# Court Approval vs. Ordinary Course:
## Issues Related to Obtaining Court Approval

Concurrent Session

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**Are We Courting?**

**A Guide to Seeking Court Approval in Chapter 11 Cases**

Given the transparency required by the Bankruptcy Code and the need for court approval of most transactions outside the ordinary course of business, it would appear, at first glance, that the issue of when you need to seek court approval would be uncontroversial and somewhat straight-forward. However, in the complex and outright weird fact situations that often arise in bankruptcy cases, first glances are not always accurate. Here is an outline of certain key issues in Chapter 11 where court approval of an action or contract will likely be necessary.

## A. 11 U.S.C.A § 327 - Employment of a Professional by Debtors

1. First, are you a professional? While attorneys, accountants and financial advisors are clear cases, there are a number of other service providers which could be considered "professionals" which require court approval. As noted by the ABI guide to the Employment of non attorney professionals:

> Courts that have considered the scope of the Code's employment and compensation approval provisions have formulated various tests for determining who are "other professional persons" under 11 U.S.C. §327. The courts have generally limited application of these provisions to persons and firms in those occupations that play a central role in the administration of the bankruptcy case. Courts also have generally held that in order for persons or firms to be considered professionals, they must have some specialized education or training. Some courts also have looked to whether a specialized service performed by the person or firm benefits the estate or the committee.
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> Applying this and other tests, courts have found the following to be professionals under U.S.C. §§ 327 and 1103: (1) investment bankers; (2) bookkeepers; (3) mediators; (4) real estate agents; (5) environmental waste remediation companies; (6) consultants who negotiated the sale and financing of a corporate debtor's assets; (7) environmental consultants; (8) oil and gas consultants; (9) management consultants; (10) financial advisors; (11) crisis managers; (12) employment

agencies; (13) pension plan administrators; (14) public relations firms; (15) lobbyists; and (16) architects.

*See* "Retention and Compensation in Bankruptcy Cases - A Guide for Non-Attorney Professionals" (ABI 2d ed 2010).

2. Make sure all elements of your employment agreement are approved. See e.g., In re Stone, 401 B.R. 897 (Bkrtcy. W.D. Ky. 2009) (Fees of counsel and retainer ordered disgorged where special litigation counsel failed to disclose and get court approval of retainer paid by individual debtor's father).

**B. 11 U.S.C. §§ 330 and 331 - Payment of Fees to Professionals**

1. See e.g., In re McCrary & Dunlap Const. Co., LLC, 79 Fed Appx 770 (6th Cir. 2003) (noting that prior court approval is required for professionals to accept or solicit payments of their fees and expenses).

**C. 11 U.S.C. § 361 - Adequate Protection**

1. Is court approval required for grants of adequate protection?

See In re Bleh M Land & Cattle Company, 859 F.2d 137 (10th Cir. 1988) (holding that failure to see court approval of an adequate protection agreement did not prevent secured creditor from asserting 11 U.S.C. § 507(b) claims) overruling 71 B.R. 818 (D. Col. 1987) (which held court approval was required for 11 U.S.C. § 507(b) claims based on adequate protection).

**D. 11 U.S.C. § 362 - Automatic Stay**

1. See Lubben & Bowles, Tis Better to See Permission than Beg for Forgiveness: A Further Lehman Report, ABI L. J. 22 (February 2011) (hereinafter "Report") (discussing sanctions arising in the Lehman case related to stay violation involving a $500,000,000 seizure of funds in overdraft account by a creditor which believed an exception to the automatic stay applied) This decision in the Lehman case is on appeal.

## E. 11 U.S.C. § 363 - Sale or Use of Assets and Cash Collateral

1. See Report at 23, 76 (discussing litigation over Multibillion dollar unresolved issues under Asset Purchase Agreement. After this article was written, the Lehman Court found the "clarification letter" was indirectly approved by the Court, but ruled against Barclays on various issues).

2. Make sure the debtor has prior court authorization to use cash collateral

See In re Delco Oil, Inc., 599 F.3d 1255 (11th Cir. 2010) (ruling that party that sold products to debtor post petition and which was paid by debtor with cash collateral [which the debtor was not authorized to use] would have to disgorge all payments received from the debtor under 11 U.S,.C. § 549).

3. Make sure all payments are authorized by prior court order or are made in the ordinary course of business. See In re Southeast Hotel Properties Limited Partnership, 99 F.3d 151 (4th Cir. 1996) (payments for a NASCAR race hospitality suit not ordinary course transfers).

4. However, loans or transfers not made to debtors, which may increase debtor liability, are generally not avoidable for failure to get court authorization of the transaction.

See In re Stanton, 330 F.3d 939 (9th Cir. 2002) (mortgage lien of bankrupt shareholders of a non-bankrupt company, whose home mortgage lien increased due to advances made on post-petition loans to the company, that was secured by the mortgage and the shareholder's guarantee could not be avoided under 11 U.S.C. § 549).

## F. 11 U.S.C. § 365 - Execution Contracts

1. Failure of Nondebtor Party to Continue to Abide by the Terms of an Executory Contract May Result In Sanctions.

See In re AC Direct, Inc., ___ B.R. ___ 2010 WL 571813 (Bkrtcy M.D. Fla. 2010) (sanctions may be imposed for unauthorized post-petition "termination" of an executory contract); In re Thomas B. Hamilton Co., Inc., 969 F.2d 1013, 1020 (11th Cir. 1992)(same).

2. Further, entry into contracts post-petition, require court approval if they are not part of the "ordinary course of business" of the debtor. See In re Roth, American Inc., 975 F.2d 949 (3rd Cir. 1992) (extension of union contract post-petition required court approval).

