Consumer Case Law Update

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I. The Automatic Stay

In re Dyer, 2013 Bankr. LEXIS 928, (B.A.P. 6th Cir. March 14, 2013)(Lloyd, B.A.P.J.).

Debtors appealed an order from the bankruptcy court denying confirmation of their plan, dismissing their case and requiring their attorney to disgorge his fees due to the fact that no automatic stay was in place. The debtors' prior bankruptcy case had been dismissed within a year, and when they filed their second chapter 13 case, their attorney failed to move for the stay to be extended pursuant to § 362(c)(3)(B). The debtors proposed a plan and no parties objected. Prior to confirmation, the bankruptcy court issued an order *sua sponte* asking the debtors to show why their case should not be dismissed since there was no automatic stay. The court also required debtors' counsel to explain why his fees should not be disgorged. Debtors argued that an automatic stay was not necessary for plan confirmation and that an extension of the stay was not necessary because the stay only expired as to the "debtors" and not as to property of the estate. The bankruptcy court was not persuaded and dismissed the case. On appeal, the appellate panel determined that the bankruptcy court had abused its discretion. Confirmation of a plan is only dependent upon the requirements of § 1325 and does not require a stay pursuant to § 362. As a result, the failure to extend the stay was a not a valid basis to deny confirmation of an otherwise confirmable plan or to require debtors' counsel to disgorge fees.

Trailer v. Troy Univ. (In re Trailer), 2013 Bankr. LEXIS 1035 (Bankr. M.D. Ala. March 18, 2013) (Williams, B.J.).

The Chapter 13 debtor filed a complaint against university for willful violations of the automatic stay pursuant to 11 U.S.C. § 362(a)(6) on the basis that the university refused to release her transcripts. The Debtor scheduled the university as an unsecured creditor and gave the university notice of her bankruptcy filing. She requested a copy of her official transcript and offered to pay the standard fees for preparation of the transcript; however, in accordance with its standard policy, the university refused to provide the transcript due to the unpaid debt owed by the debtor. The bankruptcy court held that the university's refusal to turn over the transcript was a willful violation of the automatic stay because it had notice of the bankruptcy and intended to pressure the debtor into paying the debt by withholding the transcript. The court stated that the fact that the debt was presumptively nondischargeable was irrelevant. The debtor was awarded actual damages for attorney fees.

In re Hatten, 2013 Bankr. LEXIS 1017 (Bankr. W.D. N.C. March 19, 2013) (Beyer, B.J.)

A servicer for a mortgage company moved for relief from the automatic stay in order to exercise its state law rights against the debtor's residence pursuant to § 362(d). The debtor objected to the motion and moved to have it dismissed on the basis that the servicer lacked standing to bring the motion and was not a 'party in interest' because the promissory note presented by the movant was not endorsed to the servicer or affixed with an allonge. The bankruptcy court denied the debtor's motion, finding that the debtor could not take a position inconsistent with his bankruptcy schedules, which identified the servicer as the mortgagor (even though the debtor misspelled the servicer's name). Further, the principle of *res judicata* applied, and the debtor was bound by the provisions of his confirmed Chapter 13 plan, which provided

for payment to the servicer. The debtor was estopped from challenging the standing of servicer, and the bankruptcy court granted the servicer's motion to lift stay.

II. Discharge Issues

Canning v. Beneficial Maine, Inc. (In re Canning), 2013 U.S. App. LEXIS 2317 (1st Cir. February 1, 2013)(Toruella, C.J.)

