Jackson,* ___ B.R. ___, 2009 WL 562621 (Bankr. D. Idaho Mar. 5, 2009).

Judicial estoppel applies without regard to harm to creditors. Rejecting argument that application of judicial estoppel would harm creditors, district court applies doctrine to bar debtor's pursuit of undisclosed cause of action, finding that nondisclosure was intentional. Blaming bankruptcy counsel also doesn't prevent application. *Coppedge v. Suntrust Bank, Inc.,* 2009 WL 111639 (M.D. Ga. Jan. 14, 2009). *Compare Melton v. Nat'l Dairy Holdings, L.P.,* 2009 WL 653024 (M.D. Ala. Mar. 10, 2009), where court declines to apply judicial estoppel to Chapter 13 debtor's failure to amend schedules to disclose employment discrimination claim; while there is evidence to support inference that debtor intended to manipulate the system, court cites prior authority that "failure to amend is not the same as affirmatively misrepresenting the nonexistence of claims that are being pursued in another proceeding."

Debtor implicitly has right to use estate property preconfirmation. In a dispute over whether the Chapter 7 trustee could recover assets used by the Chapter 13 debtor prior to conversion, if the debtor uses estate property in good faith while awaiting confirmation of a plan, the Code implicitly grants that right to debtors. *In re Laflamme,* 397 B.R. 194 (Bankr. D. N.H. 2008).

Exemptions

First Circuit interprets §522(g). In the first circuit to address the question of whether § 522(g) permits the denial of a debtor's homestead exemption when the Chapter 7 debtor had fraudulently transferred residential property to a spouse but then voluntarily reconveyed that property prepetition, the First Circuit concluded that the language of the statute did not permit denial of an exemption. "The second transfer—the reconveyance—was curative, not fraudulent. The ensuing declaration of homestead was, therefore, unexceptional." Since the case had been filed before the effective BAPCPA date, §522(p) didn't apply, according to the previous BAP decision. *Stornawaye Fin. Corp. v. Hill (In re Hill),* 562 F.3d 29 (1st Cir. 2009).

Debtor has no homestead after conveying property with contingent life possession. When the debtor conveyed her home to her child to enable the child to mortgage property, receiving in return a contingent right to possess the property for her life if the bank became the owner, the debtor had no life estate

under South Dakota law and had no right to homestead exemption. She merely had a contractual personal property interest, which became property of the Chapter 7 bankruptcy estate. *Fix v. First State Bank of Roscoe,* 559 F.3d 803 (8th Cir. 2009).

Amendment of exemption permits only objection to amended and not to original exemption claim. Questioning "whether the Supreme Court would, in fact, permit a trustee to use § 105 to object to exemptions to which he declined or failed to properly object pursuant to the Rules," when the Chapter 7 trustee did not timely object to the debtor's original homestead exemption claim, the debtor's amendment of exemptions only opened the door to the trustee objecting to the amended claim. The original exemption claim was to two parcels of real estate, neither of which was actually the debtor's homestead, under § 522(d) (1). The amended exemptions didn't change the homestead claim, but changed the debtor's exemption claim in stock. The trustee was unable to bootstrap an objection to the erroneous homestead claim in his objection to the amended stock exemption. *Grueneich v. Doeling (In re Grueneich),* 400 B.R. 680 (B.A.P. 8th Cir. Mar. 11, 2009).

Iowa homestead given extraterritorial effect. Section 522(b) (2)'s choice of exemption law doesn't preempt state law which prohibits application of that state's exemption to property located outside the state; instead, the fall back to federal bankruptcy exemptions becomes effective. However, the BAP interprets Iowa law and concludes that its homestead exemption applied to a Chapter 7 debtor who filed in Oklahoma but had not lived there the 730 days before filing. Since Iowa's homestead law is silent as to its extraterritorial effect, the BAP looked to Iowa case law. Iowa's personal property exemption specifies that it is available only to residents of the state, but the homestead contains no such restriction. The old case law in the state did not interpret the current homestead statute, and the BAP applies the principle that the "legislature's inclusion of a residency requirement in its personal property exemption statute, while making no reference to residency in its homestead statute, is presumed to be intentional." *Stephens v. Holbrook (In re Stephens),* 402 B.R. 1 (B.A.P. 10th Cir. Mar. 9, 2009). *Compare In re Gosnick,* 400 B.R. 582 (Bankr. W.D. Mich. Dec. 17, 2008) ("Michigan courts, for almost one hundred years, have held that its laws do not have extraterritorial application to real estate located in another state." Debtor may not claim exemption under Michigan law on real estate located in Alabama.).

Under Texas law, debtor's annuity purchase on eve of bankruptcy is in fraud of creditors for purposes of exemption. Debtors transferred $30,000 into an annuity on the day before filing Chapter 7 (pre-BAPCPA case), and the trustee objected to the claim of exemption under Texas Insurance Code, with the trustee arguing that the transfer was "a premium payment made in fraud of a creditor," excepted from the insurance exemption under Tex. Ins. Code Ann. § 1108.053. In contrast to scheduling the $30,000 as their property, the debtors testified at the objections hearing that the money was an inheritance from one debtor's father, and that the inheritance was held by the debtors in safekeeping pending division with siblings. The circuit court construes the Texas insurance exemption and its fraud exception, as well as Texas's Uniform Fraudulent Transfer Act, as including not only actual intentional fraud but conduct less than intentional fraud: "Ultimately, Texas courts will have to determine how much less than actual intent to defraud suffices to deny exemptions for insurance policies and annuities under § 1108.053….[However, traditional 'badges of fraud' may be] used to infer actual intent to defraud [as well as] to determine 'constructive' fraud. Factors relevant to determining actual intent to defraud, a higher culpability standard, should be equally probative where something less than actual intent will suffice." *Soza v. Hill (In re Soza),* 542 F.3d 1060, 1067 (5th Cir. 2008). Finding that sufficient badges of fraud existed to deny the claimed exemption as a "premium payment made in fraud of a creditor,…[the debtors] purchased the annuity on the eve of bankruptcy. Assuming the payment came from their non-exempt property, the annuity was in an amount that would have covered all of the debtors' listed debts, and the purchase deprived the creditors of all but $340 in non-exempt assets." *Id.* at 1068. On remand, the bankruptcy court must determine how much of the $30,000 was property of the debtors and how much would be property of other heirs. *Soza v. Hill (In re Soza),* 542 F.3d 1060 (5th Cir. 2008).

Overpayment of taxes on exempt retirement fund remains exempt. After certification to the Utah Supreme Court and its answer, the BAP holds that under Utah law when the debtor overpays taxes due from an exempt retirement fund, the refund is exempt, because it is traceable to the exempt property. *Smith v. Mosier (In re Smith),* 401 B.R. 487 (B.A.P. 10th Cir. Feb. 24, 2009).

Filing declaration of homestead in violation of state court order is invalid exemption. As part of state court judgment, creditor was entitled to attachment lien, and transfer of property from joint tenancy to spouse was in contempt of judgment order. Attempted spouse's declaration of homestead also violated judgment. Although the spouse removed her homestead, the debtor then filed

his homestead declaration eight days before filing Chapter 7. In a complaint objecting to discharge under § 727(a)(2)(A) and to the debtor's claimed homestead, the bankruptcy court found the homestead declaration invalid as in contempt of the state court's order and also found under a "continuous concealment" theory that the debtor had transferred his interest in the property within one year of bankruptcy filing with intent to hinder, delay or defraud creditors. The BAP reversed the objection to discharge (see discussion under **Chapter 7 Discharge**), but affirmed the denial of the homestead exemption, finding that the state court clearly intended to require both the debtor and spouse to remove their homestead claims and not refile them. *Antongnoni v. Basso (In re Basso),* 397 B.R. 556 (B.A.P. 1st Cir. Dec. 9, 2008).

Debtor who did not contribute to tax withholdings has no exemption claim. Under Minnesota law, even though a joint tax return was filed, a spouse who did not contribute to the tax withholdings has no ownership in tax refund and no exemption claim to the refund. BAP discusses three approaches that courts have taken to allocation of tax returns between spouses: (1) majority approach of allocating based on proportion of respective tax withholdings; (2) dividing refund according to income generated by each; and (3) splitting refund evenly. *Carlson v. Moratzka (In re Carlson),* 394 B.R. 491 (B.A.P. 8th Cir. 2008).

Traditional badges of fraud used for § 522(o) analysis. Although the BAP applies traditional badges of fraud for purposes of whether § 522(o)'s intent to defraud element is found, there must be extrinsic evidence of fraud before the homestead exemption is limited, and mere conversion of nonexempt assets to exempt on the eve of bankruptcy is not enough. The addition of § 522(o) by BAPCPA did not change the evidentiary standard for fraudulent conversion in the 8th Circuit; rather, it "marks out a look-back period of ten years….It also extends what was the law in the Eighth Circuit and made it uniform national law." *Clark v. Wilmoth (In re Wilmoth),* 397 B.R. 447 (B.A.P. 8th Cir. 2008) (quoting *Addison v. Seaver (In re Addison),* 540 F.3d 805 (8th Cir. 2008)).

Homestead is surcharged for trustee's expenses arising from debtor's fraud. Notwithstanding the BAP's prior reversal of an order surcharging the debtor's homestead, the BAP left open potential surcharge upon appropriate findings and conclusions, and the bankruptcy court makes such findings. Under *Latman v. Burdette,* 366 F.3d 774, 786 (9th Cir. 2004), the bankruptcy court has authority to surcharge an exemption "when reasonably necessary both to protect the integrity of the bankruptcy process and to ensure that a debtor exempts an amount no greater than what is permitted by the exemption scheme of the

Bankruptcy Code." The Ninth Circuit BAP had held that a surcharge is permitted in instances of debtor misconduct amounting to fraud on the court and creditors. *In re Onubah,* 375 B.R. 549, 554 (B.A.P. 9th Cir. 2007). In a summary of findings, the bankruptcy court found that the debtor fabricated a second-mortgage loan "in an attempt to preserve equity in his residence and defeat the collection efforts of his judgment creditors." The Chapter 7 trustee expended 1,500 hours contesting this fictitious loan, with the trustee claiming $500,000 in attorney fees. Absent the trustee's expense, the estate would have paid the creditors and trustee in full. Without yet deciding an amount of the trustee's attorney fees, the court found "reasonable costs of coping with the Debtor's deception far exceed $75,000, the exemption to which Debtor otherwise would be entitled." If surcharge of $75,000 is not made against the homestead, the "financial consequences of Debtor's misconduct would fall most heavily upon Debtor's creditors, including Trustee and his attorneys." *In re Law,* 401 B.R. 447 (Bankr. C.D. Cal. 2009). C*ompare Scrivner v. Mashburn (In re Scrivner),* 535 F.3d 1258 (10th Cir. 2008), *cert. denied,* 2009 WL 735673 (Mar. 23, 2009) (Surcharge or debtor's exempt property is not authorized under the Code; other remedies such as sanctions or revocation of discharge are available.).

Workers' compensation benefit is exempt under § 522(d) (10) (C). Postpetition settlement of workers' compensation benefit is covered by § 522(d) (10) (C)'s "right to receive" a disability benefit, rejecting the trustee's attempt to distinguish the postpetition settlement from a prepetition right to receive. The exemption is determined as of filing date and debtor had suffered injury prepetition. *In re Nielsen,* 401 B.R. 149 (Bankr. M.D. Pa. 2009).

Section 522(o) doesn't apply to tenancy by entirety. In an individual's Chapter 11 case, the court held that § 522(o) applies to an exemption claimed under homestead laws and not to a tenancy by entirety exemption, adopting *Dillworth v. Hinton (In re Hinton),* 378 B.R. 371, 389-81 (Bankr. M.D. Fla. 2007). *In re Davis,* 403 B.R. 914 (Bankr. M.D. Fla. 2009).

Section 522(o) not triggered by debtors' move and surrender of prior home. When the Chapter 7 debtors moved from larger home to smaller one on another lot prior to bankruptcy and surrendered first home for foreclosure, § 522(o) was not triggered; this is not the type of transfer the section addresses and has no effect on the value of the new home for exemption purposes; moreover, there is no evidence of transfer with the intent described in § 522(o). *In re Jones,* 397 B.R. 765 (Bankr. D. S.C. 2008).

Chapter 7 Issues

Chapter 7 eligibility, means testing, and dismissal for abuse--§ 707(b)

National Guard and Reservists Debt Relief Act of 2008. Enacted on October 20, 2008, Pub. L. No. 110-438 provides temporary exclusion from the means test for reservists and members of the Guard who are called for no less than 90 days for active service or homeland defense, with an amendment to § 707(b)(2)(D) effective on December 19, 2008, for those cases commenced within the 3-year period beginning on that effective date. Official Form B22A is amended to include a new Part 1C for qualifying debtors.

Disability insurance benefit included in CMI. Granting direct appeal of dismissal of a Chapter 7 case for abuse, the Ninth Circuit holds that the definition of current monthly income in § 101(10A), including the phrase "without regard to whether such income is taxable income," and the statutory exclusion of certain types of payments, indicates that Congress intended to broadly include income such as disability insurance benefits within CMI. Although such income may not be taxable, it is still subject to debt repayment under CMI. *Blausey v. U.S. Trustee,* 552 F.3d 1124 (9th Cir. 2009).

Deduction of vehicle ownership expenses when vehicle has no debt continues to divide courts. The Seventh Circuit held that an above-median income debtor owning a vehicle free of debt may still deduct the IRS Local Standard for ownership expenses, reversing the district court at *Neary v. Ross-Tousey (In re Ross-Tousey),* 368 B.R. 762 (E.D. Wis. 2007). After deduction of those expenses, as well as operating expenses, the debtors had no disposable income and were eligible for Chapter 7 relief, with the panel concluding that § 707(b)(2)(A)(ii)(I)'s use of the term "'applicable monthly expense amount' cannot mean the same thing as 'actual monthly expenses.' Under the statute, a debtor's 'actual monthly expenses' are only relevant with regard to the IRS's 'Other Necessary Expenses;' they are not relevant to deductions taken under the Local Standards, including the transportation ownership deduction….We conclude that the better interpretation of 'applicable' is that it references the selection of the debtor's geographic region and number of cars." The case was remanded for the district court to consider the U.S. Trustee's alternate argument that totality of circumstances supported a finding of abuse under § 707(b)(3)(B). *Ross-Tousey v. Neary,* 549 F.3d 1148 (7th Cir. 2008).

As *Ross-Tousey* points out in its discussion, the appellate courts are divided on this issue, which typically arises in Chapter 13 cases involving disposable income issues. See, e.g.: **Debtor may take the ownership deduction even when the vehicle is free and clear**-- *Ross-Tousey; Hildebrand*

v. Kimbro (In re Kimbro), 389 B.R. 518 (B.A.P. 6th Cir. 2008); *Pearson v. Stewart (In re Pearson),* 390 B.R. 706 (B.A.P. 10th Cir. 2008). **Debtor may not take the ownership deduction**—*Ransom v. MBNA America Bank N.A. (In re Ransom),* 380 B.R. 799 (B.A.P. 9th Cir. 2007); *Babin v. Wilson (In re Wilson),* 383 B.R. 729 (B.A.P. 8th Cir. 2008); *see also, In re Coffin,* 396 B.R. 804 (Bankr. D. Me. 2008); *In re Hunt,* 2008 WL 5142183 (Bankr. S.D. Ind. Dec. 5, 2008).

Debtor may deduct mortgage on home being surrendered, but § 707(b) (3) abuse still requires dismissal. Although agreeing that the debtor could deduct the mortgage "amount scheduled as contractually due" on a home being surrendered, as well as the amount that would be required to cure the mortgage in a Chapter 13 plan, the Chapter 7 debtor was caught by the totality-of-circumstances test. The surrender of the home before hearing the U.S. Trustee's motion to dismiss caught the debtor who had passed the means test in an abuse finding under § 707(b)(3). The debtor had a stable income and had improved her financial picture by moving back in with her mother—bottom line, the debtor had ability to repay a substantial portion of her debt. *In re Goble,* 401 B.R. 201 (Bankr. S.D. Ohio 2009). *See also In re Castellaw,* 401 B.R. 223 (Bankr. N.D. Tex. 2009) (Debtors would realize an "unconscionable advantage" amounting to abuse if permitted to remain in Chapter 7, when they had a substantial income and were retaining multiple luxury items, transferring "the cost of an unnecessarily extravagant lifestyle to creditors."); *In re Baker,* 400 B.R. 594 (Bankr. N.D. Ohio 2009) (Debtor budgeting for college expenses for adult child had ability to repay 50% of unsecured debt and Chapter 7 would be abuse under totality of circumstances.); *In re Booker,* 399 B.R. 662 (Bankr. W.D. Mo. 2009) (Debtors' ability to pay may be considered under totality of circumstances; although Social Security income is excluded from means test, it may be considered in ability to pay test. If unnecessary and unreasonable expenses are eliminated, debtors are able to pay significant dividend to unsecured creditors.).

Same sex couple didn't abuse system when filing separate cases. When same sex couple filed separate Chapter 7 petitions and didn't include other person's income in means test, dismissal for abuse is denied. Only married couples may file jointly. *In re Roll,* 400 B.R. 674 (Bankr. W.D. Wis. 2008).

Dismissal under §707

Lack of timely U.S. Trustee statement of abuse presumption didn't bar motion to dismiss. Although the U.S. Trustee didn't file the § 707(b)(2) statement of presumption of abuse, a motion was later filed to dismiss the case

under § 707(b)(3)'s totality of circumstances, and the BAP held that the § 707(b)(2) requirement of a timely statement only affects whether the U.S. Trustee may filed a § 707(b)(2) motion; its failure does not prevent a § 707(b)(3) motion. *Fokkena v. Draisey (In re Draisey),* 395 B.R. 79 (B.A.P. 8th Cir. 2008). *See also, e.g., In re Violanti,* 397 B.R. 852(Bankr. N.D. Ohio 2008), for dismissal based on totality or circumstances.

Dismissal under §521

Debtors' motion to dismiss for their failure to comply with § 521 requirements is denied. In the Chapter 13 phase of case, debtors failed to comply with § 521(a)(1)(B) filing requirements, and after conversion to Chapter 7, the trustee sought approval of settlement of discrimination cause of action for sufficient amount to pay all claims and return money to debtors. The debtors, who had not scheduled the cause of action originally, were unhappy with settlement and moved to dismiss, arguing that their failure to comply with § 521(a) within 45 days required automatic dismissal pursuant to § 521(i). The bankruptcy court exercised authority to deny dismissal based on waiver of the § 521(a) requirement. The First Circuit agreed, holding that the bankruptcy court had discretionary authority to waive the § 521(a) requirements after the fact, since § 521(a) (1) (B) begins with "the debtor shall file…unless the court orders otherwise." However, the ruling is not unlimited: "We do not decide today whether bankruptcy courts possess unfettered discretion to waive the disclosure requirements ex post. Where, however, there is no continuing need for the information or a waiver is needed to prevent automatic dismissal from furthering a debtor's abusive conduct, the court has discretion to take such an action….To sum up, the great divide in section 521 is between information that is required and information that is not. The Act allows courts to do the sifting suggested by that divide without rigid adherence to the forty-five-day deadline." *Segarra-Miranda v. Acosta-Rivera (In re Acosta-Rivera),* 557 F.3d 8 (1st Cir. 2009).

Trustee is estopped from moving to dismiss for debtor's failure to file payment advices. When the Chapter 7 debtor had provided payment advices to the trustee at the §341 meeting, which occurred within the 45-day period after commencement of the case, the trustee returned those to the debtor at the meeting without informing the debtor of the need to file them with the clerk. The trustee later moved for dismissal for the debtor's failure to timely file the advices with the clerk, but the court held that the trustee was equitably estopped. Although equitable estoppels can't be imposed against a governmental unit, the case trustee is not protected from the doctrine, and the trustee's discretionary

decision to move to dismiss is subject to "common law rights of estoppel." *In re Gilbert,* 403 B.R. 297 (Bankr. W.D. N.Y. 2009).