## G. 11 U.S.C. § 541 - Property of Estate

1. What constitutes property of the debtor is an issue which requires court approval. See In re Bean, 252 F.3d 113 (2nd Cir. 2001) (determining that net equity in property is only property of the estate, not the gross value of the property, ignoring the liens against it).

2. Remember that partnership property is not property of an individual debtor partner. See Matter of Newman, 875 F.2d 668 (8th Cir. 1988) (transfer of assets of a partnership in which the debtor had an interest, after the debtor's bankruptcy were not subject to avoidance under 11 U.S.C. § 549 as they are not property of the estate).

## H. 11 U.S.C. § 549 - Avoidance of Unauthorized Post Petition Transfers

1. Elements of 11 U.S.C. § 549

(i) a transfer of property;

(ii) that occurs post petition; and

(iii) was not authorized by the court. See In re Delco Oil Inc., 599 F.3d 1255 (11th Cir. 2010).

## I. 11 U.S.C. § 554 Abandonment of Property

See e.g., Catalano v. CIR, 279 F.3d 682 (9th Cir. 2002) (stay relief does not result in abandonment of the property on which relief was granted without court order approving the abandonment.)

## J. Bankruptcy Rule of Procedure 9019: Settlements of Claims and Disputes in Bankruptcy Cases

1. Prior court approval is necessary for settlements with debtors to be binding. See Matter of Triple E Transport Inc., 169 B.R. 368 (E.D. La. 1994) (settlement requires prior court approval); In re Ross-Thacker, ___ B.R. ___ 2005 WL 3263932 (Bkrtcy. D.D.C. 2005) (debtor sanctioned for accepting funds in unauthorized settlement.)

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# Tis Better to Seek Permission Than Beg for Forgiveness in Bankruptcy: A Further Lehman Report

Happy New Year to the regular insomniac readers of Straight and Narrow. In this month's installment, the authors again[1] report from the battlefront in the Lehman Brothers Holdings Inc. Chapter 11 case currently pending in the United States Bankruptcy Court for the Southern District of New York on two separate issues, Bank of America's ("BOA") post petition setoff of $500,000,000 before seeking stay relief and the decision of Barclays not to seek specific court approval of the now infamous "Clarification Letter[2] Both involve the basic question of when and whether bankruptcy court approval is necessary for the debtor and non-debtor parties to take certain actions.

## A. Possession Is Not Nine Tenths Of The Law When 11 U.S.C. § 362 Is Involved: The Bank Of America V. Lehman Brothers Holdings, Inc. November 16, 2010 Opinion[3]

The facts of the BOA AP as they involve the automatic stay are fairly straightforward, although the intricacies of New York offset law, special account law and the applicability of 11 U.S.C. § 362(b)(17) under the facts of this case are not. In short, Lehman's cash management system included several accounts at BOA, accounts that during any given day would often become overdrawn. BOA tolerated this for some time, given Lehman's long history of sorting out these matters by the end of any given business day.

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[1] The authors confess to a slight fixation on Lehman and its really big numbers. See Lubben The Sale of the Century and its Impact on Asset Securitization: Lehman Brothers, 27 ABI J. 1 (Jan. 2009); Bowles, Who Do You Trust, 29 ABI J. 28 (Mar. 2010); Bowles, Bankruptcy's Verdun? The Report From The Lehman Sale Front, 29 ABI J 36 May 2010).

[2] The "Clarification Letter" was a letter related to the Lehman Barclays assets purchase agreement which was not presented to the court prior to entry of the sale order and according to Judge Peck, was not approved by the Court. See, e.g., Comstock, "Bankruptcy Judge Bombshell," Bloomer Business Insider, October 21, 2010 www.businessinsider.com.

[3] Adv Pro 08-01753 ("BOA AP") Doc. No. 89 ("BOA Opinion").

Then in July 2008, Lehman, due to an internal accounting error, was overdrawn in one BOA account was overdrawn by $650 million. Coming about five months after Bearn Sterns, this understandably made BOA a wee bit nervous. BOA demanded and ultimately received a $500 million deposit account ("Overdraft Account") in which BOA was granted a security interest specifically to secure against future overdrafts by Lehman in its BOA accounts.[4] The security agreement also included "boilerplate" provisions under which BOA retained its statutory and common law rights.[5]

After Lehman filed bankruptcy, there was at best negligible overdraft liability that the overdraft account was to secure; however, BOA was allegedly owed over $1.9 billion and Lehman's guarantee of unrelated derivatives transactions[6] ("Derivatives Debt"). On November 10, 2008, BOA, without first obtaining relief from the automatic stay, apparently in reliance on the safe harbor language of section 362(b)(17) of the Bankruptcy Code, took the money on deposit in the Overdraft Account.

After extensive litigation over summary judgment motions in the BOA AP, the court issued its BOA Opinion on November 16, 2010, which found that BOA setoff was improper and it constituted a deliberate stay violation.[7] In a passage that should be a forceful reminder of the

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[4] Due to massive fluctuations in the balances of the clearing accounts due to the number of separate deposits and withdrawals, Lehman clearing accounts were often overdrawn at any given moment and BOA had previously agreed to allow the short term overdrafts. BOA Opinion at p. 4.

[5] Id. at pp. 16-18.