Discharge and Reaffirmation

Discharge exceptions

Bankruptcy Rule 4007(c) permits more than one extension. Holding that deadline in Rule 4007(c) for filing dischargeability complaints is not jurisdictional, the Rule does not limit a creditor to only one extension. *United States v. Horras (In re Horras),* 399 B.R. 885 (Bankr. S.D. Iowa 2009).

Tax matter partner's contesting of IRS tax adjustments suspended limitations period for individual debtor/partner. Recognizing that there may be circumstances where a tax matter partner acts in such a way as to benefit him contrary to the interests of the other partners or partnership, here the tax matter partner invoked tax court proceedings to contest adjustments made by IRS to the partnership's tax obligation, and that action was not in conflict with the partnership. As such, the partner's actions suspended the assessment limitations period, resulting in a suspension affecting the individual debtor who had been a partner, for purposes of §523(a) (1). *United States v. Martinez (In re Martinez,* 564 F.3d 719 (5th Cir. 2009).

Reckless disregard for truth of financial statements supports § 523(a) (2) (B) exception and bankruptcy court may enter monetary judgment. The bankruptcy judge may look at totality of circumstances to infer debtor's intent to deceive when there is evidence of reckless disregard for truth and the "sheer magnitude" of the misrepresentation supports the inference. The bankruptcy court has jurisdiction not only to find the debt nondischargeable but to also enter a monetary award. Although questioning why other circuits had not examined the issue of jurisdiction in light of the "jurisdictional dichotomy of core and related-to jurisdiction," the panel nevertheless adopts the "arguments of tradition and pragmatism" from the other circuits and agrees that the bankruptcy court has jurisdiction to enter a monetary judgment against the debtor. *Morrison v. Western Builders of Amarillo, Inc. (In re Morrison),* 555 F.3d 473 (5th Cir. 2009).

Reasonable reliance only required by original creditor under §523(a) (2) (B). Considering §523(a)(2)(B)(iii) as it intersects with assignment, the Ninth Circuit looked at the meaning of the word "is" in that subsection, with the debtor arguing that "is" required the creditor who held the claim at the time of bankruptcy to exercise independent reasonable reliance. Agreeing with the Seventh Circuit in *McClellan v. Cantrell,* 217 F.3d 890, 896 (7th Cir. 2000), the

statute's "obtained by" language indicates that the reliance must have been at the time of the debt's inception. The Ninth Circuit agreed with its BAP's decision, at 367 B.R. 138, that the assignee does not have to show that it reasonably relied—that reliance is only required by the original creditor. *Boyajian v. New Falls Corp. (In re Boyajian),* 564F.3d 1088 (9th Cir. 2009).

Prebankruptcy judgment under state unfair and deceptive practices act litigated same issues as in §523(a) (2) (A). Construing Massachusetts's law on effect of default judgment, substantial participation by the defendant in the state court proceedings justified application of "already litigated" principle of that state's collateral estoppel law. The litigation in state court included the same elements required for §523(a) (2) (A)'s fraud-based exception, with the state court making findings of fraudulent conduct and false representations by the debtor. *Backlund v. Stanley-Snow (In re Stanley-Snow),* ___B.R. ___, 2009 WL 1219943 (B.A.P. 1st Cir. May 6, 2009).

Reliance on financial statement with inaccuracies on its face is not reasonable. Reversing the bankruptcy court, the BAP found from the evidence that a financial statement was "inaccurate on its face in numerous areas….Any reliance…placed upon the financial statement was unreasonable." The BAP also found nothing in the record to support justifiable reliance under § 523(a) (2) A) on the debtor's representations. *R & R Ready Mix, Inc. v. Freier (In re Freier),* 402 B.R. 891 (B.A.P. 8th Cir. 2009).

Default judgment against pro se defendant given preclusive effect in § 523(a)(2) proceeding. Affirming the bankruptcy court's giving of preclusive effect to fraud-based judgment in federal district court action, the BAP applied federal preclusion law to the judgment, with the defendant having had a full and fair opportunity to litigate the fraud issue in the prior district court action, even though the defendant was financially distressed, allegedly forced to dismiss his attorney and proceeding pro se. *Melnor v. Corey (In re Corey),* 394 B.R. 519 (B.A.P. 10th Cir. 2008).

Discretion abused in denial of creditor's motion to amend § 523(a)(2) complaint. Five days before trial, the creditor moved to amend her § 523(a)(2) complaint to add § 523(a)(14) count, alleging the debtor incurred a debt to pay a tax to the United States that would be nondischargeable, with the motion asserting that facts stated in the original complaint related to the § 523(a)(14) count and that the creditor had just received information from IRS to support the amended count. The motion was denied, with trial proceeding and the debtor being granted a judgment on the § 523(a)(2)(A) and (B) counts. The BAP

affirmed the § 523(a)(2) rulings but remanded, holding that the bankruptcy court should have granted the motion to amend to add § 523(a)(14): "[T] fact that the proposed amendment was based in part on an allegation made in the original complaint weighs in favor of—not against—granting Peterson leave to amend the complaint. Peterson's entire complaint was premised on a belief that the Debtor had misrepresented to her that he intended to use the loan proceeds to pay a tax debt….Amendments to state a new legal theory based on allegations known to a defendant should be liberally allowed when statutes of limitation are not involved." *Peterson v. Weber (In re Weber),* 392 B.R. 760, 764-65 (B.A.P. 8th Cir. 2008).

Debtor's failure to schedule creditor bars discharge in no asset case, §523(a)(3). Agreeing with the Seventh Circuit, the First Circuit has held that even in a no asset case, the debtor must list a creditor in order to discharge that debt under §523(a)(3). That section does not distinguish between asset and no asset cases in its requirement that the claim be listed or scheduled in time to permit the creditor to file a timely proof of claim. The creditor had sued the debtor as a surety after the principal defaulted after the debtor's discharge, but the Circuit held that the debt arose out of the prebankruptcy surety agreement. Although the debt could have been subject to discharge if listed, the First Circuit disagreed with the Third, Fifth, Sixth and Ninth Circuits, holding that listing a creditor, or that creditor's actual knowledge of the bankruptcy filing, is a condition to obtaining a discharge. *Colonial Surety Co. v. Weizman,* 564 F.3d 526 (1st Cir. 2009).

Medical bills incurred prior to conversion to Chapter 7 are dischargeable under § 523(a) (3). While in Chapter 13, the debtors' minor child was injured, resulting in medical bills of $29,000 for which the debtors agreed to be responsible. When the debtors converted to Chapter 7, they failed to schedule the medical provider but the case was administered as a no asset. While unscheduled debts are nondischargeable in Chapter 13, in Chapter 7, the debt is dischargeable unless § 523(a) (3) applies: § 523(a) (3) (A) is not applicable since the Chapter 7 is a no asset, with no proofs of claim required; the preconversion creditor was unable to prove under § 523(a) (3) (B) that the debt would be excepted from discharge. *OSF Healthcare Systems, Inc. v. Davis (In re Davis),* 2009 WL 302221 (Bankr. C.D. Ill. Feb. 5, 2009).

Past-due contributions to ERISA employee benefit plan are dischargeable under §523(a) (4). Holding that contributions from the debtor's wholly-owned corporation to the ERISA-qualified employee benefit plan did not become "plan

assets" until actually paid, the Chapter 7 debtor had not become a fiduciary over any contributions that had not been paid by the corporation. *Rahm v. Halpin (In re Halpin),* ___F.3d ___, 2009 WL 1272632 (2d Cir. May 11, 2009).

Granting of power of attorney puts debtor in fiduciary capacity for purposes of § 523(a) (4). The debtor's motion to dismiss complaint is denied, finding that the complaint sufficiently alleged fiduciary capacity when the creditor gave the debtor a power of attorney and entrusted money in the debtor's care while the creditor underwent cancer treatment. The debtor allegedly used those funds for her own benefit, and a § 523(a) (4) cause of action is stated. *Eveland v. Kishbaugh (In re Kishbaugh),* 399 B.R. 419 (Bankr. M.D. Pa. 2009). *Compare Harrold v. Raeder (In re Raeder),* 399 B.R. 432 (Bankr. N.D. W.Va. 2009) (Debtor was not in fiduciary capacity for purposes of § 523(a) (4) simply because he had check writing authority for his mother, but sufficient facts are at issue to retain cause of action for § 727(a) (4) (A) false oath.).

Punitive sanction to force payment of alimony is not domestic support obligation. When the state court imposed on the debtor $50 for each day that his separate alimony obligation was late, that was a sanction and was not a part of the alimony for purpose of § 101(14A)'s definition of "domestic support obligation," and the sanction is not a priority claim under § 507(a)(1) for purposes of the debtor's Chapter 13 plan. Although the case does not involve discharge, its application of § 101(14A) may arise in a discharge scenario. *Smith v. Pritchett (In re Smith),* 398 B.R. 715 (B.A.P. 1st Cir. 2008).

Services by child's representative are in nature of support but not included within definition of domestic support obligation payee for § 523(a)(5). Denying a motion for default judgment by the state-court appointed representative for the debtor's child, the bankruptcy court analyzed whether the representative was a payee eligible for inclusion within § 523(a)(5)'s domestic support obligation exception from discharge. Looking at § 101(14A)'s definition of domestic support obligation, subsection (14A)(i) and (ii) provide who may be a payee "owed to or recoverable by"; while the services of the court-appointed representative are support in nature and arise under a divorce decree, the representative is not included within the designated parties who may recover a domestic support obligation from the debtor. Following the analysis of *Simon, Schindler & Sandberg, LLP v. Gentilini (In re Gentilini),* 365 B.R. 251 (Bankr. S.D. Fla. 2007), the bankruptcy court held that "[u]nder BAPCPA, the payee requirement is even more clearly set out [than in pre-BAPCPA § 523(a)(5)], as separate paragraph (A) in the § 101(14A) definition of domestic support

obligation. The requirement of that paragraph that an obligation be 'owed to or recoverable by' a specified payee must be honored as a matter of basic statutory construction….Contrary to [the representative's] argument, then, his right to payment from the debtor is not within the scope of §§ 101(14A) and 523(a)(5) simply because it is a court-ordered payment in the nature of support." In addition, the representative's claim was not one that was recoverable by the debtor's former spouse, since the state court did not place any obligation on the former spouse to pay the debtor's portion of the representative's fee. Finally, the court distinguished the court-appointed child representative from a "legal guardian," with the latter being one of the payee's designated within § 101(14A)(i), and the representative is not a "governmental unit" as that term in used in § 101(14A)(ii). *Levin v. Greco (In re Greco),* 397 B.R. 102 (Bankr. N.D. Ill. 2008).

Separate analysis of "willful" and "malicious" prongs required under § 523(a)(6). Reversing partial summary judgment, the Ninth Circuit held that precedent in that Circuit requires separate determination of the two elements of § 523(a)(6). The debtors had been found liable in a prebankruptcy jury trial for willful copyright infringement, and the bankruptcy court determined on summary judgment that the infringement constituted a willful injury; the BAP implied maliciousness from the trial court's finding of willfulness, since there was proof that the debtors were aware of the plaintiff's copyright at the time of infringement. The Circuit panel found that insufficient, seeing an unresolved issue of fact as to whether the infringement was actually willful; an issue existed whether the debtors ordered the infringement or whether an employee of their company did so. "Although there may be some overlap between the test for 'willfulness' and the test for 'malice,'…the overlap does not mean that the Bankruptcy Court can ignore entirely the malice inquiry." *Barboza v. New Form, Inc. (In re Barboza),* 545 F.3d 702, 711 (9th Cir. 2008).

Intentional breach of contract also requires tortious conduct for § 523(a)(6) exception. Holding that an intentional breach of contract is covered by § 523(a)(6)'s exception only if it also meets the applicable state-law standard for tortious conduct, the Ninth Circuit may have a different standard from the Fifth Circuit. *Compare Lockerby v. Sierra,* 535 F.3d 1038 (9th Cir. 2008), with *In re Williams,* 337 F.3d 504 (5th Cir. 2003), and *see* Hon. Paulette Delk, *Lockerby v. Sierra: The Ninth Circuit Takes a Look at the Dischargeability of Breach of Contract Claims under § 523(a)(6),* NORTON BANKR. LAW ADVISER (Jan. 2009).

Attorney fees and costs awarded against debtor are excepted under § 523(a) (6) in absence of compensatory judgment. Chapter 7 debtor had $11,573 judgment against her for contempt in violating state court order enjoining her from contacting new wife of debtor's former husband, but no compensatory judgment had been entered. The BAP affirmed that the judgment for fees and costs arose from willful and malicious acts—the debtor intentionally violated the state court order and her actions were substantially certain to lead to injury. Finding no specific Ninth Circuit authority, the BAP found the award to be similar to sanctions, and used the rationale of *Cohen v. de la Cruz,* 523 U.S. 213 (1998), a § 523(a)(2)(A) case involving attorney fees and costs, to conclude that the judgment here was the result of the debtor's willful and malicious violation of the injunction. *In re Suarez,* 400 B.R. 732 (B.A.P. 9th Cir. 2009).

Issue of material fact prevents § 523(a)(6) summary judgment on debtor's use of secured receivables to pay trust fund taxes. In adversary proceeding brought by creditor secured by receivables against individuals in Chapter 7 who were corporate officers and used receivables to pay delinquent trust fund taxes, the BAP holds that secured creditor held interest in funds that was superior to IRS's, but issues of material fact exist on whether the injury to secured creditor was willful and malicious. The debtors argued that any payment to IRS of trust fund taxes could not have been from corporate funds; rather, payment would have been from trust funds. The bankruptcy court had granted the creditor's summary judgment motion after finding that its interest was superior to that of IRS; however, the fact that the debtors used the creditor's funds did not necessarily establish the willful and malicious elements. *JP Morgan Chase Bank, N.A. v. Zwosta, et al. (In re Zwosta),* 395 B.R. 378 (B.A.P. 6th Cir. 2008).

Standard for § 523(a) (6) damages for conversion is market value. Affirming a determination that the debtor willfully and maliciously stopped feeding ex-wife's horses, the district court holds that the proper standard for determination of "damages for conversion, the common-law tort for wrongful possession or disposition of another's property, is the market value of the property at the time and place of its conversion, not the diminution in value as suggested by [the debtor]." *Hamilton v. Hamilton (In re Hamilton),* 400 B.R. 696 (E.D. Ark. 2009).

Criminal guilty plea given same preclusive effect in § 523(a)(6) as trial verdict. Under New York law, guilty plea to second degree assault for stabbing the victim in a fight is given same preclusive effect as a trial conviction, with that state's penal code for the offense requiring that the defendant acted intentionally, without excuse or justification. The bankruptcy court also considered whether

self defense could be considered under New York law. *Hernandez v. Greene (In re Greene),* 397 B.R. 688 (Bankr. S.D. N.Y. 2008).

Cost assessment by New Hampshire Supreme Court Committee on Professional Conduct is nondischargeable fine or penalty under § 523(a)(7). After two disciplinary actions against the debtor/attorney, the state's Committee on Professional Conduct assessed costs for bringing the disciplinary proceedings against the attorney, who then filed Chapter 7. Under state Supreme Court's rules, assessment of costs is discretionary, a factor supporting it being a penalty rather than mere fee or cost shifting; the cost assessment is akin to a sanction, which is in the nature of a penalty. Applying the rationale of *Kelly v. Robinson,* 479 U.S. 36, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986), "[w]hile noting that attorney disciplinary proceedings are not criminal, [cases subsequent to *Kelly*] have found that the goals of these sanctions—deterrence, rehabilitation and protection of the public interest—are sufficiently analogous to *Kelly* to support an extension of its rule." *Richmond v. New Hampshire Supreme Court Committee on Professional Conduct,* 542 F.3d 913, 920 (1st Cir. 2008).

Debtor's obligation to indemnify bail bondsman is dischargeable under § 523(a)(7). The debtor had agreed to indemnify a bail bondsman if another individual did not appear for trial; the criminal defendant did not appear, and the bond was forfeited. The bondsman paid $16,000 to the State and sued the debtor on the indemnity agreement, obtaining a default judgment for $20,150. After filing of Chapter 7, the bondsman filed an adversary proceeding to determine that the debt was excepted from discharge under § 523(a)(7). Finding no obligation from the indemnitor to the State and that the bail bondsman was not a governmental entity, the Circuit Court held that the bondsman is not subrogated to the rights of the state for nondischargeability purposes; under plain language of § 523(a)(7), the debt to the bondsman is dischargeable. *Affordable Bail Bonds, Inc. v. Sandoval (In re Sandoval),* 541 F.3d 997 (10th Cir. 2008).

Government claims under False Claims Act are within § 523(a) (7) exception. Although the government's claims for treble damages assessed under the False Claims Act were penal in nature and not compensatory, and were within § 523(a) (7)'s exception, there was no evidence that the debtor knowingly presented a false or fraudulent claim; therefore, the penalties were discharged. *McFarland v. United States (In re McFarland),* 399 B.R. 549 (Bankr. M.D. Fla. 2009).

Student account and deferment agreement with private university are in nature of loan for purposes of § 523(a) (8). Adopting reasoning of *In re Johnson,* 218 B.R. 449 (B.A.P. 8th Cir. 1998), the Ninth Circuit holds that the debtor's agreement with Vanderbilt University, establishing an account and deferment, amounted to a "loan" under that term's ordinary meaning, and the loan was within the reach of § 523(a)(8). *McKay v. Ingleson,* 558 F.3d 888 (9th Cir. 2009).

Strain on marriage is factor in § 523(a) (8) undue hardship. Applying 3-part test of *Long v. Educ. Credit Mgmt. Corp. (In re Long),* 322 F.3d 549, 554 (8th Cir. 2003), under the third element of "other relevant facts and circumstances surrounding each particular bankruptcy case," the 65-year old debtor who had been an educator for 30 years and had no probability of obtaining increased income demonstrated undue hardship in paying $300,000 student loan debt. One factor in the court's determination was evidence of strain on the debtor, his spouse and their marriage from the financial stress of the student loan debt. *Halverson v. U.S. Dept. of Educ. (In re Halverson),* 401 B.R. 378 (Bankr. D. Minn. 2009).

Under § 523(a) (19), bankruptcy court lacks authority to determine liability for securities violations or fraud. Section 523(a) (19), added under the Sarbanes-Oxley Act of 2002, has two elements: "the debt is for violation of securities laws or fraud in connection with the purchase or sale of a security, [and]…the debt must be memorialized in a judicial or administrative order or settlement agreement." The exception originally "required a *pre*-bankruptcy judgment, order or settlement agreement," but BAPCPA added to the second element that the judgment or agreement "results, before, on, or after the date on which the petition was filed," leading to "debate as to whether § 523(a) (19) now allows a bankruptcy court to render its own determination of liability…or whether the liability determination must still be made outside of the bankruptcy court." Agreeing that the BAPCPA change gave the bankruptcy court concurrent jurisdiction to determine dischargeability, this court concluded that § 523(a) (19) (B) still requires that "*the liability determination* occur outside of the bankruptcy forum, whether it occurs pre- or post-bankruptcy. Once liability has been imposed, then either a bankruptcy court or a non-bankruptcy court may determine the application of this nondischargeability statute." *Nusse v. Jafari (In re Jafari),* 401 B.R. 494 (Bankr. D. Colo. 2009).

Discharge objections

Filing declaration of homestead in violation of state court order is invalid exemption but not grounds for § 727(a)(2)(A) discharge objection. As part of state court judgment, creditor was entitled to attachment lien, and transfer of property from joint tenancy to spouse was in contempt of judgment order. Spouse's attempted declaration of homestead also violated judgment; although spouse removed her homestead, the debtor then filed homestead declaration eight days before filing Chapter 7. In complaint objecting to discharge under § 727(a)(2)(A) and to the debtor's claimed homestead, the bankruptcy court found the declaration invalid as in contempt of the state court's order and also found "continuous concealment" of the debtor's transfer of his interest in the property within one year of bankruptcy filing with intent to hinder, delay or defraud creditors. The BAP reversed the objection to discharge but affirmed the denial of the homestead exemption (see discussion under **Exemptions**), finding that the state court clearly intended to require both the debtor and spouse to remove their homestead claims and not refile them. As to the discharge objection, the transfer of the debtor's interest to his spouse took place more than one year before bankruptcy filing, and the continuous concealment doctrine did not apply even though the debtor retained a beneficial interest after the transfer. The wife had transferred the property to a trust, with herself as trustee and her husband as sole beneficiary; despite the retention of beneficial interest, the BAP found that the debtor did not conceal his beneficial interest within the one year before bankruptcy, since no steps were taken within that year to hide his interest. In fact, the debtor's declaration of homestead was the opposite of concealment. *Antongnoni v. Basso (In re Basso),* 397 B.R. 556 (B.A.P. 1st Cir. 2008).

Burden of § 727(a)(2)(A) proof remains on creditor. Although there is a presumption of fraud for a debtor's transfer of property without receiving payment, the debtors rebutted that presumption by evidence that they had "a non-fraudulent reason for the transfer of the property; namely, they created the trusts to hold property until the property increased in value to create enough equity to make a profit on the sale of the property[, with the debtors testifying they had] learned this business model in the real estate seminars they attended." The bankruptcy court had determined the evidence on fraudulent intent to be "equally split between the parties," meaning that the creditor did not carry its burden of proof, and the BAP affirmed, holding that the bankruptcy court properly applied the presumptions and burdens. *Cadlerock Joint Venture II, L.P. v. Sandiford (In re Sandiford),* 394 B.R. 487, 490 (B.A.P. 8th Cir. 2008).

U.S. Trustee fails to show "property of estate" requirement for § 727(a) (2) (B). U.S. Trustee objected to debtor's discharge after conversion from Chapter

13 to 7, on basis that debtor had won lottery after filing Chapter 13 and spent those funds. What is included in property of estate for purposes of § 727(a) (2) (B) must be examined in light of § 348(f) (1) (A). Although the lottery winnings were included in the Chapter 13 property of the estate pursuant to § 1306, the effect of § 348(f) (1) (A) is to put the debtor in the same economic position as if the case had originally been filed as a Chapter 7. Had the case been filed under Chapter 7, the debtor's postpetition lottery winning and the dissipation of that winning would not have been a basis to deny discharge under § 727(a) (2) (B), even though it might have formed basis for case dismissal under § 707. Section 348(f) (2) doesn't help the U.S. Trustee, since that section's bad faith conversion only applies if the debtor converts the case; here the case was involuntarily converted to Chapter 7. *Adams v. Bostick (In re Bostick),* 400 B.R. 348 (Bankr. D. Conn. 2009).

Collateral estoppel not given in § 727(a)(2) and (a)(4) proceeding in debtor's case to judgment against debtor's closely held corporation. When the Chapter 7 debtor had been severed from a state court trial upon his bankruptcy filing, awarding of a fraud-based judgment against his closely held corporation and a finding that the corporation was his alter ego were not given preclusive effect against the debtor. The debtor did not participate in that trial and the automatic stay prevented any judgment against him individually. A separate determination of fraud must be made in the adversary proceeding. *Adler v. Lisa Ng (In re Adler),* 395 B.R. 827 (E.D. N.Y. 2008).

Failure to justify lack of records denies discharge under § 727(a)(3). Debtor who owned and/or controlled various business entities is denied discharge on summary judgment under § 727(a)(3) and standard of *Lansdowne v. Cox (In re Cox),* 41 F.3d 1294 (9th Cir. 1994), when the creditor made prima facie case and debtor failed to demonstrate justification for failure to keep or preserve records. In *Cox*, the circuit court "stated that the purpose of § 727(a)(3) is to make discharge dependent on the debtor's true presentation of his financial affairs." When a creditor makes a prima facie case "by showing '(1) that the debtor failed to maintain and preserve adequate records, and (2) that such failure makes it impossible to ascertain the debtor's financial condition and material business transaction,…the burden of proof then shifts to the debtor to justify the inadequacy or nonexistence of the records.'" *Caneva v. Sun Communities Operating Limited Partnership (In re Caneva),* 547 F.3d 1082, 1087 (9th Cir. 2008) (quoting *In re Cox,* 41 F.3d at 1296). "[W]hen a debtor owns and controls numerous business entities and engages in substantial financial transactions, the complete absence of recorded information related to those entities and

transactions establishes a prima facie violation of 11 U.S.C. § 727(a)(3). Likewise, we hold that when a debtor transfers a substantial amount of money to a third party [$500,000], the failure to keep any documentation evidencing the terms of the transfer or the fact that the payment actually took place establishes a prima facie violation of 11 U.S.C. § 727(a)(3)." *In re Caneva,* 547 F.3d at 1088-89. Debtor's "conclusory statement tracking the language of § 727(a)(3) in his affidavit in opposing summary judgment" did not carry his burden of showing justification for lack of records. *Id.* at 1089. The "statute imposes an affirmative duty of the debtor to keep and preserve recorded information that will allow his creditors to ascertain his financial condition and business transactions." *In re Caneva,* 547 F.3d at 1090. *Caneva v. Sun Communities Operating Limited Partnership (In re Caneva),* 547 F.3d 1082, 1087 (9th Cir. 2008), *opin. amended* 2008 WL 5205899 (9th Cir. Dec. 15, 2008).

Relief from denial of discharge

Section 727(e)(2) not available to debtor. Three years after the bankruptcy court had denied discharge for the debtor's transfer of assets with intent to hinder, delay or defraud creditors, the debtor moved to "revoke denial of discharge," relying on § 727(e)(2). Finding this section applied only to provide relief when a discharge had been granted, no relief from a denial of discharge is available to the debtor. Neither did Fed. R. Civ. P. 60(b) provide relief: the debtor showed no fraud upon the court to satisfy Rule 60(b)(3), and the delay of three years in seeking relief was not reasonable for Rule 60(b)(6) purposes. The bankruptcy court did not abuse its discretion in awarding $3,825.40 sanctions against the debtor for the trustee's legal fees and expenses in defending the motion, and an order restricting the effect of future pleadings filed by this debtor was reasonable in light of the debtor's litigious history and the notice given to the debtor of the sanctions hearing. The restriction provided that future pleadings would not be effective nor require response by other parties until the bankruptcy court had conducted a hearing and given an objection deadline. *Turner v. Kristan (In re Kristan),* 395 B.R. 500 (B.A.P. 1st Cir. 2008).

Revocation of Discharge

Discharge revoked for debtor's failure to disclose settlement. Under §727(d), the discharge was properly revoked when the debtor did not disclose $25,000 postpetiton settlement of prebankruptcy cause of action, made false statements at the creditor's meeting, and failed to turn over settlement proceeds to Chapter 7 trustee. *Yules v. Gillis (In re Gillis), 403* B.R. 137 (B.A.P. 1st Cir. 2009).

Discharge injunction

Refusal to provide transcripts violates discharge injunction. Affirming the bankruptcy and district courts, the Seventh Circuit held that a private university's refusal to provide a student's transcripts was an action to collect a debt for unpaid tuition and a violation of the discharge injunction. Distinguishing the debtor's property right in the transcripts from a student loan debt that would not be dischargeable, the Circuit found a state-law property interest in the record of grades and the university's violation of that right was an attempt to collect unpaid tuition, violating both the automatic stay and discharge injunction. *In re Kuehn,* 563 F.3d 289 (7th Cit. 2009).

***Rooker-Feldman* Doctrine limited.** Notwithstanding *Rooker-Feldman* Doctrine, discharge injunction makes state-court judgment void ab initio if entered against a debtor as to debts that have been discharged. *Hamilton v. Herr (In re Hamilton),* 40 F.3d 367 (6th Cir. 2008).

Chapter 7 debtor states cause of action for violation of discharge injunction when creditor sued nondebtor spouse. The creditor's action in state court against the debtor's nondebtor spouse was found to be without merit, and the debtor's complaint alleged that this suit was an attempt to force the debtor to pay a discharged debt. The wife incurred $50,000 defending the suit in state court, proving that she had nothing to do with the transaction between the debtor and creditor. The discharge injunction complaint states a valid cause of action. *In re Lumb,* 401 B.R. 1 (B.A.P. 1st Cir. 2009).

Monetary damages for discharge injunction violation can be sought through motion. The debtors may seek recovery of damages for alleged violation of the discharge injunction through a motion rather than being required to file an adversary proceeding. No due process concerns were presented, when the motion adequately protected the creditor. *In re Englund,* 401 B.R. 377 (B.A.P. 8th Cir. 2009).

Reaffirmation

Debtor fails to rebut presumption of undue hardship for reaffirmation, but the creditor's right to repossess is questioned. When the debtor filed a reaffirmation agreement for a vehicle more than 45 days after the meeting of creditors, notwithstanding the unsupported allegation that the debtor's mother was willing to help make car payments, the debtor failed to rebut the § 524(m)(1) presumption of undue hardship when there is a $3,000 shortfall of scheduled

expenses over income. The debtor offered no proof that his mother was willing and able to assist with payments. After denying approval of the reaffirmation, the court confirmed that the automatic stay had terminated after expiration of the 45 day deadline for filing the reaffirmation agreement, but the creditor's motion to repossess the car was denied, with the creditor being required to proceed in a Rhode Island court to determine if repossession is authorized under state law. The court discusses the impact under Rhode Island's adoption of the Uniform Consumer Credit Code of the lack of payment default on the car creditor's right to repossess, citing other bankruptcy court opinions, including *In re Riggs,* 2006 WL 2990218 (Bankr. W.D. Mo. 2006). *In re Visnicky,* 401 B.R. 61 (Bankr. D. R.I. 2009).

Fourth option was not eliminated by BAPCPA. When the Chapter 7 debtors moved to reaffirm mortgage and personal property debt on farm but could not overcome presumption of undue hardship, court does not approve reaffirmation, but under those circumstances the debtors could retain the real and personal property so long as they were current and remained current in monthly payments. BAPCPA's changes to § 521(a)(6) require the debtor to enter into a reaffirmation agreement in order to retain personal property, but if the court does not approve the agreement, the debtors have still met the statutory requirement to retain personal property. The Code does not require entry into a reaffirmation agreement to retain real property--§§ 521(a) (6) and 362(h) apply only to personalty. *In re Hart,* 402 B.R. 78 (Bankr. D. Del. 2009).

Ride through permitted on real estate debt. Although court did not approve debtors' proposed reaffirmation of mortgage debt on which the debtors were current, finding reaffirmation not in the debtors' best interest, the court held that debts secured by real estate are not affected by §§ 362(h) and 521(a)(2)(C), which are limited to personal property interest; therefore, the "ride through" option remains for debtors who are current on real estate debt. *In re Waller,* 394 B.R. 111 (Bankr. D. S.C. 2008); *see also* "ride through" cases under **Automatic Stay**.

Attorney may not limit representation by excluding reaffirmation. Chapter 7 debtor's attorney attempted to limit representation by excluding negotiations or representation concerning reaffirmation agreements in the contract with debtor. The court found that limitation impermissible, first because entry into a reaffirmation is so important to debtors and assistance from an attorney is part of the necessary services "that make up competent representation of a Chapter 7 debtor. Second, the Code [§ 524(c)] lays the responsibility for advising a debtor

about the reaffirmation process and evaluating the effect of each agreement at the feet of debtor's counsel." *In re Minardi,* 399 B.R. 841 (Bankr. N.D. Okla. 2009).

Mortgage servicer lacks legal authority to reaffirm. At hearing on approval of a reaffirmation agreement, it became clear that mortgage servicer lacked legal interest in the underlying note and had no authority in its own right to enter into reaffirmation. *In re Waring,* 401 B.R. 906 (Bankr. N.D. Ohio 2009).

Section 524(m) doesn't apply when attorney certification is filed and no presumption of undue hardship arises. The statutory deadline in § 524(m) doesn't apply when the debtor's attorney files a certification with the reaffirmation agreement, and the agreement indicates a positive cash flow, or when other conditions of the Code are met. If no court action is required, then § 524(m) is irrelevant. *In re Clark,* 401 B.R. 75 (Bankr. D. Conn. 2009).

Excusable neglect not established for relief from approved reaffirmation. After the court had approved the debtors' reaffirmation agreement, which had been entered into against the debtors' attorney's advice, the debtors moved to rescind after the statutory time for rescission; the motion was motivated by the debtors' default in payments and by the Chapter 7 trustee's questioning whether the creditor was properly perfected. The court found that the debtors understood the consequences of reaffirmation and failed to establish cause for relief from the approval. *In re Mahannah,* 2008 WL 4951590 (Bankr. W.D. Mo. 2008).

Chapter 13 Issues

Eligibility and Means Testing

Means test is constitutional. Section 1325(b)(3)'s means testing use of state and local median income standards does not render the provision nonuniform under Art. I, § 8 of the Constitution, with the Sixth Circuit applying the same analysis used by the Supreme Court in holding the exemption opt-out constitutional. *Schultz v. United States,* 528 F.3d 343 (6th Cir. 2008), *cert. denied,* 2008 WL 4819925 (Dec. 8, 2008). *See also In re Cox,* 393 B.R. 681 (Bankr. W.D. Mo. 2008), holding that § 1325(b)'s objective standards for determination of expense deductions, rather than using the debtor's actual expenses, was rationally related to congressional limitations on judicial discretion and establishment of a floor for recovery by unsecured creditors from above-median income debtors; § 1325(b) doesn't violate a debtor's equal protection rights.

Deduction of mortgage and vehicle ownership when surrendered is permitted. Construing the phrase "scheduled as contractually due" for secured debts under § 707(b) (2) (A) (iii), the court found the statute not to be ambiguous, giving the phrase its ordinary meaning. A secured payment is contractually due on the date of the petition filing, even though the debtor may intend to surrender the collateral, and the liability on the debt may not be eliminated until discharge. The debtor may deduct the "average monthly payments on account of secured debt" payable over the 60 months, without regard to whether the debtor intends to surrender the home. As to vehicle expense, the court also holds that the debtor may deduct ownership costs for a vehicle even though there is no outstanding debt on the vehicle, following the Seventh Circuit decision, *In re Ross-Tousey,* 549 F.3d 1148 (7th Cir. 2008). The court notes that passing the means test by such deductions does not insulate the case from dismissal under § 707(b) (3). *In re Ralston,* 400 B.R. 854 (Bankr. M.D. Fla. 2009). *See, however, In re Rahman,* 400 B.R. 362 Bankr. E.D. N.Y. 2009) (In context of projected disposable income, debtor may not deduct secured debt payments on collateral proposed for surrender.).

As *Ross-Tousey* points out in its discussion, the appellate courts are divided on this issue, which typically arises in Chapter 13 cases involving disposable income issues, as follows: **Debtor may take the ownership deduction even when the vehicle is free and clear**-- *Ross-Tousey; Hildebrand v. Kimbro (In re Kimbro),* 389 B.R. 518 (B.A.P. 6th Cir. 2008); *Hildebrand v. Thomas (In re Thomas),* 395 B.R. 914 (B.A.P. 6th Cir. 2008) (debtors may deduct payments contractually obligated on petition date, notwithstanding later surrender); *Pearson v. Stewart (In re Pearson),* 390 B.R. 706 (B.A.P. 10th Cir. 2008); *see also, e.g., In re Hedge,* 394 B.R. 463 (Bankr. S.D. Ind. 2008); *In re Pearl,* 394 B.R. 309 (Bankr. N.D. N.Y. 2008). **Debtor may not take the ownership deduction**—*Ransom v. MBNA America Bank N.A. (In re Ransom),* 380 B.R. 799 (B.A.P. 9th Cir. 2007); *Babin v. Wilson (In re Wilson),* 383 B.R. 729 (B.A.P. 8th Cir. 2008) (suggesting that debtors owning high-mileage vehicles may be able to deduct $200 monthly operating expenses under IRS standards or may qualify for "special circumstances" deduction under § 707(b)(2)(B)); *see also, e.g., In re White,* 393 B.R. 436 (Bankr. N.D. Miss. 2008); *In re Coffin,* 396 B.R. 804 (Bankr. D. Me. 2008); *In re Hunt,* 2008 WL 5142183 (Bankr. S.D. Ind. Dec. 5, 2008).

Deduction of mortgage expense allowed when stay relief is granted. The debtor was permitted to deduct mortgage payments to which she was contractually obligated at filing for means test purposes, notwithstanding the

court then granted stay relief to the creditor and the debtor's subsequent eviction. The court analyzes the effect of state law on the debtor's homestead interest at the time she filed: "This court agrees with the *Burmeister* [378 B.R. 2276 (Bankr. N.D. Ill. 2007)] line of cases that neither the Debtor's intent nor postpetition events affect the Debtor's right to include the monthly mortgage payment on the means test if the Debtor had a note in effect regarding that debt on the date she filed for bankruptcy relief." *In re Willette,* 395 B.R. 308, 326 (Bankr. D. Vt. 2008).

Preconfirmation Issues, Current Monthly Income and Disposable Income

Projected disposable income, what is the starting point? Examining "the proper way to calculate the 'projected disposable income' of an above-median Chapter 13 debtor under…BAPCPA," the Tenth Circuit adopted the "forward-looking approach" used by both the bankruptcy court and BAP, which is also the "method adopted by the majority of bankruptcy courts and bankruptcy appellate panels." *Hamilton v. Lanning (In re Lanning),* 545 F.3d 1269, 1270 (10th Cir. 2008). The debtor had an increase in income during the 6-month period prior to filing Chapter 13, showing on Form B22C monthly disposable income of $1,114.l98; however, her Schedules I and J reflected excess monthly income over expenses of only $149.03. The Circuit reviewed BAPCPA's amendments to § 1325(b) and related statutes, as well as prior court opinions construing disposable income, dividing them between the "forward-looking approach" and the "mechanical approach," with the latter primarily using Form B22C as providing presumptively correct income amounts. **Forward-looking courts include**: *Coop v. Frederickson (In re Frederickson),* 545 F.3d 652 (8th Cir. 2008) (Form B22C is starting point but actual income and expenses on Schedules I & J must be considered); *Hildebrand v. Petro (In re Petro),* 395 B.R. 369 (B.A.P. 6th Cir. 2008); *Kibbe v. Sumski (In re Kibbe),* 361 B.R. 302 (B.A.P. 1st Cir. 2007); s*ee also, In re Wilson,* 2008 WL 619196 (Bankr. M.D. N.C. March 3, 2008).