[6] Id. at p. 7 n. 7. Lehman had guaranteed the performance of a subsidiary under an ISDA Master Agreement with a BOA predecessor8 One of the authors – the one without real clients to complain about it – has argued that these safe harbor provisions are a bad idea and should be repealed. Stephen J. Lubben, Derivatives and Bankruptcy: The Flawed Case for Special Treatment, 12 U. Pa. J. Bus. L. 61 (2009). Section 362(b)(17) provides for an exemption to the automatic stay for the exercise by a swap participant or financial participant of any contractual right (as defined in section 560) under any security agreement or arrangement or other credit enhancement forming a part of or related to any swap agreement, or of any contractual right (as defined in section 560) to offset or net out any termination value, payment amount, or other transfer obligation arising under or in connection with 1 or more such agreements, including any master agreement for such agreements..

[7] Id. at p. 44.

importance of seeking stay relief when there is even a reasonable question to the stay applicability, the Court held

> It is difficult to understand how BOA could have thought that taking the money was the right thing to do without first seeking permission from the Court. While being free to advance novel theories, lenders and other counterparties must be obedient to the bankruptcy law as it is written and should exercise great care in determining the applicability of any claimed exception to the automatic stay before presuming to have the right to take debtor property without court approval.
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> BOA acted with the advice of experienced and sophisticated counsel. The Court assumes that BOA was fully informed regarding the untested, uncertain and extremely aggressive legal position that it was advancing and the risks it was thereby assuming that the exception to the automatic stay on which it relied might be found inapplicable to the seizure of LBHI's collateral. BOA, in the Court's view, had a responsibility to approach the setoff issue with far more restraint than was shown here, and the Court believes that the actions taken were surprising and, quite frankly, disappointing for a leading financial institution that should care a great deal about its reputation. BOA's setoff of property of Lehman is not supported by any reasonable application of the exception to the stay to the undisputed facts, and further proceedings will be needed to determine an appropriate remedy for this calculated violation of Section 362(a)(7) of the Bankruptcy Code.[8]

### B. Court Approval Of Amendments And/Or Clarifications Of Sale Orders And Their Underlying Agreements: A Multibillion Dollar Question[9]

It is a stark commentary on the size and complexity of today's financial services industry in general and the Lehman case in particular, that the BOA dispute is not the largest example of an issue that a party decided not to placed before the bankruptcy court.

As noted in footnote one, the authors have written extensively on legal issues related to the sale of Lehman brokerage assets to Barclays ("Sale").[10] The latest aspect of interest is the failure of Barclays or any other party to seek separate court approval of the Clarification Letter.

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[8] Id. at 44-45.

[9] One of the authors admits to being a total coward on this issue. In a case several years ago, as Debtor's counsel and sought, over the objections of the buyer's law firm, clarification of an 11 U.S.C. § 363 sale order to eliminate 20 plus year old oil and gas exploration leases.

The Clarification Letter is a letter agreement between the parties dated "as of September 20," but which was only finalized and executed on September 22, 2008, some two days after the hearing on the Sale concluded and the Order approving sale was entered. The parties hotly dispute its purpose, with Lehman arguing that the Clarification Letter materially altered the terms of the sale[11] and Barclays primarily arguing that the Clarification Letter was approved by the Court, even if the Court did not realize that it had done so, and the Clarification Letter was in any events essentially meaningless, as all assets in question were transferred to Barclays by the APA and Sale Order anyway.[12]

At the beginning of the final arguments in the Barclays' Lehman litigation by Barclays' counsel, the Court rejected Barclays' first argument stating from the bench: "Let me be clear about something.... I never approved the Clarification Letter. You're making a circular argument about what the Sale Order says."[13] While the Court has not entered its final order in this litigation, it seems unlikely that Barclays can prevail on this issue at the bankruptcy court level in spite of its numerous arguments advanced on this issue, including: (a) Lehman and the SIPA trustee are estopped from arguing that the Clarification Letter was not approved by the Court;[14] (b) the amendments of the Clarification Letter were allowed by the Court without

[10] For this reason, we will only briefly discuss the details of the sale.
[11] In some of its initial pleadings, Barclays also stated the Clarification Letter transferred different or substituted assets from those transferred under the sole APA. See Lehman post trial brief at pp. 5-6, for examples.
[12] See Barclays Post Trial Brief at para 91, "For example, before the Closing on September 22, 2008, Movants *knew* the express terms of the Clarification Letter, and that it provided for Barclays to acquire all of the Repo Collateral, the Clearance Box Assets, the ETD Margin (as also confirmed in the Sale Order, the TAA and numerous e mails with the OCC), and the $769 million in 15c3-3 securities (or equivalent securities). *See* FOF ¶¶ 31.14, 43, 44.1.5, 45.1, 44.4, 48.1-48.9, 48.9, 48.120-48.125. Movants chose not to come back to Court because they believed those terms had *already been approved* (and hence would certainly be approved if presented in a new hearing). *See* FOF ¶¶ 39, 58. They are in no position now to argue otherwise."
[13] See footnote 11; Lehman's Post Trial Brief at p. 6.
[14] Barclay Post Trial Brief at para. 154.

approval;[15] (c) Lehman and the trustee are barred from seeking return of the assets transferred pursuant to the Clarification Letter;[16] or (d) the Court lacked jurisdiction to hold the Clarification Letter was not approved by the Court.[17]

While Barclays has raised numerous factual, legal and equitable issues to demonstrate that the Clarification Letter is either approved or irrelevant, the facts and post trial briefs filed in this case clearly establish that there was at least a legitimate question as to whether the Clarification Letter needed court approval. Further, going back to the court to seek a hearing on court approval of the Clarification Letter would have been easy to obtain,[18] and there were no time pressures on the closing of the sale transaction that would have prevented the parties from seeking court approval.[19]