Certiorari had been sought but was denied in *Frederickson v. Coop,* 2009 WL 210498 (Mar. 23, 2009), where the Eighth Circuit held that projected disposable income is a starting point, subject to replacement by actual income, *Coop v. Frederickson (In re Frederickson),* 545 F.3d 652 (8t5h Cir. 2008), *cert. denied,* 2009 WL 2120498 (Mar. 23, 2009). The petition pointed out that circuit split exists on the issue. For a recent discussion of the "conclusive approach" found in *Maney v. Kagenveama (In re Kagenveama),* 541 F.3d 868 (9th Cir. 2008), the "presumptive approach" found in *Frederickson,* and adopting

"harmonizing approach," *see In re Johnson,* 400 B.R. 639 (Bankr. N.D. Ill. 2009). The *Johnson* court points out the conflict in definitions of "current monthly income" found in § 101(10A), the 6-month look-back, and § 1325(b), with the latter utilizing a deduction of projected expenses during an applicable commitment period, concluding that § 1325(b) is more specific and therefore governs the more general statute. "The end result is a synthesis of §§ 101(10A) and 1325(b) that measures the 'current monthly income' inclusions and exclusions of § 101(10A) projected to be received by the debtor during the applicable commitment period defined by § 1325(b), reduced by the necessary expenditures incurred by the debtor during that period."

Mechanical approach courts are represented on the appellate level by *Maney v. Kagenveama (In re Kagenveama),* 541 F.3d 868 (9th Cir. 2008); *see also In re Smith,* 2008 WL 4964720 (Bankr. W.D. Wash. Nov. 14, 2008).

The *Lanning* court concludes that to make BAPCPA's definition of "disposable income" make sense with "current monthly income" one must read "a presumption into the statute—that the defined term 'disposable income' is just the starting point—which can be rebutted by showing a substantial change in circumstances bearing on how much the debtor realistically can commit to repayment of unsecured creditors as of the effective date of the plan." *Lanning*, 545 F.3d at 1278. The terms "'projected' links 'disposable income' and 'to be received in the applicable commitment period,' requiring the debtor to commit all 'disposable income' (as defined by § 1325(b)(2) and its reliance on the definition of 'current monthly income') that is 'projected…to be received in the applicable commitment period.' Under this reading, the debtor's actual circumstances at the time of plan confirmation are taken into account in order to 'project' (in other words, to 'forecast') how much income the debtor will actually receive during the commitment period, which, after deducting permitted expense, then 'will be applied to make payments' to the unsecured creditors, as the statute requires." *Lanning*, 545 F.3d at 1279.

In contrast, the *Kagenveama* court reads § 1325(b)(2) to mean that "projected disposable income" is "disposable income" projected over the applicable commitment period; therefore, if projected disposable income is a negative number, there is no relevant applicable commitment period….'Projected' is simply a modifier of the defined term 'disposable income.'" 541 F.3d at 876.

See In re Almonte, 397 B.R. 659 (Bankr. E.D. N.Y. 2008), for a discussion of this issue and contrasting of the "starting point" views. The *Almonte* court refers to the *Lanning* decision as the "crystal ball approach," rather than the "forward-

looking" approach, using "a debtor's current monthly income as a starting point for calculating projected disposable income, subject to a showing of 'substantial change in circumstances.'…The crystal ball approach to 'projected disposable income' arguably furthers Congress's intent that a debtor commit disposable income to repayment of creditors without leading to the absurd result that a debtor be required to repay more than they can afford, or an equally unintended result that a debtor who *has* post-petition disposable income need not commit that disposable income to the repayment of unsecured creditors because they had little or no disposable income prior to the petition date." The *Almonte* court refers to the *Kagenveama* opinion as following a "rear view mirror approach," one that opens the door to a debtor with actual disposal income not having to pay anything to unsecured creditors. "The divergent views and interpretations of Section 1325(b)'s 'projected disposable income' evidenced by the 'crystal ball and 'rear view mirror' approaches are both good faith attempts to resolve this question in a manner that is consistent with the intent of the statute….[T]his court believes that the line of cases adopting the 'crystal ball' approach to projected disposable income is the correct interpretation of the statute when an objection to confirmation is filed under Section 1325(b)…."

Balloon payment of long term mortgage is not equal monthly amount. Citing other cases in agreement, the BAP holds that "by its very terms, a balloon payment is not equal to the payment that preceded it, and thus violates § 1325(a) (5) (B) (iii) (I) with respect to periodic payments on a secured claim." The debtor's plan proposed to make a balloon payment to satisfy the mortgage on nonresidential real estate near completion of the plan. The BAP also rejected the argument that prohibiting such payment nullifies § 1322(b) (2), which permits modification of mortgages other than on the debtor's principal residence (this mortgage was not protected by the anti-modification provision), with the BAP disagreeing with *In re Davis,* 343 B.R. 326 (Bankr. M.D. Fla. 2006): "[T]he idea that § 1322(b) (2) or (b) (5) is at odds with § 1325(a) (5) (B) (iii) (I) is simply wrong." *Hamilton v. Wells Fargo Bank, N.A. (In re Hamilton),* 401 B.R. 539 (B.A.P. 1st Cir. 2009). *Accord, Flynn v. Bankowski (In re Flynn),* 402 B.R. 437 (B.A.P. 1st Cir. 2009), where the BAP also noted that the Code and Rules contain no mechanism for a creditor's acceptance of a plan. While silence of a creditor that receives proper notice of a plan may constitute "implied" acceptance, such "implied consent requires, however, that the secured claim holder has received both proper and adequate notice and proper and adequate service. Proper and adequate notice is a highly factual inquiry and necessarily depends on the language in the plan and the context of the case." The record

here did not permit the BAP to determine if notice and service were proper and adequate to imply acceptance.

Equal monthly payments need not begin with first plan payment. Reviewing two lines of authority, the court concludes that the position of *In re DeSardi,* 340 B.R. 790 (Bankr. S.D. Tex. 2006), is correct, that § 1325(a) (5) (B) (iii) (I) requires "payments to be equal once they begin, and to continue to be equal until they cease." This plan was not confirmed, however, because of lack of feasibility. *In re Butler,* 403 B.R. 5 (Bankr. W.D. Ark. 2009).

Debtor may not deduct payments on junior, wholly unsecured mortgage for disposable income purposes. Under Ninth Circuit authority that a wholly unsecured mortgage may be treated as unsecured in a plan, such a creditor does not fall within § 707(b) (2) (A) (iii) (I)'s term "secured creditor"; therefore, in the context of the trustee's objection to confirmation, the Chapter 13 debtor may not deduct payments for such mortgages in the determination of projected disposable income. The court declined to decide the broader issue of whether such deductions were proper for purposes of Chapter 7 eligibility. *In re Thissen,* 400 B.R. 776 (Bankr. E.D. Cal. 2009).

Debtor may deduct property taxes and insurance on residence. For projected disposable income purposes, above median debtor may deduct property taxes and homeowner's insurance that are contractually due under the mortgage; "a payment requirement in a mortgage that inures to the financial benefit of the lender is a payment 'to' that lender, as that term is used in 11 U.S.C. § 707(b)(2)(A)(iii)." *In re Bermann,* 399 B.R. 213 (Bankr. E.D. Wisc. 2009).

Relief from stay giving debtor time to sell property is not modification of mortgage. When debtor's plan proposed to give stay relief to mortgage creditor but delayed relief to permit sale of property, that provision doesn't violate § 1322(b)(2), which doesn't require maintenance of payments. The delay was for less time than state law would require for foreclosure, so creditor is not unduly delayed, distinguishing facts from *In re Proudfoot,* 144 B.R. 876 (B.A.P. 9th Cir. 1992). *In re Dunn,* 399 B.R. 909 (Bankr. W.D. Wash. 2009).

Accelerated payment of secured claims ahead of unsecured is not good faith. Confirmation is denied for lack of good faith when the plan proposed to pay secured claims before any distribution to unsecured creditors. Such preferential treatment is suspect in light of fact that debtors may convert the case after paying secured claims in full. *In re Pearson,* 398 B.R. 97 (Bankr. M.D. Ga. 2008).

Direct payment by debtor on ongoing mortgage is affirmed. Adopting the opinion of the BAP, *Cohen v. Lopez (In re Lopez),* 372 B.R. 40 (B.A.P. 9th Cir. 2007), the Ninth Circuit affirms the holding that a Chapter 13 debtor may act as disbursing agent on the long term mortgage, and BAPCPA did not alter that conclusion. Section 1326(c) provides that the trustee shall make plan payments, except as otherwise provided in the plan. The BAP had distinguished *Fulkrod v. Savage (In re Fulkrod),* 973 F.2d 801 (9th Cir. 1992), a Chapter 12 case in which dicta indicated that an impaired claim should be paid by the trustee, with the BAP stating that ongoing mortgage obligations were not modified by the plan and not impaired. *Cohen v. Lopez (In re Lopez),* 550 F.3d 1202 (9th Cir. 2008).

Under local rule, debtors fail to justify direct payment on mortgages. Under local rule, debtors who are current on mortgages at time of filing may continue paying directly, but debtors who are delinquent must make ongoing payments in the plan unless the court orders otherwise. Section 1326(c) "creates a presumption in favor of payments through the Trustee," and the trustee testified of experience demonstrating that debtors who were delinquent at filing often became delinquent postpetition, creating late charges, difficulties in record-keeping and post-discharge delinquencies when the trustee did not make the ongoing mortgage payments. These debtors failed to show that they would be able to keep the mortgage payments current, and feasibility was an issue. *In re Carey,* 2009 WL 613581 (Bankr. W.D. Mo. Mar. 9, 2009).

What is the applicable commitment period? Agreeing that the statutory language of § 1325 is "rather murky," the court concludes that the applicable commitment period is "pegged to a debtor's 'current monthly income'" but that "natural language of § 1325(b)(1)(B) sets forth only a requirement that a debtor make payments to unsecured creditors from projected disposable income received. It does not impose a required plan length….Section 1325(b)(1)(B) is a forward looking provision that does point to a temporal period of time that can be three or five years into the future. However, that temporal period is a reference to define the boundaries of the disposable income to be included in the plan. For example, the statute requires an above median debtor to provide for five years of projected disposable income in the plan. It does not require the plan to extend for any certain length of time." *In re Lopatka,* 400 B.R. 433 (Bankr. M.D. Pa. 2009).

Income of nonfiling spouse is included but deducted if not used regularly for household expenses. Although a debtor initially must include the nonfiling spouse's income in current monthly income, it is deducted if that income is not

used regularly for the household expenses of the debtor or debtor's dependents. *In re Sharp,* 394 B.R. 207 (Bankr. C.D. Ill. 2008).

Current monthly income includes state unemployment compensation received in six-month look-back. When Chapter 13 debtor received unemployment compensation within the six months prepetition from the state rather than federal government, the benefit was not received under the Social Security Act; therefore, it is income used in CMI calculation. *In re Baden,* 396 B.R. 617 (Bankr. M.D. Pa. 2008).

Earned income credit portion of tax refund is current monthly income. That portion of a tax refund attributable to earned income credit and received within six-month window is income included in CMI. *In re Royal,* 2008 WL 4900527 (Bankr. N.D. Ill. Nov. 7, 2008).

"Derived" adds nothing to "received." Section 101(10A)'s definition of "current monthly income" uses both terms "derived" and "received," but "derived" adds no additional meaning to "received"; it is mere surplusage; "the court concludes that the definition of 'current monthly income'…refers to income received during the prescribed six-month period, and that no additional criterion that the income actually be earned during that period exists or was intended when BAPCPA was drafted and enacted." *In re Burrell,* 399 B.R. 620 (Bankr. C.D. Ill. 2008).

Hanging Paragraph Issues

Hanging paragraph is mandatory confirmation requirement. Bankruptcy court has no discretion to confirm a plan that proposes to bifurcate purchase money secured claim on 910 vehicle. The hanging paragraph of § 1325(a) is a mandatory requirement for confirmation. *Shaw v. Aurgroup Fin. Credit Union,* 552 F.3d 447 (6th Cir. 2009).

Surrender of 910 vehicle does not eliminate deficiency claim. The Eleventh Circuit has recently joined other circuits in holding that the debtor may not eliminate the car lender's unsecured deficiency claim by surrender of the vehicle purchased for personal use within 910 days of the bankruptcy filing. "A plain reading of the hanging paragraph makes clear that Congress intended to (and did) make Section 506(a) inapplicable to a 910 vehicle. In such a situation, we agree with the Seventh Circuit that 'by knocking out § 506, the hanging paragraph leaves the parties to their contractual entitlements." *DaimlerChrysler Fin. Servs. America LLC v. Barrett (In re Barrett),* 543 F.3d 1239, 1246 (11th Cir. 2008). The other circuits agreeing on the result, but with different rationale are:

Tidewater Fin. Co. v. Kenney, 531 F.3d 312 (4th Cir. 2008); *AmeriCredit Fin. Servs., Inc. v. Long (In re Long)*, 519 F.3d 288 (6th Cir. 2008); *In re Wright,* 492 F.3d 829 (7th Cir. 2007); *Capital One Auto Fin. V. Osborn*, 515 F.3d 817 (8th Cir. 2008); *AmeriCredit Fin. Servs., Inc. v. Moore,* 517 F.3d 987 (8th Cir. 2008); *DaimlerChrysler Fin. Servs. Ams. LLC v. Ballard (In re Ballard),* 526 F.3d 634 (10th Cir. 2008); *Wells Fargo Fin. Acceptance v. Rodriguez (In re Rodriguez),* 375 B.R. 535 (B.A.P. 9th Cir. 2007).

Negative Equity Issues. Christopher Frost, "Negative Equity and the Hanging Paragraph: What is a Purchase Money Security Interest and What Law Should Apply," 29 No. 3 Bankruptcy Law Letter (Thomson Reuters March 2009), available on WestLaw, concludes: **"**Regardless of one's view of the merits of these observations regarding Congress's intent, one thing seems clear--Congress enacted the hanging paragraph with bankruptcy law, not state law, in mind. An analysis that focuses on the use of the term "purchase-money security interest" in the context of the broader purposes of BAPCPA is likely to yield more satisfying results that an analysis that simply looks to the unrelated use of the term in the UCC. As the drafters of the UCC themselves recognized, their definition of the term purchase-money security interest has nothing to do with the fresh start policies underlying the Code. Even further afield are analyses that look beyond the UCC to state consumer disclosure statutes that are unrelated either to the UCC or the Code. These fragile interpretive strings cannot cover for the fact that Congress failed utterly to enact a provision that yields a clear and uncontroversial interpretation."

Negative equity: Dual status or transformation rule? Adopting a "dual status" rule, a panel of the Ninth Circuit BAP held that when the debtor trades in a vehicle, including in the new vehicle financing "negative equity" on the trade-in, the negative equity is not protected from stripping by the hanging paragraph of § 1325(a), but the remainder of the financing, the actual purchase money security interest, continues to be protected. That paragraph's use of "purchase money security interest" is construed consistently with the way that term is used in the Uniform Commercial Code, and the term "negative equity" is not equivalent to the other types of expenses incurred when a creditor acquires rights in collateral, with the panel citing UCC § 9-103, Off. Comment 3. At least as the term "price" is used in California's version of UCC § 9-103(a)(1), negative equity is not included in "price." Concluding that the creditor's financing of negative equity is not protected from modification, the panel reviews the two views that have been taken by the courts. The "transformation" rule transforms the entire financing

into a non-PMSI, *see, e.g., In re Burt,* 378 B.R. 352 (Bankr. D. Utah 2007); the "dual status" rule allows the financing to be divided into its PMSI and non-PMSI portions. "Adopting the Dual Status Rule would treat debtors who contract separately to pay off a deficiency on a trade-in the same as those who roll that deficiency into the new car purchase. It would ensure that whether assumption of unsecured debt is paid in full in a chapter 13 case turns not on the form in which the debt was satisfied but on the substance of the transaction." *Americredit Fin. Servs., Inc. v. Penrod (In re Penrod),* 392 B.R. 835, 859-60 (B.A.P. 9th Cir. 2008). *See also, In re McCauley,* 2008 WL 5104235 (Bankr. D. Colo. Nov. 20, 2008) (applying dual status); *In re Hall,* 2008 WL 5102274 (Bankr. S.D. W.Va. Dec. 3, 2008) (applying dual status); *In re Hargrove,* 2008 WL 5170399 (Bankr. M.D. Tenn. Dec. 10, 2008) (applying dual status to gap insurance and negative equity); *In re Crawford,* 397 B.R. 461 (Bankr. E.D. Wis. 2008) (negative equity not PMSI). *Compare In re Carlton,* 2008 WL 5045908 (Bankr. M.D. Ala. Nov. 24, 2008) (under *In re Graupner,* 537 F.3d 1295 (11th Cir. 2008), negative equity financed in new purchase is part of PMSI). The First Circuit has certified the issue of whether negative equity is included within PMSI under New York's UCC to the New York Court of Appeals. *Reiber v. GMAC, LLC (In re Peaslee),* 547 F.3d 177 (1st Cir. Oct. 2, 2008).

Fourth Circuit holds negative equity protected by hanging paragraph. Section 1325(a)'s hanging paragraph's protection of purchase moneys security interests includes negative equity financed as part of a trade-in; negative equity financing is a crucial part of the purchase transaction. *Wells Fargo Fin. Acceptance v. Price (In re Price),* 562 F.3d 618 (4th Cir. 2009).

Negative equity and gap insurance financing are part of purchase price under state law. Looking to definition of "cash sale price" under Illinois Motor Vehicle Retail Installment Sales Act, state law includes within PMSI amounts for taxes, fees, gap insurance, service contracts and negative equity. Comment to Illinois UCC also includes those items within "price." Court cites opinions going both ways on negative equity. *In re Smith,* 401 B.R. 343 (Bankr. S.D. Ill. 2008).

Till interest applies to 910 creditor. Even though creditor is protected from cramdown by hanging paragraph, *Till* interest rate calculation still applies to such creditor. Here, contractual interest rate is less than *Till* allows. *Ford Motor Credit Co., LLC v. Robertson,* 396 B.R. 672 (S.D. W.Va. 2008).

Vehicle not purchased for personal use is not "any other thing of value." Agreeing with the majority of courts addressing the issue, when the debtor's purchase of a vehicle was not for personal use, therefore not covered by the first clause of § 1325(a)'s hanging paragraph, the court held that the vehicle does not fall with the second clause for "collateral…consist[ing] of any other thing of value….The result hinges on the meaning of 'other thing of value' as that term is used in the statute….First, since the 'hanging paragraph' creates an exception to the general right of a debtor to value secured claims under § 506, any ambiguity should be resolved in favor of limiting, not expanding the exception. Second, the scant legislative history supports the majority interpretation." *In re Horton,* 398 B.R. 73 (Bankr. S.D. Fla. 2008); *contra In re Littlefield,* 388 B.R. 1 (Bankr. D. Me. 2008).

Binding Effect of Confirmation

Disagreeing with other circuits and its own BAP, a panel of the Ninth Circuit concluded that when the student loan creditor had notice of a plan providing for discharge of a student loan, without the filing of a separate adversary proceeding, and the creditor took no action to object to confirmation or otherwise seek timely relief from confirmation, the creditor is bound by § 1327(a)'s effect of confirmation. The panel sees no reason to recommend *en banc* reconsideration of *Great Lakes Higher Educ. Corp. v. Pardee (In re Pardee),* 193 F.3d 1083 (9th Cir. 1999). Key to the decision is the panel's distinction between what other circuits have seen as a due process problem when the debtor doesn't follow the adversary proceeding route and this panel's view that notice of a plan means what § 1327(a) says—binding effect. The opposing circuits "divine some sort of conflict between the Bankruptcy Code's finality provision, 11 U.S.C. § 1327(a), and those provisions of the Code and Rules that call for an adversary proceeding before a student loan debt may be discharged. We see no such conflict; both provisions can operate fully, within their proper spheres." *Espinosa v. United Student Aid Funds, Inc.,* 553 F.3d 1193 (9th Cir. 2008). Assuming proper notice of the plan proposing discharge, as existed here, "the creditor can objet to the plan until the debtor shows undue hardship in an adversary proceeding." *Id.* Even if the confirmed plan contains provisions that are not permitted by the Code, the finality of confirmation recognizes that such errors may be waived by creditors who have notice and opportunity to object.