### C. OK So I Didn't Get A "Comfort Order" From The Court Before Taking Action, It Does Matter Under These Facts!

There is one extremely creative, strongly factually based, and at the same time, troubling argument raised by Barclays in their Post Trial Brief, which bears further consideration. At paras 87-90, of its post hearing brief, Barclays argue that even if it did not seek required court

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[15] Id. at paras. 155-158.
[16] Id. at paras. 159-160.
[17] Id. at paras. 202-203.
[18] "Lewkow also admitted that the Closing could have taken place 'a day or two later' than September 22 and that the parties could have returned to Court on September 22. Ms. Leventhal confirmed that the FRBNY had set no deadline for a Monday closing, it just wanted the deal closed as soon as possible. And the Asset Purchase Agreement itself contained no contractual obligation to close before the markets opened on Monday, September 22. (M.1 ¶ 4.4; 8/31/10 [Lewkow] 177:20-178:21 ('there was a very strong desire' to close Monday but no drop-dead date of Monday in the Assert Purchase Agreement).) Indeed, the September 17 Barclays Press Release had previously disclosed to the public that the closing would take place before September 24, that Wednesday." Lehman Post Trial Brief at para 725.
[19] "The problem is that you're making an argument about Court approval of the clarification letter and a very critical feature of the current dispute. And it is absolutely clear, based upon the evidence, that the parties who prepared the clarification letter during the weekend immediately following the sale hearing were ware that one of the options available to them was to come back to court and to [obtain] express approval of that document which everyone recognizes effected certain substantial changes in the transaction. In lieu of doing that, the parties, including Barclays, determined that no such approval was required and instead, the letter was lodged in the docket.

approval of the Clarification Letter, that fact is irrelevant because the Court, as an absolute matter of fact, would have approved the Clarification Letter if it had been submitted for such approval. Barclays states at para 87 of its post trial brief,

> Even if the Court were to conclude that there were shortcomings in the disclosures made at the September 19 Sale Hearing, or that the parties should have returned to Court on or before the morning of September 22 to present the Clarification Letter, the evidence at trial showed that any 'additional disclosures' that might be hypothesized would simply have confirmed that the Sale was reasonable and was correctly approved.

While the authors believe that Barclays is likely right as a matter of fact with this argument, given the reality of September 2008.

But as a policy matter, this argument should be rejected. While under extreme time pressures and extremely compelling facts, Courts have approved willful stay violations *nunc pro tunc*,[20] such approval only comes where time pressures are such that, unlike here, there is an extreme time pressure requiring immediate action by the creditor.

In Lehman case, Barclays' argument, taken to its full extreme, would mean that buyers, debtors and committee members would have full and unfettered control over what assets were included in asset sales, rather than the Court. Such a result would greatly weaken, if not fatally eliminate, the clear oversight and control given to courts under 11 U.S.C. § 363 and its related

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Thereafter, it was referenced in various pleadings. But at [no] time did anyone ever seek formal approval of that document." [emphasis added] Lehman Post Trial Brief at para 343.

[20] See e.g., In re Casse, 198 F.3d (2nd Cir. 1999) (Chapter 13 case dismissed *nun pro tunc* to date of filing. In re Meyers, 334 B.R. 136 (E.D. Pa. 2005) In re Albany Partners Ltd., 799 F.2d 670 (11th Cir. 1984). Indeed, BOA request for *nun pro tunc* stay relief was rejected as BOA's request being without merit in the BOA action.

provisions. While 363(m) encourages finality in sale orders, it does not give carte blanche to buyer interpretation of sale orders and the provisions of underlying APA's.[21]

### D. So We Guessed Wrong, What is the Worst That Can . . . O No Mr. Bill[22]

As both the BOA and Barclays[23] litigation show, action without necessary or even arguably necessary court approval is extremely dangerous in bankruptcy cases. First, taking such actions without first obtaining court approval can create a negative impression with the court. The automatic stay and clear judicial authority over the estate are prerogatives strongly guarded by bankruptcy courts. Even the appearance of slighting the requirements of the Code or the authority of a court is not well received by judges and may put your client in an unwanted and likely unnecessary "hole" in the underlying litigation. Second, actions taken without necessary court approval are at the very least voidable[24] and in many cases void as a matter of law. Therefore, even if your actions would not draw the ire of a court, they will likely be a costly exercise in futility for you or your client. Therefore, coming back to the title of this Column, remember when in doubt try to err on the side of seeking permission. The transaction you save may be your own.

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[21] See, generally, e.g., In re LWP, Inc., 2007 WL 2668512 (W.P. Ky. Sept. 6, 2007); Morrison v. Brosseau, 377 B.R. 815 (Ed. Tx. 2007).

[22] While we am not comparing judges to Mr. Sluggo or Mr. Hands of Saturday Night Live, the pain inflicted on Mr. Bill can be analagous to what can happen if a party acts without needed court approval. The younger half of the writing duo had to look up these references on Wikipedia; his parents didn't let him stay up late. http://en.wikipedia.org/wiki/Saturday_Night_Live_TV_show_sketches_of_the_1970s#The_Mr._Bill_Show.

[23] While at the time of writing of this article, no final decision on the Barclays litigation has been entered by the Court, even if it were to prevail, it will have incurred tens of millions of dollars in unnecessary legal fees.

[24] See, e.g., Eastern Refractories Co. Inc. v. Forty Eight Insulations, Inc., 157 F.3d 169 (2nd Cir. 1998); In re Albany Partners, Ltd., 749 F.2d 670, 675 (11th Cir. 1984).