Res judicata is not really the issue for this panel, since that doctrine applies to the preclusive effect of a judgment given in another case, not one in the same case. Rule 60(b)(4) or (6) may provide a remedy for setting aside a

judgment, but only under the limitations of those Rules, with the panel finding that notice to the creditor of the plan was constitutionally adequate to overcome any due process argument: "The three circuits that have held that the creditor is denied due process in circumstances such as these appear to have a different view of what due process requires. As best we can follow their reasoning, it is that a creditor who is entitled to heightened notice by statute is also entitled to such heightened notice as a matter of due process….To begin with, we find it both wrong and dangerous to hold that the standard for what amounts to constitutional adequate notice can be changed by legislation.…Even if Congress could affect the constitutional standard, it didn't do so here: Congress made it quite clear that a creditor need only get ordinary notice of a Chapter 13 plan to be bound by its terms. That Congress provided heightened notice requirements for an adversary proceeding…is of no consequence….We reject the idea that a creditor who is in the business of administering student loans has a *constitutional* right to ignore a properly served notice that clearly specifies that its debt will be discharged on successful completion of the plan." *Id.* at *8-9. The panel capped its opinion by overruling those bankruptcy opinions in the Ninth Circuit that denied confirmation to plans providing for discharge by declaration, even when properly noticed, as well as those sanctioning attorneys for including such provisions in plans. In the Ninth Circuit, discharge by declaration is revived and a clear circuit split is set up. *Espinosa v. United Student Aid Funds, Inc.,* 553 F.3d 1193 (9th Cir. 2008), *amending prior opinion* at 2008 WL 4426634 (9th Cir. Oct. 2, 2008).

***Espinosa* applied by district court.** Refusing to dismiss the debtor's complaint to recover funds collected by student loan creditors on debts discharged-by-declaration in completed plan, the district court applies *Espinosa v. United Student Aid Funds, Inc.,* 553 F.3d 1193 (9th Cir. 2008), where the plan provided for discharge of student debt, notice was given of the plan and no objections were filed. *Needelman v. Penn. Higher Educ. Assistance Agency,* 399 B.R. 695 (S.D. Cal. 2009).

Confirmed plan curing mortgage could not be modified to strip down. The debtor and mortgage creditor had stipulated that the creditor was undersecured, but the debtor's confirmed plan did not rely on that status, instead providing for curing of the arrearage and maintenance of the mortgage payments "outside the plan." After confirmation, the property appreciated in value, and the debtor moved to modify the plan to adopt the stipulation and to pay only the stripped down amount of the secured claim**.** The district court held that the proposed modification violated § 1329(a) (1)'s provisions for changing the amount of

payments to a "class," with this modification affecting only a single creditor. *Columbia Nat'l, Inc. v. Brown (In re Brown),* 399 B.R. 574 (D. Conn. 2008).

Section 1330 trumps Rule relief from confirmation. Relying on *Mason v. Young (In re Mason),* 237 B.R. 791 (B.A.P. 10th Cir. 1999), § 1330 is exclusive means for obtaining relief from confirmation, and Rules 9023 and 9024 are applicable only in instances where adequacy of notice of the plan is at issue. *In re Smith,* 2009 WL 243396 (Bankr. D. Kan. Jan. 27, 2009).

Modification of plan

Trustee has standing to object to debtor's reclassification of claim. Under § 1302(b) (3)'s duty to properly disburse payment of claims, the Chapter 13 trustee has standing to object to the debtor's motion to reclassify a claim; here, the debtor moved to reclassify a secured claim to unsecured, asserting that the documentation with the proof of claim did not show a properly perfected security interest in an ATV, and the trustee objected on the basis that the debtor had executed a purchase money security interest. "Because a trustee must be able to verify that secured claims are, in fact, secured, it necessarily follows that a trustee has standing to object when a debtor attempts to reclassify a secured claim as an unsecured claim." The Second Circuit cites the Fifth and Ninth Circuits as in agreement. *Overbaugh v. Household Bank N.A. (In re Overbaugh),* 559 F.3d 125 (2d Cir. 2009).

Discharge

Interpretation of § 1328(f)'s 4-year bar. Concluding "that § 1328(f) sets a date-of-filing trigger," the debtor who filed a prior Chapter 7 case more than four years before filing the current Chapter 13 case is eligible for Chapter 13 discharge, even though the Chapter 7 discharge was granted within that four-year period. The focus of the opinion is on when the clock begins to run, the date of filing the prior case or the date of discharge. The Chapter 13 trustee objected to the debtor receiving a second discharge, but the Sixth Circuit panel applied "the rule of last antecedent" to create a presumption that "qualifying phrases attach only to the nearest available target…Read with this rule in mind, § 1328(f)(1)'s pieces fit sensibly together, each phrase modifying the one that comes before it and each phrase having an independent task to do. The 'in a case filed under' phrase that begins subsection (f)(1) modifies 'received a discharge,' and the phrase that frames the four-year window—'during the 4-year period preceding [the second petition]'—modifies the 'filed under' fragment that comes immediately before it." The panel cited *Bateman v. Bateman (In re Bateman),* 515 F.3d 272 (4th Cir. 2008), as similarly interpreting § 1328(f)(2)'s two-year

period between Chapter 13 discharges. *Carroll v. Sanders (In re Sanders),* 551 F.3d 397 (6th Cir. 2008).

Interpretation of § 1328(f)'s 2-year bar. Another BAP applied § 1328(f)(2)'s bar on discharge within two years of receiving a prior Chapter 13 discharge consistently with *Bateman* and *Sanders,* finding "no exceptions to the plain meaning of § 1328(f) that would cause us to apply the statute other than as written….As such, we conclude that the provisions of the statute dictate that the period between the first and second cases must be calculated as written, from the date of filing to the date of filing." *Gagne v. Fessenden (In re Gagne),* 394 B.R. 219 (B.A.P. 1st Cir. 2008).

Determination of undue hardship discharge of student loan debt is ripe prior to plan completion. Discussing the "two components of the ripeness doctrine: constitutional ripeness and prudential ripeness," the Sixth Circuit BAP held that the debtor's complaint to determine discharge of a student loan on the basis of undue hardship was ripe prior to plan completion, and "the contingency of [the debtor's] discharge does not create a constitutional ripeness impediment to the bankruptcy court's resolution of this adversary proceeding….Delay of the dischargeability determination would deprive [the debtor] of the opportunity to pay any nondischargeable student loan debt and attorneys fees related to the adversary proceeding through the chapter 13 plan as well as potential loss of the automatic stay." *Cassim v. Educ. Credit Mgmt. Corp. (In re Cassim),* 395 B.R. 907, 911-12 (B.A.P. 6th Cir. 2008). The panel distinguished *Bender v. Educ. Credit Mgmt. Corp. (In re Bender),* 368 F.3d 846 (8th Cir. 2004), as being based on prudential ripeness rather than constitutional ripeness, while this appeal was argued on the basis of constitutional ripeness alone. **See also** *Educational Credit Management Corp. v. Coleman (In re Coleman),* 560 F.3d 1000 (9th Cir. 2009). Although the Chapter 13 debtor's discharge will not occur until plan completion, that does not defeat constitutional and prudential ripeness of the debtor's complaint to determine undue hardship of student loan debt earlier in the case.

Mortgage Issues

First Circuit finds plan not specific on plan payment application. Reversing an award of damages under § 105(a) for the creditor's violation of § 1322(b) in failing to properly apply mortgage payments under the confirmed plan, the Circuit found insufficient specificity in the plan to impose on the creditor liability for failing to distinguish between and apply prepetition arrearage and postpetition ongoing mortgage payments. Section 1322(b) concerns permissive plan

provisions, not mandatory ones. *Ameriquest Mortgage Co. v. Nosek (In re Nosek),* 2008 WL 4445707 (1st Cir. Oct. 3, 2008). *Compare Rodriquez v. Countrywide Home Loans, Inc. (In re Rodriguez),* 2008 WL 4371669 (Bankr S.D. Tex. Sept. 18, 2008) (discussing the binding effect of confirmation as imposing obligations on the lender to comply with "the allocation scheme provided for by the plan); and *In re Aldrich,* 2008 WL 4185958 (Bankr. N.D. Iowa Sept. 4, 2008) (some plan restrictions on mortgage creditor violate antimodification provision in Code).

Antimodification protection requires real property. The amendment to the definition of the debtor's principal residence in § 101(13A) did not change the requirement in § 1322(b) (2) that only property secured by real estate is protected from modification. Here, mobile home creditor was not protected. *In re Ennis,* 558 F.3d 343 (4th Cir. 2009).

TILA "tolerance for accuracy" defense applied. In the Chapter 13 debtor's adversary proceeding alleging failure to receive her disclosure and seeking rescission, under the Truth in Lending Act, the Third Circuit found the application of the Act's "tolerance for accuracy' defense to be a general one that may be raised by the defendant through its reliance on the TILA instead of affirmatively pleading under FED. R. CIV. P. 8(c). "Option One's general denial that it committed any disclosure violations was sufficient to preserve the tolerance issue. Given that denial, and given the absence of any real prejudice suffered by [the plaintiff], the Bankruptcy Court's sua sponte application of [15 U.S.C.] § 1605(f) was not improper." *Sterten v. Option One Mortgage Corp. (In re Sterten),* 546 F.3d 278, 288 (3d Cir. 2008).

Debtor not entitled under § 108(a) to equitably toll TILA limitation. Under § 108(a)'s language, the trustee may commence a time-barred cause of action within its two-year extension, but the debtor is not given that benefit. When the debtor alleged that the mortgagee violated Truth in Lending Act but that Act's one-year limitation had expired, bankruptcy filing didn't save the action. Section 108(a) is intended to benefit the bankruptcy estate. *Roach v. Option One Mortgage Corp.,* 598 F.Supp.2d 741 (E.D. Va. 2009).

U.S. Trustee has standing to pursue discovery from mortgage creditor. Under § 307, the U.S. Trustee has standing to discover the mortgage creditor's practices in Chapter 13 cases. The opinion adopts the reasoning of *In re Countrywide Home Loans, Inc.,* 384 B.R. 373 (Bankr. W.D. Pa. 2008), and cites the majority of opinions in accord, as well as those disagreeing on standing. *In re Wilson,* 2009 WL 304672 (Bankr. E.D. La. Feb. 6, 2009).

Notice to mortgage creditor that mortgage is current is insufficient. When the motion deeming mortgage to be current upon plan completion was not served under Rule 7004(b)(3) to the attention of an officer, managing or general agent or other authorized agent, the creditor is given relief from the order. An attorney who had appeared in the case for the creditor did not sufficiently participate in the case to justify implied authority to accept service. *In re Ochoa,* 399 B.R. 563 (Bankr. S.D. Fla. 2009).

Requiring mortgage creditor to obtain approval before assessing fees is improper modification. Disagreeing with some courts and citing others in agreement, Rule 2016 does not require the mortgage creditor to obtain court approval before assessing attorney fees postpetition, and putting such requirement in plan is a modification of the creditor's contractual right. However, plan requirement that creditor apply plan payments in allocation between prepetition arrearage and ongoing obligation is not a contractual modification; rather, that provision states the statutory cure provisions. *In re Booth,* 399 B.R. 316 (Bankr. E.D. Ark. 2009).

Plan ambiguous as to stay remaining in effect until resolution of TILA claims. Confirmed plan provided for litigation of debtor's recission claims under TILA in state court, that mortgage would be paid outside the plan after conclusion of that litigation, and that automatic stay would remain until "resolution" of that litigation. The court reviews principles for the stay to remain in effect after confirmation, and the effect of § 1327(b)'s vesting, along with § 362(c) (1)'s termination of the stay as to property revested in the debtor. Since this plan did not include any terms for payment of the mortgage, the "outside the plan" language did not provide for the mortgage claim for purposes of § 362(d) (1)'s adequate protection requirement. Since the plan did not provide for the mortgage claim and the debtor failed to make periodic payments on the mortgage or to otherwise adequately protect the creditor, the mortgage creditor is entitled to stay relief under § 362(d)(1). *In re Stuart,* 402 B.R. 111 (Bankr. E.D. Pa. 2009).

Loan servicer doesn't violate stay by filing proof of claim for increased postpetition mortgage obligations under loan contract. *See* discussion of *Campbell v. Countrywide Home Loan, Inc.,* 2008 WL 4542843 (5th Cir. Oct. 13, 2008), under **Automatic Stay.**

Debtors are bound by confirmation from seeking disgorgement of excess interest. On appeal in complaints filed by Chapter 13 debtors, the district court affirmed the holding that § 1327(a) binds the debtors, preventing them from

seeking disgorgement of what they now contend was overpayment of interest to the mortgage creditors. The debtors in their confirmed plans had proposed to pay the interest now subject to attack under their argument that § 1322(e) was a mandatory provision that should have precluded interest on the curing of their mortgages. The district court did not reach the issue of whether that section was mandatory or permissive, instead holding that "nothing in § 1322(e) prevents the bankruptcy court from holding the debtors to their own proposals." *Ruhl v. HSBC Mortgage Services, Inc.,* 399 B.R. 40 (E.D. Wis. 2008).

Mortgage creditor's failure to properly apply payments violates § 1322(b)(5) cure. When the creditor incorrectly applied postpetition contractual payments to prepetition interest and to oldest installment due, plan provisions for curing prepetition default were not followed; creditor failed to recognize that confirmed plan divided debt into two claims—ongoing mortgage and prepetition arrearage. Purpose of confirmed plan is to bring mortgage current, and creditor is required to make corrections to its accounting. *Boday v. Franklin Credit Mgmt. Corp. (In re Boday),* 397 B.R. 846 (Bankr. N.D. Ohio 2008).

U.S. Trustee fails to state cause of action for monetary damages. Although the court has § 105 authority to sanction abuse of process and abusive litigation, U.S. Trustee's complaint against Countrywide Home Loans failed to state cause of action for monetary damages, when the U.S. Trustee suffered no damage; U.S. Trustee's statutory authorization doesn't include pursuing punitive sanctions on behalf of the public. *Walton v. Countrywide Home Loans, Inc. (In re Sanchez),* 2008 WL 4467207 (Bankr. S.D. Fla. Oct. 2, 2008); *rev'd and remanded,* No. 08-23337 (S.D. Fal. June 9, 2009) (concluding that U.S. Trustee could recover monetary sanctions and injunctive relief).

Dismissal

Case properly dismissed on debtor's failure to file payment advices. The bankruptcy court properly dismissed the Chapter 13 case when the debtor failed to comply with § 521(a) (1) (B) (iv)'s requirement to file payment advices within 15 days of filing the case. "The statute is clear that, if such information is not timely filed, the case is subject to dismissal, whether 'automatic' or by court order," with the Circuit finding it unnecessary to address whether automatic dismissal is required. *In re Daniel,* 2009 WL 382434 (10th Cir. Feb. 17, 2009) (unpublished).

No absolute right to voluntarily dismiss Chapter 13 case. After failing to turn over arbitration awards to the trustee, the bankruptcy court sua sponte converted

the case to Chapter 7, but before the conversion order was entered, the debtor voluntarily moved to dismiss the case, with the Ninth Circuit applying the rationale of *Marrama v. Citizens Bank of Massachusetts,* 549 U.S. 365, 127 S.Ct. 1105, 166 L.Ed.2d 956 (2007), to hold "that the debtor's right of voluntary dismissal under § 1307(b) is not absolute, but is qualified by the authority of a bankruptcy court to deny dismissal on grounds of bad-faith conduct or 'to prevent an abuse of process.' 11 U.S.C. § 105(a)." *Rosson v. Fitzgerald (In re Rosson),* 545 F.3d 764, 774 (9th Cir. 2008); *accord In re Letterese,* 397 B.R. 507 (Bankr. S.D. Fla. 2008).

Case is dismissed for failure to file tax returns when trustee doesn't hold open § 341 meeting. The Chapter 13 debtor failed to file tax return for a prepetition tax year, as required by § 1308, and the U.S. Trustee moved to dismiss the case. (The debtor argued that she had obtained an IRS extension to file and that § 1308 was inapplicable.) Addressing the issue of what § 1307(e)'s dismissal provisions require and what § 1308(b) (1) means by the trustee "hold[ing] open" the § 341 meeting, the BAP reviews cases and authority construing § 1308(b), concluding that the phase "'the trustee may hold open'…requires the trustee to exercise discretion and take an affirmative step to hold the meeting open for a finite period of time." Here, the trustee merely opined that the meeting was held open because she did not announce a conclusion of the meeting. "The trustee gave no indication that she had affirmatively exercised any discretion with respect to the meeting or that she had taken any steps to hold the meeting open." As to the debtor's argument concerning an IRS automatic extension to file the return, § 1308(a) controls—the return was due on or before the meeting, unless the trustee took the affirmative step of holding open the meeting. Under these circumstances, § 1307(e) mandates dismissal of the case upon the U.S. Trustee's motion. *United States v. Cushing (In re Cushing),* 401 B.R. 528 (B.A.P. 1st Cir. 2009).

Undistributed funds are not paid to debtor after dismissal. After the confirmed-plan case was dismissed, which followed the pro se debtor's refusal to pay a sanction awarded to a charter school as a result of the debtor's "acrimonious" and frivolous litigation, the trustee moved to pay $1,267.21 on hand to the holder of the sanction award, and the debtor objected. Upon the debtor's failure to appear at the hearing, the bankruptcy court ordered the funds paid, less trustee commission, to the sanction claimant. The BAP affirmed, holding that the debtor's failure to appear was sufficient reason. *Stevenson v. Bankowski (In re Stevenson),* 399 B.R. 289 (B.A.P. 1st Cir. 2009).

Creditor with disallowed claim has standing to move for bad faith dismissal after confirmation in pre-BAPCPA case. Although the creditor's claim had been disallowed on the trustee's time-barred objection, the creditor was still a party in interest with standing to move for case dismissal, and the confirmation order in pre-BAPCPA case did not bar dismissal motion based on debtor's bad faith, with the BAP concluding that the binding effect of confirmation did not bar the motion since prior to BAPCPA amendments the bankruptcy court was not required to make a finding that the debtor filed the case in good faith as a part of its confirmation order. "The Bankruptcy Code has always contained [the provision that the plan be proposed in good faith] and dictated that it be met in order that a Chapter 13 plan be confirmed….But [the] requirement [that the case be filed in good faith] was not applicable to this pre-BAPCPA case. When confirming the Chapter 13 plan in this case, the Debtor's good faith in filing her petition was nether raised no litigated, nor was the bankruptcy court required to make that determination. Accordingly neither claim nor issue preclusion apply." *Martinez v. Arce (In re Martinez),* 397 B.R. 158 (B.A.P. 1st Cir. 2008).

Claims procedure

Claims allowance process trumps Fair Debt Collections Practices Act complaint. Reversing the bankruptcy court, the Ninth Circuit BAP held that claims brought by the Chapter 13 debtor under Washington's Consumer Protection Act for the creditor's filing of proofs of claim on time-barred debts were preempted by the Code's claims process, and the FDCPA has no application in the claims process. Objecting to a claim as being time-barred under state law is a simple process for debtors. The concurring judge observed that the act of filing a proof of claim is not a debt collection activity under the FDCPA. *B-Real, LLC v. Chaussee (In re Chaussee),* 399 B.R. 225 (B.A.P. 9th Cir. 2008).

When the debtors alleged violations of FDCPA related to creditor's filing of proof of claim, court holds that claims allowance process trumps the FDCPA, limiting application of that Act in bankruptcy cases to situations involving automatic stay violations or discharge issues. *Pariseau v. Asset Acceptance, LLC (In re Pariseau),* 395 B.R. 492 (Bankr. M.D. Fla. 2008).