# OBTAINING COURT APPROVAL: A FEW TIPS AND TRAPS FOR CONSUMER BANKRUPTCY ATTORNEYS

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**This outline generally reflects my interpretation of the provisions of the Bankruptcy Code (as amended by BAPCPA), of the Federal Rules of Bankruptcy Procedure, and of case decisions relating to consumer bankruptcy practice.**

**As the chapter 13 trustee in the Eastern District of Kentucky, I reserve the right to take a contrary position in any particular case depending on the facts of that case, and I reserve the right to argue an interpretation of the law that may differ from that set forth in these materials.**

**Furthermore, the outline does not necessarily reflect the views of other panelists.**

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# OBTAINING COURT APPROVAL: A FEW TIPS AND TRAPS FOR CONSUMER BANKRUPTCY ATTORNEYS

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Introduction:

This outline is intended to highlight a few areas of bankruptcy practice (with primary emphasis on chapter 13 practice) where obtaining court approval is necessary and sometimes tricky. The outline also highlights a few areas where requesting court approval in order to remedy an attorney's mistake will be unsuccessful because the court is restrained by the Code or Rules from providing the relief hoped for. Finally, some questions are raised that are intended to be food for thought.

The reader is assumed to possess more than a rudimentary knowledge of bankruptcy terms and concepts. This outline is not to be relied on as a substitute for the reader's own research.

References herein to "§" are to sections of Title 11, United States Code. References to "Rule" are to the Federal Rules of Bankruptcy Procedure.

**A) Credit Counseling and Eligibility: § 109(h)**

1) Court approval is necessary:
   a) To obtain an "exigent circumstances" delay in getting credit counseling (§ 109(h)(3));
   b) To get a waiver of the requirement for credit counseling due to disability, incapacity, or active military duty in a combat zone (§ 109(h)(4)).
2) But the deadlines and procedures are unforgiving.
   a) The debtor must file with the petition, either:
      (i) the credit counseling certificate (Rule 1007(b)(3)(A)),
      (ii) the "exigent circumstances" certification (Rule 1007(b)(3)(C)), or
      (iii) the request for determination that the debtor need not get credit counseling due to disability (Rule 1007(b)(3)(D)).
   b) There is no exception for the court to order otherwise with respect to the timing or filing of these documents. Rule 1007(c); Rule 9006(b)(3).
3) Compare the situation where the debtor obtained credit counseling but has not received the certificate yet: "Unless the court orders otherwise," if the debtor files a statement with the petition that the debtor has received credit counseling but

does not have the certificate (Rule 1007(b)(3)(B)), the certificate must be filed within 14 days from the date of the petition. Rule 1007(c).

4) Tips and traps:

a) Debtors' attorneys must be careful not to check the box on Exhibit D to the Petition ("Individual Debtor's Statement of Compliance With Credit Counseling Requirement") that says the debtor received credit counseling but has not yet received the certificate (Box #2), if what is meant is that the debtor did not get prepetition credit counseling due to exigent circumstances (Box #3) or disability (Box #4). The rules do not allow for an extension of time after the petition is filed in which to file the exigent circumstances certification or the request for waiver due to disability, so asking the court to approve an exigent circumstance or waiver is to no avail if the proper certification was not made with the petition.

b) Attorneys must be aware of what constitutes "exigent circumstances" and the procedures necessary to assert an exigent circumstance exception (did the debtor request and was unable to obtain credit counseling in the preceding 7 days, and is the exigent circumstance explanation "satisfactory to the court").

c) If the debtor is seeking a waiver due to incapacity, disability, or military duty, a motion must be filed with the petition. The Exhibit D Statement alone is insufficient (the Form even says "Must be accompanied by a motion for determination by the court."). The rules do not allow for an extension of time in which to file the motion.

d) Attorneys must also remember that if the debtor did receive pre-petition credit counseling, it must have been done within 180 days prior to the filing of the petition (a potential trap for a debtor in his/her second or third bankruptcy case). § 109(h)(1). The court cannot cure this jurisdictional defect.

**B) Automatic Stay Issues: Repeat Filers**

1) Court approval is necessary to extend the automatic stay of a repeat filer with one prior dismissed case.

a) The automatic stay terminates on the 30th day after a petition is filed if the debtor had a case pending within the previous year that was dismissed. § 362(c)(3).

b) "On motion of a party in interest for continuation of the automatic stay and upon notice and hearing, the court may extend the stay in particular cases as to any or all creditors (subject to such conditions or limitations as the court may then impose) after notice and a hearing completed before the expiration of the 30-day period only if the party in interest demonstrates that the filing of the later case is in good faith as to the creditors to be stayed . . . ." § 362(c)(3)(B).

(i) The debtor must overcome the presumption that the case was not filed in good faith. § 362(c)(3)(C).

(ii) The hearing must be concluded before the 30th day after the petition is filed.

2) Similarly, court approval is necessary to impose the automatic stay if the debtor had 2 prior cases dismissed within the previous year. § 362(c)(4)(A)(i).

a) "if, within 30 days after the filing of the later case, a party in interest requests the court may order the stay to take effect in the case as to any or all creditors (subject to such conditions or limitations as the court may impose), after notice and a hearing, only if the party in interest demonstrates that the filing of the later case is in good faith as to the creditors to be stayed . . . ." § 362(c)(4)(B).

(i) The request must be made within 30 days after the petition is filed. § 362(c)(4)(B).

(ii) The debtor must overcome the presumption that the petition was not filed in good faith. § 362(c)(4)(D).

(iii) The stay is not effective until an order is entered. § 362(c)(4)(C).

b) In the meantime, upon request of a party in interest, "the court shall promptly enter an order confirming that no stay is in effect." § 362(c)(4)(A)(ii).