Claims bar date reset upon reinstatement of dismissed case. Acknowledging that "Rule 9006(b) (3) appears to unambiguously preclude any equitable discretion on the part of a bankruptcy court to extend or toll [the Rule 3002(c)] deadlines," the court applied rationale from its Fifth Circuit authority

under Rules 4004 and 4007, to "nullify original case deadlines and recalculate them when there has been the extenuating circumstance of disruption of a case….This court holds that *where a case is disrupted*, such as through a stay or dismissal, and a proof of claim deadline runs prior to the reinstatement of the case, a court has the power to nullify the original proof of claim deadline and recalculate it." *In re Gulley*, 400 B.R. 529 (Bankr. N.D. Tex. 2009) (citing *Coston v. Bank of Malvern*, 987 F.2d 1096 (5th Cir. 1992) (approving nullification and resetting of deadlines under Rules 4004 and 4007) and *State Bank & Trust, N.A. v. Dunlap (In re Dunlap)*, 217 F.3d 311 (5th Cir. 2000) (approving resetting of § 341 meeting and resulting Rule 4007 deadline when case was dismissed in error).

Debtor has no private right of action arising from creditor's proof of claim. The debtor objected to creditor's electronic proof of claim and moved to redact full social security number and birth date that were included in proof of claim attachments. The court ordered that all attachments to the proof of claim be removed from the ECF system, and the debtor then filed a complaint that alleged multiple violations for the creditor's failure to redact privacy-protected information. Bankruptcy Rule 9037 addresses privacy protections concerning filings made with the court, and that Rule's remedies had already been applied through the order removing the offending attachments. The court found no private right of action under § 107, which provides for public access to court records but also protects an individual's privacy in certain respects. The legal sufficiency of the proof of claim is not otherwise attacked by the debtor. No private right of action existed under the Gramm-Leach-Bliley Act or the E-Government Act of 2002. Section 105 does not create a private right of action that does not otherwise exist. The debtor's allegation of negligent infliction of emotional distress is dismissed also, for failure to sufficiently state a claim for that tort. The only action surviving dismissal is the debtor's claim for a contempt finding; the court has authority under § 105(a) for contempt if the ultimate finding is that creditor violated § 107. *French v. American General Fin. Sers. (In re French),* 401 B.R. 295 (Bankr. E.D. Tenn. 2009).

Creditors may have standing to object to other creditor's claims. The Chapter 7 debtor typically lacks standing to object to creditors' claims, but creditors have a pecuniary interest, giving standing to object as parties in interest, if there either is no trustee appointed or the trustee refuses to act. *In re Ulz,* 401 B.R. 321 (Bankr. N.D. Ill. 2009).

Debtor's objection to claim sustained when state court lacked personal jurisdiction. Although state court had entered default judgment to creditor, that court lacked personal jurisdiction when the service of process was improper, and the bankruptcy court was not required to give full faith and credit to the judgment. The debtor's objection to the claim established that the creditor never had a contractual relationship with the debtor, making the debt unenforceable under state law. *In re Hall,* 403 B.R. 224 (Bankr. D. Conn. 2009).

How much documentation is required? Citing *In re Kinkaid,* 388 B.R. 610 (Bankr. E.D. Pa. 2008), one court holds that all Bankruptcy Rule 3001 requires is writing to show the claimant acquired the claim, not that the claimant have proof beyond question that it holds the claim. *In re Cleveland,* 396 B.R. 83 (Bankr. N.D. Okla. 2008). *Compare In re Samson,* 392 B.R. 724 (Bankr. N.D. Ohio 2008) (adopting *B-Line, LLC v. Kirkland (In re Kirkland),* 379 B.R. 341 (B.A.P. 10th Cir. 2007) and finding sufficient documentation for prima facie validity); *B-Real, LLC v. Melillo (In re Melillo),* 392 B.R. 1 (B.A.P. 1st Cir. 2008) (assignee's documentation insufficient); *Stauder v. eCast Settlement Corp. (In re Stauder),* 396 B.R. 609 (Bankr. M.D. Pa. 2008) (finding documentation insufficient to establish prima facie validity); and *see In re Andrews,* 394 B.R. 384 (Bankr. E.D. N.C. 2008) (Judge Small suggests need for local and national rules addressing claim documentation).

Amending claims to add documentation comes too late. Another court rejects the assignee's amendment of its proof of claim on the day of the objection hearing, also holding that Texas law requires a creditor to produce evidence of an enforceable contract; therefore, insufficient documentation of ownership of the claim results in disallowance. *In re Gilbreath,* 395 B.R. 356 (Bankr. S.D. Tex. 2008). *Compare In re Fleming,* 2008 WL 4736269 (Bankr. E.D. Va. Oct. 15, 2008) (amended claim had sufficient documentation to show assignment).

Jurisdiction and Court Powers

Bankruptcy court has authority to suspend attorney. Bankruptcy court has inherent authority under § 105(a) to sanction an attorney, including suspension from practice in all bankruptcy courts in the district; however, remand is ordered for the bankruptcy court to consider the reasonableness of six-month suspension, using ABA standards, as required by prior Ninth Circuit BAP authority, *In re Lehtinen,* 332 B.R. 404 (B.A.P. 9th Cir. 2005) and *In re Crayton,* 192 B.R. 970 (B.A.P. 9th Cir. 1996). *In re Brooks-Hamilton,* 400 B.R. 238 (B.A.P. 9th Cir. 2009).

Debtor forfeits exclusive bankruptcy court jurisdiction by failing to schedule creditor. When the debtor failed to schedule a known creditor or to otherwise notify that creditor of the bankruptcy filing, the debtor forfeited the right to have a dischargeability determination made only by the bankruptcy court, citing *In re Franklin,* 179 B.R. 913 (B.A.P. 9th Cir. 1995). After the debtor received a discharge, the plaintiff sued him and other defendants in state court for Fair Debt Collection Practices Act violations, related to collection and garnishment on a judgment that had been set aside, and the action was removed to U.S. District Court. The debtor, a former collections manager, did not amend Chapter 7 schedules to add the plaintiff after the action was filed. *Johnson v. JP Morgan Chase Bank, et al.,* 395 B.R. 442 (E.D. Cal. 2008).

Appeals

Payment by IRS of refunds after denial of stay relief for setoff did not moot appeal. The bankruptcy court denied motion by IRS for stay relief to permit set off against repetition tax refunds, and by administrative mistake IRS paid the refunds to the debtor, but the BAP holds that this payment did not make IRS's appeal constitutionally or equitably moot. Under Ninth Circuit authority, the appellate court may still fashion an effective remedy when payment has been made to a party in the appeal. The fact that IRS did not obtain a stay pending appeal doesn't prevent hearing the appeal, when the payment was made by administrative error. The BAP rejects contrary authority from the Eighth Circuit BAP, *IRS v. Ealy (In re Ealy)*, 396 B.R. 20 (B.A.P. 8th Cir. 2008), where that court held that the payment destroyed mutuality of debt. The Ninth Circuit BAP commented that *Ealy* "summarily ignores basic principles that underlie the doctrine of constitutional mootness." *United States v. Gould (In re Gould),* 401 B.R. 415 (B.A.P. 9th Cir. 2009).

Professionals

$1,000 per motion sanction against law firm filing bad faith motions for stay relief. Finding that the law firm repeatedly filed, and then withdrew, stay relief motions with improper purpose and in bad faith, sanctions of $1,000 per motion, for a total of $21,000 were imposed. Over a five month period, the firm filed 41 stay relief motions for mortgage creditors, but withdrew the motions before scheduled hearings; a show cause order was entered as to 21 motions, asking the firm to demonstrate that it intended to pursue those to hearing, and the court found a pattern of abusive filings with no intent to proceed to hearing.

BUSINESS BANKRUPTCY CASE LAW UPDATE

ABI SOUTHEAST BANKRPUTCY WORKSHOP

JULY 30—AUGUST 1, 2009

HILTON HEAD ISLAND, SC

Jeffrey W. Morris
Samuel A. McCray Chair and Professor of Law
University of Dayton School of Law
Dayton, OH 45469
(937) 229-3315
morris@udayton.edu

And

Of Counsel
Porter, Wright, Morris & Arthur
One South Main Street
Suite 1600
Dayton, OH 45402-2028
(937) 449-6708
jmorris@porterwright.com

TABLE OF CONTENTS

The troubles in the economy translate into an increase in bankruptcy filings and bankruptcy litigation. This on the heels of the enactment of the 2005 amendments to the Bankruptcy Code means that bankruptcy lawyers and the courts have been extremely busy in the past year. If anything, the pace of filings and litigation is going to increase, so these materials are intended to provide you with an overview of what has been going on at the higher appellate levels in the last year or so. Of course, as soon as a list is compiled, more decisions are rendered. The Supreme Court has recently accepted two more bankruptcy cases, and in the next term it will decide the constitutionality of the restrictions on attorney/client communications under § 528 of the Code, Milavetz, Gallop & Milavetz. P.A. v. U.S., 541 F.3d 785 (8th Cir. 2003), *cert. granted*, 129 S.Ct. 2966 (mem) (2009), as well as the effect of an ambiguous exemption claim In re Reilly, 534 F.3d 173 (3d Cir. 2008), *cert. granted*, 129 S.Ct. 2049 (mem) (2009).

The following materials are set out topically. They also attempt to follow the chronological course of bankruptcy cases.

I. INVOLUNTARY CASES

In re Trusted Net Media Holdings, LLC, 550 F.3d 1035 (11th Cir. 2008). A judgment creditor brought an involuntary bankruptcy case against a debtor. The debtor did not file a response, and the court, pursuant to §303(h) entered an order for relief against the debtor. Two years later, a creditor challenged the court's jurisdiction asserting that the debtor had more than 11 creditors, and that the claim of the petitioning creditor was the subject of a bona fide dispute. The Bankruptcy Court denied the motion to dismiss, and the case proceeded. The trustee took action to liquidate the estate, and still two years later the debtor and other creditors moved to dismiss the case, again on jurisdictional grounds. The bankruptcy court and district court each denied that motion to dismiss, but the Eleventh Circuit originally reversed. On a rehearing en banc, the Eleventh Circuit affirmed the lower courts. It concluded that the provisions of § 303 establishing minimum standards for the entry of an order for relief, did not constitute jurisdictional requirements for the bankruptcy court to act in the case. Rather, they are standards for the entry of the order for relief rather than prerequisites to the existence of jurisdiction. The court recognized and rejected a conflicting precedent of the Second Circuit, and also held that its decision would overrule its earlier decision in *In re All Media Properties, Inc.*, 646 F.2d 193 (5th Cir. 1981), to the extent that it may have held that § 303's provisions were jurisdictional.

II. USE OF STATE LAW AND PROPERTY OF THE ESTATE

In re Eldercare Properties, Ltd., 2009 WL 1312472 (5th Cir., May 13, 2009). In this case, the court notes that state law has an important role to play in determining whether a debtor can assume a nonresidential real estate lease. The decision, authored by Justice O'Connor, sitting by designation, found that Texas law permitted the equitable tolling of the deadline for the renewal of the lease. The parties were engaged in negotiations to modify and extend the term of the lease, and the lessor had not taken any action to reinstate the renewal deadline. Consequently, the failure to renew the lease by the deadline set out in the agreement did not prevent the debtor from assuming the lease during the Chapter 11 case. The court also concluded that Texas law

excused the failure to give notice to extend the lease because to do otherwise would have resulted in an unconscionable hardship to the tenant with very little loss to the landlord. Moreover, the delay was minimal, and the delay took place in the context of the parties' continuing negotiations and mediation to resolve disputes. In short, the important lesson of the case is to recall the role that state law can play in determining the status of the parties' relationship.

III. VALUATION OF COLLATERAL

United Airlines v. Regional Airports Improvement Corp., 564 F.3d 873 (7th Cir. 2009). The issue in this case was the proper manner for valuing the terminal leases United Airlines held at the Los Angeles International Airport. The leases provided that United would pay $17 per square foot for its terminal space, and the Bankruptcy Court used that figure to determine the value of those leases which secured obligations to its lender. The Seventh Circuit reversed the lower courts and rejected the idea that the actual rental payments could provide the necessary evidence to establish the value of the leasehold interest. The court noted that the $17 per square foot rate was the rental amount paid by United Airlines to the airport for unimproved space. The terminal area had been improved, so the court considered the $17 per square foot figure inadequate. There was no evidence in the record as to sublease rates for terminal space at the airport, but the court did note that terminal leases at another Los Angeles airport were $63 a foot. While that number was not directly used to establish the value of the leases at issue in the case, the court noted that even if the leases were set at only $30 a foot, they would render the loan fully secured. On another matter, the court considered whether the bankruptcy court had properly determined the appropriate discount rate for setting a present value on the long term lease payments. The lender had asserted an 8% discount rate, while the debtor's expert proposed a 12% rate of return as appropriate. The bankruptcy court adopted a 10% discount rate, and the Seventh Circuit found that this "splitting the difference" method is not appropriate. Instead, the court stated that the bankruptcy court must choose the correct discount rate rather than simply add the two recommended rates and divide by 2.

IV. CLAIMS

A. PRIORITY

In re Lorber Industries of California, 564 F.3d 1098 (9th Cir. 2009). At issue in this case was the proper treatment of a claim for reimbursement of workers compensation obligations that were assumed by the California self-insurers' security fund. The fund serves as a backup or insurance against the failure of a self-insured workers compensation plan. The question in the case was whether the payments required to be made by the fund constituted an excise tax that is entitled to priority under § 507(a)(8)(E)(ii). In an earlier case, the Ninth Circuit had held that an excise tax is "(a) an involuntary pecuniary burden, regardless of name, laid upon individual or property, (b) imposed by or under the authority of the legislature, (c) for public purposes, including the purposes of defraying expenses of government or undertakings authorized by it, and (d) under the police or taxing power of the state." The Ninth Circuit had issued this test in 1982, and

eleven years later the Sixth Circuit refined the test by adding two additional factors. The Sixth Circuit held that the pecuniary obligation must be universally applicable to similar situated entities, and the priority treatment being given to a governmental creditor cannot disadvantage similarly situated private creditors. The court adopted the Sixth Circuit's position and held that the reimbursement obligation in *Lorber* was not an excise tax. It noted that other creditors had similar reimbursement claims, so the government should not have a priority for a similarly situated claim.

In re Imperial Credit Industries, Inc., 527 F.3d 959 (9th Cir. 2008). A holding company of a federally insured bank filed a Chapter 11 petition. Section 365(*o*) is deemed to have assumed any commitment to a federal deposit institution's regulatory agency. This little used provision of the Bankruptcy Code was enacted in 1990 by Congress as a part of its response to the savings and loan crisis. Notwithstanding the existence of this provision, however, the debtor did not meet its depository obligations and instead converted the case to Chapter 7. Section 365(*o*) also provides that any claim for a "subsequent" breach of the obligations to cure deficits under any commitment to the federal regulatory agency is entitled to priority under § 507 of the Bankruptcy Code. The FDIC asserted its claim under § 507(a)(2) as an administrative expense of the Chapter 11 case. The district court had granted that status, but on appeal the Ninth Circuit reversed. It stated instead that there is a specific priority for these claims set out in § 507(a)(9) and this specific priority would be more apt than the more generalized administrative expense priority. Moreover, the Court noted that the debtor's failure to pay its obligation to the FDIC did not constitute an actual, necessary cost and expense of preserving the estate. Thus, it is not in the nature of an administrative expense claim, and priority exists only under § 507(a)(9).

McMillan v. LTV Steel, Inc., 555 F.3d 218 (6th Cir. 2009). An individual steelworker sued LTV asserting that his claims were entitled to administrative expense status. He asserted claims for payments under a defined contribution plan as well as under a defined benefit plan. He also asserted a cause of action for a WARN Act violation. The Sixth Circuit rejected all of the claims. It noted, for example, that the creditor asserted a claim that arose prior to the commencement of the case. Such claims cannot receive administrative expense status. He also asserted, among other things, that a settlement entered into by the United Steelworkers Association could not be effective as to him. In part, he asserted that he had not received sufficient notice of a stipulation during the case which resulted in a limitation on his ability to pursue his claims. The Court concluded, however, that notice to the union was sufficient notice to the individual. The union was acting as the individual worker's agent, and the notice to the agent was sufficient notice for the principal.

In re M&S Grading, Inc., 541 F.3d 859 (8th Cir. 2008). During the course of a Chapter 11 case and the converted Chapter 7 case, a trustee failed to make payments to employee benefit plans. The employee benefit plans brought an action seeking to remove the trustee, and to recover funds paid by the estate to a perfected secured creditor. The basis on which the plans sued was that the money used by the trustee to pay a secured creditor was not property of the estate, but was property of the plans. The plans argued that the trustee had failed to pay over funds due to the plans, and that those funds were trust funds for the benefit of the employees. The Eighth Circuit rejected the argument. The plans had cited cases in which funds withheld from employee's pay were trust funds that did not constitute property of the estate. In the case, however, the funds

being sought were not funds that were withheld from employees' paychecks. Instead, they were contributions due directly from the employer to the employee benefit plan. In that situation, the property was property of the estate and the plans simply had a claim against the estate rather than a claim to the specific funds. Interestingly, the amounts due to the plans functionally were "withheld" from employee wages. To the extent that any increase in the payments due to the plans was required, employee wages were concomitantly reduced. For example, if insurance premium costs increased, the company would have to pay those increased amounts, but would reduce employee wages to the same extent. Notwithstanding this "economic reality," the Court of Appeals concluded that the funds due to the plans were not employee wages which had been withheld. Consequently, they were property of the estate rather than property of the individual employees or the plan.

B. EQUITABLE SUBORDINATION

In re Kreisler, 546 F.3d 863 (7th Cir. 2008). In an unusual "claims trading" case, two Chapter 7 debtors formed a corporation to purchase a secured claim against their bankruptcy estates' assets. The bankruptcy court was, to the say the least, skeptical of this action and equitably subordinated the claim now held by the debtors' corporation. The district court affirmed, but the Seventh Circuit reversed. The debtors' corporation that was formed to purchase the claim was set up in such a way that they were not directly identified with the entity. It was only after the transaction took place that the bankruptcy court became aware of their interest in the corporation. Moreover, one of the two debtors was an attorney who stood to recover an additional windfall if the claim was collected. The Court of Appeals did not address whether the debtor's actions constituted an equitable conduct. Instead, the court reversed because it concluded that the actions of the debtors affected only the creditor whose claim they purchased. Since it did not harm any other creditors, equitable subordination to those other claimants was improper. Notwithstanding this "underhanded" activity, the claim was not subordinated. The court did note, however, that if the trustee could have shown that she would have been able to reach a more favorable deal with the original creditor than with the debtors' entity that purchased the claim that some subordination might have been appropriate. There was no real evidence to support this in the record, so the court did not accept that argument.

In re SI Restructuring, Inc., 532 F.3d 355 (5th Cir. 2008). Struggling entities often seek loans from insiders. Loans by insiders made on the verge of bankruptcy frequently generate efforts to equitably subordinate the position of those insiders. Such was the case in this matter. The creditors were officers, directors and the largest shareholders of Schlotzsky's. They made a total of $3.5 million in loans to the company which were secured by the company's royalty streams from franchisees, intellectual property, and other intangible property. In November of 2003, the insiders made additional substantial loans to the company on an expedited basis. Within six months or so, the insiders were removed as officers of the corporation and the company filed for Chapter 11 relief in August 2004. The unsecured creditors committee challenged the secured claims of these insiders. The bankruptcy Court concluded that the insiders had breached their fiduciary duties by taking advantage of the company's precarious financial position. After the district court affirmed the bankruptcy court, the insider creditors appealed to the Fifth Circuit. The Court of Appeals reversed in reliance on its earlier decision in *In re Mobile Steel.*

Specifically, the Court of Appeals noted that there was no finding by the bankruptcy court below nor was there any support in the record that either the debtor or unsecured creditors were harmed by the transaction in which the insiders obtained a security interest in the assets of the debtor. Importantly, the loan proceeds were used to pay unsecured creditors who were therefore not harmed when the creditor obtained a security interest in the debtor's assets. The Court also rejected any assertion that the creditor's claims should be subordinated on the theory of deepening insolvency. Most importantly, the case reiterates that equitable subordination requires a showing of harm to the claims that would be preferred if subordination were ordered.