3) Tips and traps:

a) In some jurisdictions, the need to request an extension of the automatic stay is considered unnecessary because of a majority view of courts that the stay is only terminated as to property of the debtor, but continues in effect against property of the estate. However, this view is not uniformly adopted. See In re Reswick, 446 B.R. 362 (9th Cir. BAP 2011) (debtor did not seek to extend the stay in his chapter 13 case; after 30 days, the creditor's wage garnishment did not violate section 362 as there was no longer a stay).

b) When there has been only one prior dismissed case, the hearing on the debtor's motion to extend the stay must be CONCLUDED before the 30th day. A request to extend the stay made too late for the court to conclude the hearing by the 30th day will likely have no effect.

c) Confirmation of a plan, while not reviving the automatic stay, might bind the creditor as to the treatment of its claim, but a delay in confirmation could certainly have adverse consequences for the debtor.

d) Debtors' attorneys who ignore the need to get an extension of the stay do so at their peril.

**C) The Automatic Stay As To Assets of a Debtor's Business Entity.**

1) It is not uncommon for a chapter 13 debtor to have business assets in the name of an LLC or corporation in which the debtor is the sole member or shareholder (e.g., rental property; commercial vehicles). Occasionally a chapter 13 case is filed in an attempt to stop a foreclosure or repossession action against the business assets. The question then arises whether the creditor needs to get relief from the

automatic stay to continue with the foreclosure or other collection efforts against the business.

2) The majority of courts recognize that

   a) The automatic stay does not protect third parties and does not protect property that is not property of the estate or of the debtor.

   b) The LLC or corporation is a legal entity separate and distinct from the member/shareholder debtor (in contrast with a sole proprietorship where the debtor runs a business as a "d/b/a").

   c) It is only the debtor's interest in the LLC or the corporation that becomes property of the estate in the chapter 13 case. The entity's assets are not property of the individual debtor's estate and are not property of the debtor.

   d) A foreclosure action against assets owned a debtor's separate business entity may proceed without being in violation of the automatic stay. In re Biorge, 2011 WL 1134109, Bankr. D. Utah, March 28, 2011 (No. 10-23318) (also suggesting that in some circumstances a temporary injunction might be appropriate to stop a sale).

3) However, one bankruptcy judge recently awarded damages against a creditor that proceeded with a foreclosure sale of property owned by a corporate entity, finding that because the debtor had personally guaranteed the debts of the corporation the automatic stay somehow applied. In re Ebadi, 2011 WL 1257211, Bankr. E.D.N.Y., March 30, 2011 (No. 10-73702-AST).

4) Tips and traps:

   a) Debtors' attorneys should not rely on the automatic stay in an individual's chapter 13 case to protect the business assets under these circumstances, and – the Ebadi decision notwithstanding – would probably not get the court to go along with an argument that the automatic stay applied. It should be noted also that the co-debtor stay of § 1301 applies only as to consumer debts, not business debts, and would therefore be inapplicable.

   b) The debtor's attorney might ask the court to temporarily enjoin the creditor from proceeding with the collection activity against a related party (the LLC or corporation) *a la* a Johns-Manville type injunction to protect related parties, but such relief, if obtained at all, would be very limited. Most likely the LLC or corporation will need to file its own chapter 11 case.

   c) The real trap here is for creditors' attorneys. The Ebadi decision is baffling, but will likely be relied on by debtors' attorneys in other jurisdictions. Creditors may need to ask the bankruptcy court for a comfort order holding that the stay does not apply in order to proceed with the foreclosure sale, or ask the court to annul the stay retroactively to validate the sale.

**D) Court Approval Via Chapter 13 Plan Confirmation? Or By Motion?**

1) There are several rules that specifically refer to a motion as the method to obtain necessary court approval, yet these issues are routinely dealt with in the context of plan confirmation.

   a) The court may determine the value of a secured claim "on motion of any party in interest and after a hearing on notice . . . ." Rule 3012.

   b) The court may determine classes of creditors "on motion after hearing on notice as the court may direct. . . ." Rule 3013.

   c) A proceeding by the debtor to avoid a lien under § 522(f) "shall be by motion . . . ." Rule 4003(d).

   d) Compare Rule 6006: "A proceeding to assume, reject, or assign an executory contract or unexpired lease, other than as part of a plan, is governed by Rule 9014" (relief by motion). Rule 6006(a) (emphasis added).

2) Should chapter 13 plans be combined with these motions? Are separate motions necessary instead? Should the Rules Committee make changes to deal with the realities of chapter 13 practice?

3) Chapter 13 Plan and Payments – Deadlines

   a) The chapter 13 plan may be filed with the petition, but must be filed within 14 days of the petition, "and such time may not be further extended except for cause shown and on notice as the court may direct." Rule 3015(b).

   b) "Unless the court orders otherwise," the debtor's first plan payment in a chapter 13 case is due 30 days "after the date of the filing of the plan or the order for relief, whichever is earlier." § 1326(a)(1).

      (i) Will the plan ever be earlier than the order for relief (i.e., the petition)? It is probably best to conclude that the first plan payment is due 30 days after the petition is filed, unless the court orders otherwise.

      (ii) If a skeletal petition is filed and an extension of time is needed to prepare a plan, it may be appropriate to ask the court to order an extension of the deadline for the first plan payment as well.

   c) Section 1326(a) also requires the debtor to make certain adequate protection payments directly to creditors "unless the court orders otherwise."

      (i) Many courts have ordered otherwise by local rule or general order, so that adequate protection payments are made to creditors and accounted for by the chapter 13 trustee from the debtor's plan payments.