In re WinstarCommunicaitons, Inc., 554 F.3d 382 (3rd Cir. 2009). *See* Part V infra.

V. PREFERENCES

In re WinstarCommunicaitons, Inc., 554 F.3d 382 (3rd Cir. 2009). Lucent received a payment in excess of $188 million within the year prior to the filing of Winstar's bankruptcy. The trustee challenged that payment as a preference made to an insider within a year of the filing of the case. A number of issues were presented in the case (generating a lengthy opinion) with the most significant issue being the definition of "insider" for preference purposes. Section 101(31) sets out the statutory definition of insider which includes any "person in control of the debtor." Bankruptcy Code §101(31)(B)(v). As the Third Circuit noted, however, the definition itself provides that the term "includes" a series of statutory insiders. The word "includes", however, is not limiting. Bankruptcy Code §102(3). Therefore, "non-statutory" insiders are likewise possible. The court concluded that actual control of the debtor is necessary for an entity to be an insider under the statutory definition of insider. The court concluded, however, that this extent of control is not necessary to be a "non-statutory" insider. The creditor argued that any "non-statutory" insider must exercise control similar to the kinds of control that other statutory insiders would hold. As the court noted, however, statutory insiders included entities such as a partnership in which the debtor is a general partner and a relative of a director of a corporation. These entities typically do not exercise "control" over the debtor, nevertheless they are statutory insiders under §101(31). Thus, the court concluded that a non-statutory insider need not exercise control to fall within the category. Instead, the court concluded that a "non-statutory insider depends primarily on the closeness of the parties' relationship and the transaction between the parties being one that was not negotiated at arms-length. In that circumstance, the creditor could be a non-statutory insider and the preference period would extend back one year rather than 90 days. The opinion contains an extensive discussion of the exercise of control by the creditor over the debtor. The sheer size of the alleged preference makes the case unusual. When nearly $200 million is involved, you can expect a "21-day bench trial, 1400 exhibits, and 39 witnesses." The court distinguished the actions of this creditor from the actions of other creditors who simply drive a hard bargain. Beyond compelling the repayment of its obligations, the creditor in this case "had the ability to coerce [the debtor] to make unnecessary purchases" and employed its superior position to inflate its own revenues rather than simply to collect a debt.

The court next addressed whether the creditor's claim should be equitably subordinated. The bankruptcy court had subordinated the claim to those of all other unsecured creditors and some equity holders. The equity holders were entities that purchased equity interests in the debtor who would not have so acted if the creditor had not strategically delayed announcement of defaults by

the debtor. The Court of Appeals affirmed the bankruptcy court's decision to subordinate the creditor's claim to the claims of other unsecured creditors, but it reversed the court's subordination of the creditor's claim to the interests of equity holders. Rather, the court noted that §510(c) allows subordination only to other claims.

In re Globe Manufacturing Corp., 567 F.3d 1291 (11th Cir. 2009). This is a case that implicates the pre-2005 version of § 547(c)(2) regarding the ordinary course of business exception to preference recoveries. In short, the court noted the pre-amendment law and held that the exception did not apply if the creditor could not prove that the payment was according to ordinary business terms. The creditor had offered testimony from an engineer familiar with the project, but the engineer was not familiar with industry standards in the payment of past due obligations. The creditor had also argued that it did not receive a preference because it could have obtained a mechanic's lien on the debtor's property and would have done so if the debtor had not paid the outstanding amounts. The payments came approximately one month late (there were two payments during the preference period), and the court concluded that the absence of a filed lien on the property meant that the creditor could not assert that it would have received payment in full. The court also noted that the property was also subject to liens in excess of the value of the property, so any additional mechanic's lien would have been valueless. The court also considered whether prejudgment interest should attach to the trustee's preference claim. The court concluded that this was a matter for the discretion of the court and upheld the lower court's decision that no prejudgment interest should apply. It specifically rejected the Seventh Circuit rule as set out in *In re Milwaukee Cheese Wisconsin*, 112 F.3d 845 (7th Cir. 1997).

Velde v. Kirsch, 543 F.3d 469 (8th Cir. 2008). Kirsch sold and delivered soybeans to Miller, the operator of a grain storage elevator. Miller issued a $45,000 check to Kirsch for previously delivered soybeans, but the check was dishonored. Miller then replaced the dishonored check with a "bank check" during the preference period. This transfer was clearly a preference, but Kirsch defended on the grounds that the transfer was a substantially contemporaneous exchange protected by § 547(c)(1). The exchange for which the bank check was given was the release of a security interest in the soybeans held by Kirsch's lender. That lender released its security interest only when the bank check was actually paid. Consequently, the Eighth Circuit concluded that this distinguished the case from other contemporaneous exchange cases upon which the trustee had relied, and it affirmed the district court's decision that the transfer was protected by § 547(c)(1). The case may be somewhat limited in its application. Since the goods involved were farm products, the transfer of the soybeans to the grain elevator operator did not result in a release of the security interest automatically. Such a result would occur if the goods were inventory and UCC § 9-320 applied to the case.

VI. FRAUDULENT TRANSFERS

Freeland v. Enodis Corp., 540 F.3d 721 (7th Cir. 2008). When a trustee recovers a judgment in excess of $30 million, two things are likely to occur. The first is the filing of a notice of appeal. The second is the issuance of a lengthy opinion. This case follows the norm. The trustee recovered as fraudulent transfers a number of payments by a subsidiary to its parent. The first

issue considered by the court was whether the debtor was insolvent at the time of the transfers. In particular, the debtor had issued notes to its parent with a face amount of $30 million. The notes provided among other things that they represented a payment of a dividend that had been declared by the board of directors, and further provided that the notes were payable "only out of funds legally available for the payment of a dividend." It further provided that failure to pay the note when due would generate additional obligations for the cost and expenses of collection. Over an 8 or 9 year period, the parent received almost $24 million in interest payments. The recipient of the transfer argued that the debtor was not insolvent at the time of these transfers because the notes should have been valued at zero or some small amount. The argument was that since the notes could only be paid out of funds appropriate for the distribution of dividends to shareholders, that unless the debtor was solvent in the face amount of the notes, payment would be inappropriate and the notes should be valued at zero. The court rejected this argument and concluded that the notes were unconditional, noncontingent obligations of the debtor. Not only did the language of the note support this conclusion, but the court also indicated that the parties themselves treated the notes as not contingent. The lengthy and regular payment of substantial interest amounts led the court to conclude that the notes were fully enforceable and were so viewed by the parties. The parent eventually cancelled the notes, but the lower courts had concluded that this still did not make the debtor solvent. The debtor was facing a huge number of claims from consumers who had purchased allegedly defective furnaces from the debtor. The bankruptcy court did not make a sufficiently clear finding of fact, however, and the Court of Appeals remanded the case for further findings on that issue. On other issues, however, the court concluded that the bankruptcy court had properly reached its decision as to the parent company's actual fraud as evidenced by a variety of transactions that served as badges of that fraud. As to another transaction, however, the Court of Appeals reversed the grant of summary judgment by the court below and directed that the trial be held on preference and fraudulent transfer issues relating to the separate transaction. Interestingly, the court noted that a number of arguments were raised in the Court of Appeals that had not been raised in the lower courts. Consequently, the Court of Appeals refused to consider those arguments. The interesting aspect of this is that the hearing in the lower court was a 22-day trial with 19 witnesses and 457 exhibits. Hard to believe that so many arguments would not have been raised in the lower court given the extent of that trial.

VII. POSTPETITION TRANSFERS

In re Straightline Investments, Inc., 525 F.3d 870 (9th Cir. 2008). The debtor filed a Chapter 11 petition and shortly thereafter sought permission to borrow funds secured by an interest in its property. The court approved a lesser amount than requested, and also limited the security interest to a security interest in the debtor's equipment and a junior lien on the debtor's inventory. The court specifically rejected a request for the approval of a loan secured by the debtor's accounts receivable. Notwithstanding these orders, the debtor and the post-petition creditor continued to engage in borrowing transactions. The creditor paid the debtor approximately $186,000 to factor or purchase approximately $200,000 in accounts. The creditor eventually collected approximately $160,000 on those accounts. In the meantime, the case was converted to Chapter 7 and the trustee brought an action under § 549 to recover the value of the property improperly transferred post-petition. The creditor made two primary arguments in

response to the trustee's actions. First, it asserted that since the debtor had no control over the money that might be collected from the accounts, that no property of the estate was transferred. The court noted the obvious flaw in this argument being that the property of the estate is the receivable itself, not the proceeds of the receivable. The creditor also asserted, however, that the transfer should not be recoverable because no depletion of the estate had occurred. Instead, the creditor had given the debtor approximately $186,000 and only recovered $163,000 from it. The creditor argued that the estate was, in fact, better off by having had the benefit of the funds it had contributed to the debtor. The court concluded, however, that the lack of any depletion of the estate is not a defense to a claim under § 549. The creditor also asserted that the transfer of the accounts should be approved as an ordinary course of business transaction under § 363. Of course, the fact that the bankruptcy court had already disallowed such loans made such an argument unattractive, at best. Most importantly, the Court of Appeals affirmed the lower courts' awarding of damages in the full amount of the transferred property, the $163,000 that the creditor collected from the accounts. The court rejected the argument that the creditor had paid more than that for those accounts and should be protected. The court again noted specifically that the creditor was fully aware that the bankruptcy court had already rejected a proposed loan from the creditor to the debtor secured by the receivables. In light of that fact, the creditor was on very shaky grounds in asserting any equitable right to recovery.

VIII. DISCHARGE AND DISCHARGEABILITY

In re Jennings, 533 F.1333 (11th Cir. 2008). Shortly after the first extension of credit in history, a debtor in default used his assets to improve his cave rather than to pay his creditors. Such behavior continues today. In this case, the debtor was a defendant in a tort action. During the course of the litigation, he purchased a home and adjacent airplane hanger in Florida. He also made substantial renovations to the home (to make it more "livable"), and during the damages phase of the tort litigation, initiated substantial construction on the hanger. In fact, the debtor prepaid the contractor on the hanger renovation $130,000. The contractor had only requested $50,000, but the debtor testified that he "wanted to save money and move the project forward" so he prepaid the larger amount. The deposition testimony of the contractor, however, contradicted the debtor's testimony. The court concluded that this sufficiently demonstrated the debtor's actual intent to hinder, delay or defraud the creditor and affirmed the denial of the debtor's discharge.

In re Arch Wireless, Inc., 534 F.3d 76 (1st Cir. 2008). In this case, Arch Wireless and Nationwide Paging were involved in a dispute over the quality of paging devices that Arch had supplied to Nationwide. Subsequent to this ongoing dispute, Arch filed a Chapter 11 petition, but it did not include Nationwide on any list of creditors. Nationwide received no notice of the Chapter 11 case, and after confirmation of the plan, Nationwide pursued its action in the state courts in Massachusetts. Arch defended and removed the case seeking contempt in the Bankruptcy Court for violation of the Chapter 11 discharge. The First Circuit affirmed the lower court's which found that Nationwide's claim was a known claim that should have been listed among the claims against Arch Wireless. Since it was a "known" creditor, it had a right to the specific notice of the case and related matters. Publication notice to a known creditor was viewed as insufficient notice under the due process clause. Even though the President of

Nationwide was "generally aware of the bankruptcy filing in December, 2001," there was no actual knowledge of the claims bar date, the confirmation hearing, or the contents of the confirmed plan. The First Circuit rejected the notion that general awareness of a pending Chapter 11 is sufficient to constitute notice for due process purposes. The court also noted that since this was a Chapter 11 case, it would be treated differently than situations under Chapters 7 or 13. In Chapters 7 and 13, the rules set out the deadlines for the filing of a proof of claim. In Chapter 11 on the other hand, the bar date is set by separate order. Therefore, general knowledge of a bankruptcy under Chapters 7 and 13 is more directly effective than a general knowledge of a pending Chapter 11. The court did recognize that if a creditor has actual knowledge of the relevant deadlines such as the claims bar date or confirmation hearing, then the creditor may not be able to challenge those actions at a later time. The court also noted that there was no exception to discharge for a corporate debtor for the failure to list a claim for creditors who have no actual knowledge of the case as is provided for individual debtor cases under § 523(a)(3). Thus, the case is most accurately viewed as a corporate Chapter 11 case rather than just a Chapter 11 case.

In re Patel, 565 F.3d 963 (6th Cir. 2009). In this case, the debtor was a corporate officer of a construction company. The construction company failed to turn over funds that it had received and which were due to subcontractors on the project. Under a Michigan statute, the "contractor" is a fiduciary and holds funds in trust for the benefit of the subcontractors. When this fund was not used to pay the subcontractor, it constituted a defalcation and brings §523(a)(4) into play. The twist in this case is that the "contractor" is not just the corporate entity that held the funds, but also included the individual debtor who was the president and chief operating officer of the company. The Court of Appeals concluded that the state statute applicable in the matter would apply as well to the individual corporate officer, as well as to the corporation itself. Therefore, the debt of the individual was nondischargeable under § 523(a)(4).

Colonial Surety Co. v. Weizman, 2009 564 F.3d 526 (1st Cir. 2009). The debtor was an indemnitor who promised to reimburse a surety if the surety had to complete certain construction contracts. The contractor defaulted, the surety completed the job, and the surety brought an action against the individual indemnitor for reimbursement of its costs. The surety obtained judgment against the indemnitor, but the indemnitor later defended after having the original case reopened by asserting that he had in the meantime obtained a bankruptcy discharge. The problem was, however, that the debtor did not include the surety among his creditors either on the creditor matrix or in the schedule of liabilities. There was no indication that the surety was aware of the debtor's bankruptcy, and the district court hearing the reopened action concluded that the debts were not discharged in the bankruptcy. The court relied on § 523(a)(3). That section provides that debts that are not listed or scheduled are not dischargeable unless the creditor had notice or actual knowledge of the case in time for the filing of a proof of claim. The debtor argued that since his case was a no asset case, that the creditor was not deprived of an opportunity to file a timely proof of claim since notice had been sent indicating that no claims need be filed unless the court further notified the creditors that assets had been identified. The First Circuit affirmed the district court in holding that the failure to list the claim on the debtor's schedules operated to make the debtor nondischargeable even in a no asset case. The court specifically rejected a contrary Ninth Circuit decision, *In re Beezley,* 994 F.2d 1433 (9th Cir. 1993), and held that the debtor has the burden of correcting the record if he/she wants to obtain a

discharge of previously unscheduled debts. Specifically, the court noted that the debtor should move to reopen the case and add the creditor to the list of creditors in the bankruptcy proceeding. This would put the burden on the debtor to "correct" the record, and it would provide the court with an opportunity to evaluate the debtor's reasons for omitting the listed creditor. The court was persuaded by *In re Stark*, 717 F.2d 322 (7th Cir. 1983), which had held that a debtor who innocently omitted a creditor from a list of creditors still has the burden to show that relief and a discharge should be granted. The First Circuit found this argument persuasive, and there is a continuing split in the circuits on this issue. One wonders whether the court would have reached the same conclusion if the debtor were a consumer who had neglected to include a $700 medical bill from the schedule of liabilities as compared to this business debtor who omitted an $813,000 obligation. In the case, the court also considered briefly whether the surety had any claim whatsoever. The surety had argued that it had no claim because no default had occurred on the underlying contracts until after the debtor had obtained a discharge in his Chapter 7 case. The court noted that the definition of claim is extremely broad, and includes contingent claims. Therefore, the court rested its decision on the debtor's failure to include the creditor on the schedule of liabilities thereby rendering the debt nondischargeable under § 523(a)(3).

IX. PONZI SCHEMES

In re Bayou Group, LLC, 564 F.3d 451 (2nd Cir. 2009). The Bayou Group was a large scale Ponzi scheme. When the scheme came to light, creditors brought an action in the federal district court to have a "federal equity receiver" appointed to pursue litigation. The district court appointed an individual to take that position. Among the actions taken by that receiver was the filing of a Chapter 11 petition followed by the commencement of over 125 adversary proceedings. Approximately three weeks into the Chapter 11 case, the US Trustee moved for the appointment of a Chapter 11 trustee to replace the receiver. Upon denial of that motion, appeals were taken all the way to the Second Circuit. The Court of Appeals held that the bankruptcy court probably concluded that no trustee should be appointed. To the extent that there was mismanagement by the debtor, that mismanagement had taken place prepetition and was not under the direction or control of the current operating officer. Moreover, the court noted that the district court's appointment of the receiver also included language in its order that specifically authorized the individual to be the sole and exclusive managing member of the limited liability company. Through that order, he was vested with complete authority to manage and file the bankruptcy case.

In re Slatkin, 525 F.3d 805 (9th Cir. 2008). The Ninth Circuit in this case held that a debtor's admission in a guilty plea that he operated a Ponzi scheme with the actual intent to defraud creditors conclusively establishes that fraudulent intent under Bankruptcy Code § 548(a)(1)(A) and the comparable state law. The plea agreement even precludes the re-litigation of that issue by a person who is being sued by the trustee to recover payments made to that person as a part of the Ponzi scheme. The court affirmed a judgment against the defendant for the amount of the "profit" that they made through payments received from the operating of the Ponzi scheme. The court also affirmed the lower courts' granting of prejudgment interest on the claim.

In re AFI Holding, Inc., 525 F.3d 700 (9th Cir. 2008). Gary Isenberg convinced people to give him money by promising them that he would return even greater amounts to them. He was able to do this for a short time. He is now serving a 63-month sentence in a federal penitentiary. In addition to his familiarity with the federal criminal process, he also became familiar with the federal bankruptcy process. His company, AFI, filed a Chapter 11 petition in October of 2001, and in October of 2003 the trustee commenced approximately 170 adversary proceedings against investors in AFI. The trustee sought the recovery of any amounts received by the investors in excess of the amount they paid into the company. The Ninth Circuit reviewing the matter concluded that the lower courts were correct in permitting the trustee to recover the excess over the amount paid in by the investor. The court also recognized, however, that the investor could protect the amount it paid in to the extent it had in good faith contributed reasonably equivalent value for the transfer. The case was remanded for the lower court to determine if the particular investor acted in good faith, but if the court were to so find, then the only recovery would be for the excess returned. The Ninth Circuit stated that the reasonably equivalent value would be the surrender of a claim against the debtor for fraud or similar recovery when they were repaid the amount of their contributions. The court also remanded the case for determination as to whether any prejudgment interest should be awarded in the matter.

X. PROFESSIONALS

A. FEES

In re Babcock & Wilcox Company, 526 F.3d 824 (5th Cir. 2008). Counsel for the Asbestos claimant's committee in this Chapter 11 case filed a fee application seeking about $6.5 million in fees and expenses. The United States trustee objected to full hourly rates for travel time of attorneys who were not working on the case during that travel. The representative of the law firm testified that the firm bills for travel time just as it does for any other time, and that he was aware that other law firms bill travel time at full rates. The firm argued that if travel rates were not billed at the full rate, firms would effectively discriminate between clients who require travel time and those who do not. The court awarded the travel fees at only 50% of the hourly rate if the attorney was not working on the matter during the travel. The district court affirmed as did the Court of Appeals. The court recognized that courts are split on the rate that can be charged for an attorneys' travel time. It concluded, however, that the rule should be the same in the circuit for bankruptcy cases as for civil rights cases and concluded that travel time should be billed at only a 50% rate. The court also noted that the law firm did not specify that it will bill its full hourly rate for "non-productive" travel time. Thus, the court found no abuse of discretion in the bankruptcy court disallowing the fees in excess of one-half of that requested with regard to travel time.