      (ii) If not already reflected in local rules or general order, such a request should be made by motion (unless early confirmation negates the need for preconfirmation adequate protection altogether).

4) Length of plan for a below-median income debtor with an applicable commitment period of 3 years:

   a) "the plan may not provide for payments over a period that is longer than 3 years, unless the court, for cause, approves a longer period . . . ." § 1322(d)(2).

   b) A plan modified after confirmation may not provide for payments over a longer period than the original 3-year period, "unless the court, for cause, approves a longer period . . . ." § 1329(c).

5) Tips and traps:

   a) Sometimes an issue relating to valuation of a secured claim arises in the context of whether an adversary proceeding is necessary to "strip off" a wholly unsecured junior mortgage.

   b) A safe practice might be to style a plan as "plan and motions", and instead of just asserting that a secured claim will be valued as follows, state "The debtor moves the court to value the collateral as follows," thereby complying with the bankruptcy rules as to the manner of obtaining court approval.

   c) Practitioners should be aware that extending the length of a plan past 36 months for a below-median income debtor is not automatic, but instead the court must approve the extension for cause. Presumably an order confirming the plan would constitute the court's approval.

**E) Conversion or Dismissal**

1) A debtor can convert a chapter 13 case to chapter 7 at any time "without court order" by filing a notice of conversion under § 1307(a). Rule 1017(f)(3).

2) A debtor can voluntarily dismiss a chapter 13 case by filing a motion and giving notice of hearing pursuant to Rule 2002(a)(4). § 1307(b); Rule 1017(a), 1017(f)(2). If the case had not previously been converted to chapter 13 from another chapter, "the court shall dismiss the case" "on request of the debtor at any time." § 1307(b).

3) On request of a party in interest, the court may convert or dismiss a chapter 13 case, whichever is in the best interests of creditors and the estate, for cause (including certain enumerated items). § 1307(c).

4) The court may dismiss, or with the debtor's consent convert a case from chapter 7 to chapter 13 for abuse under § 707(b) on motion after a hearing on notice. Rule 1017(e).

5) The court SHALL dismiss a chapter 13 case on request of a party in interest or the U.S. Trustee if the debtor fails to file prepetition tax returns within the deadlines set forth in § 1308. § 1307(e).

6) Tips and traps:

   a) The Supreme Court case of Marrama v. Citizens Bank of Massachusetts, 127 S.Ct. 1105 (2007) might impact a debtor's ability to convert from chapter 7 to

chapter 13 (chapter 7 debtor who engaged in bad faith conduct could not convert to chapter 13).

b) Debtors' attorneys must be aware of the requirement in § 1308 for filing with the IRS and other taxing authorities prepetition tax returns prior to the § 341 meeting, especially if the petition is filed between January 1 and April 15.

(i) If the trustee concludes the section 341 meeting, the tax returns have not been filed as required by § 1308, and the IRS or any other party files a motion to dismiss, "the court SHALL dismiss the case." See In re Cushing, 401 B.R. 528 (1st Cir. BAP 2009).

(ii) Asking the court to extend the time for filing those tax returns will be fruitless at that point.

(iii) Even the one instance set forth in § 1308 in which the court can provide limited relief is only available "After notice and a hearing, and order entered before the tolling of any applicable filing period [under § 1308(b)] . . . ." § 1308(b)(2).

**F) Certain Discharge Issues in Chapter 13 Cases**

1) § 523(a)(2), (a)(4) and (a)(6) debts in chapter 13:

a) After BAPCPA, debts under § 523(a)(2) or (a)(4) are discharged in chapter 13 unless "on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge. . . ." § 523(c)(1).

(i) This of course requires an adversary proceeding. Rule 7001(6).

(ii) The complaint to determine the nondischargeability of a debt under § 523(a)(2) or (a)(4) must be filed no later than 60 days after the first date set for the § 341 meeting of creditors. Rule 4007(c).

b) Although the same rules apply to debts under § 523(a)(6) in a chapter 7 case, those debts are not excepted from discharge in a chapter 13 case.

(i) It is of no use whatsoever to file an adversary proceeding to ask the court to determine that a § 523(a)(6) debt is nondischargeable in a chapter 13 case.

(ii) If, however, the debtor seeks a hardship discharge, the court would send out a notice setting a deadline for filing a complaint under § 523(a)(6), because such debts would not be discharged by a hardship discharge. § 1328(b).

2) Discharge in prior chapter 7 case affecting the discharge in a subsequent chapter 13 case:

a) "The court shall not grant a discharge . . . if the debtor has received a discharge . . ." in a prior chapter 7 case filed within 4 years of the filing of the present chapter 13 case.

b) How is the court to know not to enter a discharge?

(i) The procedure seems to vary by jurisdictions.

(ii) In some jurisdictions, the debtor must file a form or certification that s/he has not previously received a discharge that would bar a discharge in the present case (the form usually includes other certifications necessary to obtain a discharge) – in other words, the debtor must essentially request entry of a discharge upon completion of plan payments.

(iii) In some jurisdictions, the trustee or U.S. Trustee takes the position that an order is needed to effectuate the "no discharge" provision of § 1328(f) by denying the debtor's discharge or seeking a waiver of discharge.

(1) A motion or an adversary proceeding might be filed to obtain a determination by the court that a discharge is not available under § 1328(f), and these are often styled as seeking a "waiver of discharge."

(2) If the discharge is waived, are the debts owed in this case then nondischargeable in any future bankruptcy case pursuant to § 523(a)(10)? ("A discharge . . . does not discharge an individual debtor from any debt . . . (10) that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor . . . in which the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) . . . .")?

3) Tips and traps:

a) Debtors' attorneys must know the local procedure for determining whether the debtor gets a discharge in the chapter 13 case, and whether the debtor must ask the court for entry of a discharge order.

b) If court approval is sought by the trustee or U.S. Trustee to declare that the debtor is not entitled to a discharge, debtors' attorneys should consider carefully whether a waiver of discharge is the appropriate vehicle.

**G) Representation and Compensation Issues in Consumer Bankruptcy Cases**

1) May a debtor's attorney limit his/her representation of a chapter 13 debtor in the retainer agreement to services rendered up to confirmation, or must the attorney request court approval to limit the representation?

a) Many jurisdictions with "no-look fees" have adopted a Model Retention Agreement, or a "Rights and Responsibilities of Debtors and Their Attorneys," or local rules that dictate what services must be provided by debtor's counsel.

b) If the debtor is unable to afford to pay for post-confirmation services (and the attorney expects payment up front rather than through the plan), can the attorney decline to appear at a hearing? Or must the attorney ask the court for permission to withdraw as counsel?

2) Must a debtor's attorney file an amended Rule 2016 disclosure statement for compensation earned post-confirmation?

3) If the debtor is employing an attorney to represent him/her in a personal injury lawsuit (or other non-bankruptcy cause of action), must s/he file an application to employ a professional under § 327? An application for compensation under § 330?

4) Tips and traps:

a) The answers are largely dependent on local practice and culture.

b) Some courts scrutinize fee applications; other courts rely on a "no-look" fee.

c) Fee applications requesting court approval of compensation for post-confirmation services may or may not be required.

**H) Sale of Property in Chapter 13 Cases**

1) The debtor has, exclusive of the trustee, the rights and powers of a trustee to sell property of the estate under certain subsections of § 363.

2) The debtor must give 21 days' notice to all creditors of a proposed sale, "unless the court for cause shown shortens the time or directs another method of giving notice." Rule 2002(a)(2).

3) An objection to the proposed sale must be filed and served not less than 7 days before the date set for the proposed sale, "or within the time fixed by the court."

4) If property of the estate vests in the debtor at confirmation (§ 1327(b) and (c)), must the debtor obtain court approval to sell property after confirmation?

5) Tips and traps:

a) In many jurisdictions, the form plan, or order confirming the plan, or other court order bars the debtor from selling property without prior court approval, regardless of the vesting issue.

b) A motion seeking court approval for a sale may be more in the nature of seeking approval of a post-confirmation plan modification than of a § 363 sale. Either way, appropriate notice and full disclosure of the terms of the sale are required.

c) Perhaps the biggest trap for debtors' attorneys is the "nobody told me" lament of debtors after they sell property without court approval, use the proceeds improperly, and face a trustee's motion to dismiss or a motion to modify the plan to increase the dividend to unsecured creditors. Counsel should advise their clients (and document the advice given) that court approval will be required before selling any property.

**I) Incurring Debt**

1) Chapter 13 debtors often need to incur debt at some time during the life of the case, for example, to repair or replace a car, to buy a house, or perhaps even to refinance a home loan on more favorable terms.

2) There are no specific Code provisions or Rules authorizing a debtor to incur debt or requiring the debtor to seek court approval.

3) Tips and traps:

a) The form plan, order confirming, local rule, or other general order might require the debtor to get court approval to borrow money or incur debt.

b) Local practice usually dictates the procedure, and local rules or the chapter 13 trustees often supply forms that are expected to be used.

c) A motion to incur debt may be more in the nature of a motion to modify the plan after confirmation.

d) Is borrowing money post-petition from a 401K or other exempt retirement account "incurring debt" that would require court approval?

e) Does a HAMP (or other consensual) mortgage modification require bankruptcy court approval?

f) As with advising debtors not to sell property without court approval, debtors' attorneys should counsel their clients not to borrow money, go into debt, or refinance an existing loan without prior court approval.

**J) Settlement of Personal Injury or Other Cause of Action.**

1) Prepetition causes of action are property of the estate. § 541(a)(1). In a chapter 13 case, causes of action that arise post-petition might also be property of the estate. § 1306(a)(1).

2) Does the debtor need court approval to:

a) Pursue the cause of action?

b) Employ counsel to pursue the cause of action?

c) Approve a settlement or compromise?

3) If property of the estate vests in the debtor at confirmation (§ 1327(b) and (c)), must the debtor obtain court approval of the above after confirmation?

4) Does it matter if the cause of action is exempt?

5) Tips and traps:

a) Local practice and customs often dictate the procedure.

b) The plan or order confirming the plan might authorize the debtor to prosecute the cause of action but pay non-exempt proceeds into the plan for the benefit of unsecured creditors. Such provisions might require the debtor to get court approval of the employment of counsel or of a settlement.

c) The biggest trap for debtors and their attorneys is in the failure to disclose the cause of action to begin with. Nonbankruptcy courts now regularly apply the doctrine of judicial estoppel to bar the debtor from pursuing a cause of action that s/he did not disclose in the bankruptcy case. Asking the bankruptcy court to reopen a bankruptcy case or to vacate an order confirming a plan to allow the debtor to amend the schedules and disclose the cause of action will likely not salvage the situation. White v. Wyndham Vacation Ownership, Inc., 617

F.3d 472 (6th Cir. Aug. 11, 2010) (debtor's attorney's affidavit that failure to disclose was due to inadvertence was not adequate; debtor was judicially estopped from prosecuting her sexual harassment claim against former employer).