In re Smart World Technologies, LLC, 552 F.3d 228 (2nd Cir. 2009). Special counsel was employed to represent the debtor-in-possession in a particular matter. The employment of special counsel was approved with the fee to be paid not on the basis of any hourly rate, but as a contingent fee depending upon the underlying success in the litigation. The terms of the contingency were somewhat elaborate with the percentage of recovery varying depending on the length of time that the matter was pending as well as the amount of the recovery. Upon settlement of the matter, the law firm sought in excess of $2 million in fees. The bankruptcy

court, however, concluded that the amount of the fee should be reduced by over $1 million. Not surprisingly, this generated an appeal by a law firm. The district court reversed the bankruptcy court's decision, and the Second Circuit thereafter affirmed. The Court of Appeals first determined that the approval of the law firm's employment was granted under § 328(a) of the Code. This section authorizes the employment of a professional "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis." While the terms of the employment were not as explicit as one would prefer (it is always good practice to include a specific reference to § 328(a) when being employed as special counsel under special fee arrangements), the Court of Appeals concluded that the employment was undertaken under that section. Section 328(a) further provides that the Court can allow the compensation to be paid in a manner different from the amount originally agreed upon, "if such terms and conditions prove to have been improvident in light of developments not capable of being anticipated at the time of the fixing of such terms and conditions." The Court of Appeals concluded that this part of § 328(a) protected the law firm's claim for the full contingent fee amount. The circumstances that arose after the approval of the employment, objections to settlement and other actions that delayed the conclusion of the matter, were not incapable of being anticipated. The Court emphasized that this Code section focuses on an inability to predict these specific circumstances rather than a failure to predict those circumstances. As a result, the Court approved the law firm's fees in the approximate amount of its original agreement.

B. LIABILITIES

Gray v. Evercore Restructuring, LLC, 544 F.3d 320 (1st Cir. 2008). Confirmation of a Chapter 11 plan does not necessarily mean success. In this case, shortly after the debtor's plan was confirmed, the reorganized debtor was subsequently liquidated. When a Chapter 11 case fails in this manner, fingers frequently point to the financial and legal advisors to the original Chapter 11 debtor. Such was the case in this matter. The primary basis for the claims against the financial and legal advisors to the original Chapter 11 debtor was that the financial data on which the original Chapter 11 plan was based was stale at the time of confirmation. Moreover, the liquidating trustee in the subsequent Chapter 11 case asserted that the financial and legal advisors to the original debtor in possession knew that the information was stale. The liquidating trustee in the subsequent Chapter 11 then brought the action against the former advisors. The advisors' defense was that the debtor-in-possession was just as much to blame for the submission of the stale material and was likewise aware that it was not up to date. The First Circuit affirmed the lower court's decision that the financial and legal advisors could rely on the *in pari delicto* defense. The Court of Appeals rejected the liquidating trustee's assertions that the professionals were experts and therefore are more responsible than the debtor for submitting the stale financial information. In this regard, the Court of Appeals found that the debtor was at least as responsible for the submission as were the various professionals. The Court of Appeals also rejected a defense that the improper actions by the Chapter 11 debtor were attributable only to its management and not to the corporation itself. The Court noted, however, that there was no indication that the wrongdoing was undertaken to protect the interests of management as opposed to the interests of the corporation itself. Furthermore, the Court of Appeals rejected the argument that permitting the *in pari delicto* defense would be inconsistent with basic bankruptcy policy. The trustee argued that dismissing the case would make it more likely that professionals

would not meet their fiduciary duties in future cases. The Court of Appeals rejected this argument. The court suggested that because this was a decision upholding a dismissal of the case on the pleadings, that the trustee's argument "exaggerates the precedential value of this case." Presumably, the court here is referring to the fact that in future cases, parties will be more creative in their pleading of the matter.

XI. DISMISSAL OF CASES

In re Bartle, 560 F.3d 724 (7th Cir. 2009). The debtor, John Bartle, owed substantial taxes. At one point, Bartle and the IRS had agreed to a repayment plan, but it does not appear that Bartle ever performed under that agreement. Eventually, Bartle filed a Chapter 11 petition and the IRS collection efforts were temporarily stayed. The bankruptcy court permitted continued collection by the IRS, and in a related district court case appointed a receiver to handle Bartle's finances. The district court withdrew the reference of the Chapter 11 petition to the bankruptcy court, and placed the case with the district court that was already handling the collection of the taxes. After a partial payment of the taxes, Bartle still owed nearly $8 million to the IRS. While the debtor's schedules asserted assets in excess of approximately $7 million, those amounts may have been slightly "overstated." The debtor's income was less than $70,000 for the year prior to the commencement of the case, and just $17,000 for the first eight months of the year in which the debtor filed his Chapter 11. The court granted a government motion to dismiss the case. That is not a surprising result. The battle in the case, however, was over the manner in which the dismissal motion was granted. The motion was filed on June 11, 2007, and the district court granted the motion on June 21. The debtor did not file any written response to the motion, and no hearing was held. The debtor filed a motion under Bankruptcy Rule 9023 and Civil Rule 59 for a new trial. His primary position was that the court had not properly dismissed the case because of its failure to conduct a hearing as is anticipated by § 1112(b)(2) of the Code. The motion did not include any defense to the merits of the motion, but instead asserted only that it was improper for the court to grant the motion in the absence of a hearing. The district court denied the motion and the Court of Appeals affirmed. In particular, the Court of Appeals noted that action can be taken in the absence of a written response under the provisions of § 102(1) of the Code. The court recognized that Rule 2002(a)(4) would provide at least 20 days notice of the motion. The court concluded, however, that while the debtor was arguably deprived of adequate notice, but concluded that the error was harmless. The debtor never offered any substantive defense to the motion to dismiss throughout the entire appellate process. Thus, the court concluded that he apparently had no defense and that granting the motion to dismiss was harmless error even though inadequate notice was given.

XII. APPEALS

In re United Producers, Inc., 526 F.3d 942 (6th Cir. 2008). A group of unhappy creditors appealed the confirmation of a Chapter 11 plan. On appeal, the BAP sent the case back to the bankruptcy court for further findings on the issue of the equitable mootness of the appeal. On remand, the bankruptcy court found that the plan was substantially consummated and that a

change in the order would have an adverse effect on the interests of third parties. A second appeal followed, and the BAP affirmed. On appeal to the Sixth Circuit, the Court of Appeals held that it should review the lower court's decision *de novo* because the BAP was sitting as an appellate court. Consequently, the Court of Appeals is in as good a position to review the lower court's decision as would be the BAP. In reviewing the lower court's decision, the Sixth Circuit concluded that equitable mootness should prevent any further consideration of the appeal and dismiss the case. The bankruptcy court had made significant findings regarding the substantial consummation of the plan, and the creditors who appealed eventually conceded that the plan had been substantially consummated. They still asserted, however, that the confirmation order should be reversed because it included the retention of the management that had "mismanaged" the debtor prior to the commencement of the case. The creditors asserted that they should be permitted to propose their own plan that would include the removal of existing management. It would also "change the debtors' business model" in a variety of ways. The Court of Appeals concluded that such a proposal would potentially have an adverse impact on the interests of third parties. As the bankruptcy court had noted, the debtor's reorganization was accomplished in part based on the financing of the business which required confirmation of the original plan as a condition to the disbursement of the loan. Overturning the confirmation order would result in a default under the financing arrangements and could lead to the shutdown of the business. Thus, the court concluded that the equitable mootness doctrine prevented its consideration of the matter and dismissed the appeal.

XIII. MISCELLANEOUS

Travelers Indemnity Company v. Bailey, 129 SCt. 2195 (2009). In this case, the Supreme Court addressed, among other things, the finality of a 1986 bankruptcy court order in the Manville bankruptcy case. In that case, the bankruptcy court had enjoined actions against Manville's insurers to the extent that claims were channeled to the personal injury settlement trust in the bankruptcy case. Those claims included claims and allegations against the insurers of Manville that were based upon, arising out of or relating to the Manville insurance policies. Some years after the 1986 order, plaintiffs began Travelers in state courts on the grounds that Travelers had violated state consumer protection laws or failed to meet other common law duties. In general, the claims asserted that Travelers had failed to warn the public about the dangers of asbestos as required by the common law, and had otherwise violated state consumer protection statutes. Travelers defended by asserting that these claims were enjoined by the bankruptcy court's order in 1986. The Second Circuit held for the plaintiffs, but the Supreme Court reversed. It concluded that these actions were covered by the 1986 injunction issued by the bankruptcy court. The Supreme Court further held that the plaintiffs were barred from collaterally attacking the 1986 injunction by res adjudicata principles. Their failure to challenge the injunction directly by appeal in 1986 precluded their much later action. The court was careful to point out, however, that its decision did "not resolve whether a bankruptcy court, in 1986 or today, could properly enjoin claims against non-debtor insurers that are not derivative of the debtor's wrongdoing."

In re Chira, 567 F.3d 1307 (11th Cir. 2009). Husband and wife were engaged in a protracted divorce proceeding which included efforts to sell a hotel co-owned by the parties. A receiver was appointed in the divorce proceeding to continue to operate the hotel given that operation of

the property by H & W proved impossible. Eventually, the receiver entered into an agreement with a buyer for the property. The buyer was to obtain both the husband's and the wife's interest in the property. Prior to the conclusion of that transaction, however, an involuntary Chapter 7 petition was filed against the husband. The Chapter 7 trustee moved to settle all disputes relating to the transaction and to provide for the transfer of the hotel to the buyer. The estate was to receive $2 million in cash, which was greater than the amount necessary to pay all creditors in the case. The wife sought recovery of some portion of the $2 million and to object to the proposed settlement. The lower court did not expressly evaluate the settlement under the test set out by the Eleventh Circuit in *In re Justice Oaks, II, Ltd.*, 898 F.2d 1544 (11th Cir. 1990). On appeal in the Eleventh Circuit, the Court of Appeals concluded that although the bankruptcy court did not expressly evaluate the proposal under the "Justice Oaks II" test, the bankruptcy court still conducted a sufficient evaluation of the transaction that it met the standards set out in Justice Oaks. Moreover, the court noted that the wife did not have any rights under § 363 because the transaction was an assumption of a pre-bankruptcy contract rather than a sale of debtor's interest in the property under § 363. The proposed settlement that the court approved included a variety of matters related to the underlying sale agreement, but the court held that the extent of the "modifications" to that agreement did not constitute such a modification that it permitted the nondebtor-wife to object to the transaction. The determination of the extent the modification was allowed was made under applicable nonbankruptcy law and not as a matter of federal bankruptcy law.

Ferguson v. Commissioner of Internal Revenue, 568 F.3d 498 (5th Cir. 2009). This is an appeal from the United States Tax Court, but it includes a discussion of Tax Court jurisdiction over the dischargeability of certain tax obligations. The debtors challenged an assessment by the IRS regarding its 2000 taxes. The debtors asserted that their tax liability was discharged in bankruptcy, but the Tax Court held that it was without jurisdiction to resolve that issue. After addressing a variety of tax specific issues, the court turned to the question of whether the Tax Court had jurisdiction in a redetermination proceeding to determine whether a prior tax liability was discharged in bankruptcy.

In re United Operating, LLC, 540 F.3d 351 (5th Cir. 2008). Dynasty Oil & Gas filed a Chapter 11 case and had a confirmed plan. Under the terms of the plan, all of its assets were transferred to United, with the exception of some specifically reserved matters. Thereafter, Dynasty brought an action against entities that had operated Dynasty's business during the Chapter 11 case. It alleged that they had wasted assets and otherwise improperly operated the business. The Bankruptcy and District Courts rejected the claim on res adjudicata grounds because a nearly identical action brought by the creditors committee in the Chapter 11 case had already been dismissed. On appeal, the Fifth Circuit affirmed, but on very different grounds. The court stated that it need not address the res adjudicata issue because the debtor had no standing to bring the case. The court noted that the cause of action being asserted had not been preserved in the Chapter 11 plan, and all of the other assets of the company had been purchased by another entity. Thus, the court concluded that the reorganized debtor had no standing to pursue this action.

In re Western Iowa Limestone, Inc., 538 F.3d 857 (8th Cir. 2008). The debtor owned several quarries in Iowa and sold agricultural lime as a byproduct of its quarry operation. The lime was

sold through fertilizer and chemical dealers who then resold the product at retail. The normal transaction was for the retailers to purchase the lime from the debtor but to have the debtor retain possession of the lime until the retailer sold it to a third party customer. The customer would then typically hire the debtor to ship the product directly to the customer's premises. The lime was in fungible piles until it was placed in trucks for removal. Not surprisingly, a lender had a perfected security interest in all of the debtor's assets, including the inventory and receivables of the business. Upon the sale of all the debtor's assets in the bankruptcy case, the retailers asserted that they had a prior right to the proceeds of the goods over the claim of the secured creditor. The bankruptcy court concluded that the retailers had taken "constructive possession" of the goods and therefore were buyers in the ordinary course of business under the Uniform Commercial Code. The Eighth Circuit BAP reversed, but the Court of Appeals concluded that the retailers were buyers in the ordinary course of business. Consequently, they took free of the claims even of the perfected secured creditor for purposes of Iowa law. The Court of Appeals concluded that the Iowa courts would recognize "constructive possession" as a form of possession sufficient to meet the definition of buyer in the ordinary course of business.

In re Adelphia Communications Corp., 544 F.3d 420 (2nd Cir. 2008). As a part of the Adelphia Chapter 11, substantial claims were asserted against prepetition lenders and investment banks that had supported Adelphia prior to the filing of the bankruptcy case. During the case, the equity security holders' committee had been granted derivative standing to assert the claims on behalf of the debtors. After the case had been initiated, the district court withdrew the reference for the adversary proceeding between the equity security committee and the lenders. Thereafter, the debtors' Chapter 11 plan was confirmed. Among the provisions in the plan was one to transfer the authority to pursue the claims against the lenders and investment banks from the equity security holder committee to the litigation trust established as part of the plan. The equity security committee objected to that action, but the bankruptcy court concluded that it had the authority to withdraw the derivative standing from the committee and to permit the litigation to proceed under the direction of the litigation trust. On appeal, the district court dismissed the appeal, and the Second Circuit affirmed that dismissal. The Court of Appeals concluded that the Bankruptcy Court's discretion to recognize derivative standing for the committee included the ability of the court to withdraw that derivative standing. The bankruptcy court had concluded that the transfer of the causes of action to the litigation trust was in the best interests of the estate. In the absence of an abuse of that discretion, the appellate court concluded that the transfer of those claims was effective.

In re Trailersource, Inc., 555 F.3d 231 (6th Cir. 2009). A creditor asserted that the debtor and several related entities had engaged in a series of fraudulent transfers. The Chapter 7 trustee determined that the estate did not have sufficient assets to conduct a full scale investigation and action to recover the alleged fraudulent transfers. Consequently, he refused to proceed with those actions, although later agreed to settle the approximately $20 million claim for $50,000. The creditor holding a $19 million claim requested that the court authorize it to pursue the fraudulent transfer under § 544(b) given that the trustee would not take on the case. The bankruptcy court refused the request, but the district court, on appeal, authorized the creditor to pursue the matter. On appeal to the Sixth Circuit, the Court of Appeals affirmed the District Court's decision to permit derivative standing for the creditor. The defendants had argued that derivative standing for creditors was no longer available since the Supreme Court's decision in

Hartford Underwriters Insurance Co. v. Union Planters Bank, N.A., 530 U.S. 1 (2000). In that case, the Court refused to allow a party that had provided workers compensation protection for the debtor to recover their claim from property securing an allowed secured claim. The Supreme Court held that recovery under § 506(c) was limited to the trustee as indicated in the plain language of that section. In the case, however, the Supreme Court stated that it was not addressing whether bankruptcy courts can permit other parties to act on behalf of the trustee in pursuing recoveries under § 506(c). The Sixth Circuit noted this specific carve out by the Supreme Court, and concluded that while the avoiding powers typically are stated in terms of a "trustee's authority", authorized actions by creditors are not prohibited by the Hartford Underwriters case. The case includes an extensive discussion of the issue providing both Bankruptcy Code and pre-Bankruptcy Code support for its conclusions. In particular, the Court notes that derivative standing pursuant to a court order does not present the problem of a loss of control over the process that might occur if derivative standing were authorized in the absence of court approval. The Court of Appeals also noted other code sections, including § 503(b)(3)(B), which anticipate the compensation of creditors who take action to recover property for the benefit of the estate.

In re LTV Steel Company, Inc., 560 F.3d 449 (6th Cir. 2009). During the course of the debtor's Chapter 11 case, the United States Trustee appointed an official committee of administrative claimants. The claimants were authorized by standing order of the bankruptcy court to bring an action against the debtor's officers and directors on the grounds that they had operated the business in such a manner as to reduce the likelihood that the administrative expense claimants would recover on their claims. The debtor's former chief executive officer and other officers and directors moved to have the committee dissolved and to challenge the court's original order appointing the committee. On appeal, the district court dismissed the appeal finding a lack of finality as well as a lack of standing. The officers and directors appealed to the Sixth Circuit, and the Court of Appeals concluded, among other things, that the chief executive officer was not a "person aggrieved" by the bankruptcy court's standing order that granted the administrative claimant's committee derivative standing to bring an action against him. The court concluded that a party is not aggrieved simply because the bankruptcy court authorized the committee to bring an action against that person. It also rejected the defendant's argument that further pursuit of the matter would additionally reduce the already insufficient funds to meet administrative expenses, including the administrative expense that he would assert on the basis of an indemnification provision applicable to the officers and directors. The same argument existed with respect to the motion by the other officers and directors seeking to dissolve the administrative expense claimant committee. Again, the court concluded that they were not persons aggrieved by the appointment of the committee, even though they may eventually be defendants in an action brought by the committee.

Contemporary Industries Corp. v. Frost, 564 F.3d 981 (8th Cir. 2009). Several individuals and family trusts collectively owned all of the shares of the debtor. In December 1995, the shareholders sold all of their interests to an outside investment group. The purchase was accomplished through a leveraged buyout, and as part of the transaction, over $25 million in cash was deposited in a Nebraska bank, along with the shares owned by the sellers. An escrow agreement set out the treatment to be given to the cash and stock certificates. Approximately two years later, the debtor filed a Chapter 11 petition as a result of its heavy debt load acquired

as part of the buyout. The debtor then sought to recover payments made to the former shareholders asserting that they were fraudulent transfers under the Nebraska Fraudulent Transfer Law. The defendants responded with a motion for summary judgment under § 546(e) asserting that the transfers were "settlement payments made by or to a financial institution." The bankruptcy court granted summary judgment on this basis, and the district court affirmed. The Eighth Circuit likewise affirmed the decision. It found that the plain meaning of § 546(e) governed the transaction. It rejected the arguments posed by the debtor that § 546(e) was intended to apply to the settlement of public securities transactions and should not have applied to this privately held securities agreement. The Court of Appeals joined the Third, Ninth and Tenth Circuits in noting that the definition of a settlement payment as set out in § 741(a) is extremely broad and reached this transaction. The court recognized that much of the legislative history reflects the notion that these provisions are intended to protect national financial markets against instability, but concluded that the plain language of the statute is not so limited. Therefore, the safe harbor of § 546(e) protected the transaction and these settlement payments were not recoverable by the debtor.