The debtors filed a Chapter 7 bankruptcy case and indicated an intent to surrender their residence to the mortgage company. They then received a discharge of their personal liability on the mortgage loan and vacated the premises. Later, the debtors demanded that the mortgage company foreclose on the residence or release their lien. The mortgage company sent letters to the debtors acknowledging the discharge of their personal liability on the loan but refusing to release their lien or to foreclose on the property. The mortgage company stated that they would be willing to consider a settlement offer or a short sale of the property. Debtors reopened their bankruptcy and filed a complaint against the mortgage company alleging violations of the discharge injunction. The bankruptcy Court found no violation and the BAP affirmed. The debtors then appealed to the First Circuit Court of Appeals. The court affirmed the lower court rulings and found no discharge violation. In doing so, the court found that the present case was distinguishable from the *Pratt* case, wherein the Court had previously held that a secured creditor's refusal to repossess an inoperable vehicle or to release their lien was coercion that violated the discharge injunction. *Pratt v. GMAC* (In re Pratt), 462 F.3d 14 (1st Cir. 2006). Unlike a worthless vehicle, the real property collateral in this case was not worthless and the value could increase over time. Furthermore, the creditor's offer to consider a settlement or short sale indicated that they only intended to collect no more than the value of the property at issue.

Mele v. Bank of Am. Home Loans (In re Mele), 2013 Bankr. LEXIS 455 (Bankr. N.D. Ga. January 8, 2013) (Ellis-Monro, B.J.).

A debtor filed a Chapter 13 bankruptcy case which was subsequently converted to Chapter 7. The debtor received a discharge, which included discharge of her personal liability on her residential mortgage. After the case was closed, the mortgage company sent the debtor over 15 letters in an eighteen month period. The debtor reopened her case and filed a complaint against the mortgage company alleging violations of the discharge injunction and requesting damages in excess of $2 million. The bankruptcy court held that the mortgage company did not violate the discharge injunction because the letters were merely informational, required by the FHA, or responses to requests made by the debtor herself. The letters also included information about how the debtor could avoid foreclosure. The creditor did not make any phone calls to the debtor or otherwise harass her or demand payment.

Rabbi Harry H. Epstein School, Inc. v. Goldstein (In re Goldstein), 2012 Bankr. LEXIS 6034 (Bankr. N.D. Ga. November 26, 2012)(Diehl, B.J.).

A private school filed an adversary proceeding against a Chapter 7 debtor seeking a determination that the debt owed to the school for tuition for the debtor's minor children was nondischargeable as an educational loan pursuant to § 523(a)(8). The court granted the school's motion for judgment on the pleadings finding that the debt was properly characterized as an educational loan. The debtor signed a contract agreeing to pay for his children's education in

installment payments over time, and the school provided the agreed upon one year of educational services. It was irrelevant that the education was not for "higher education" because Congress removed that requirement in 1984. It was also irrelevant that the education was not received by the debtor individually, but by the debtor's children.

In re Lynch, 2012 Bankr. LEXIS 5222 (Bankr. W.D.N.C. November 7, 2012)(Beyer, B.J.).

The Chapter 7 debtors proposed to except a $24,000 debt secured by a fishing boat from discharge and sought approval from the bankruptcy court for a reaffirmation agreement. Although the debtors were represented by counsel and the attorney signed the reaffirmation agreement, the agreement also indicated that debtors were not represented by counsel in negotiation of the agreement. As a result, the bankruptcy court scheduled a hearing to consider approval of the reaffirmation agreement. The debtors' schedules indicated that their monthly expenses exceeded their income by more than $1200. Despite the fact that the debtors testified that they could afford the monthly payments on the boat debt of $279, the bankruptcy court denied the reaffirmation agreement. In doing so, the court found that the reaffirmation agreement was not in their best interests because it was unlikely that they had actually reduced their expenses enough to afford the boat, the value of the boat was considerably less than the amount owed, and the boat was not a necessity. The court found that it had an duty to determine that the reaffirmation agreement was not an undue hardship on the debtors and that it was in their best interests whether or not it represented a consensual agreement.

III. Trustee's Avoidance Powers

Walschmidt v. Bank of Am. (In re Wheeler), 2012 Bankr. LEXIS 5048 (Bankr. M.D. Tenn. October 26, 2012)(Mashburn, B.J.).

A Chapter 7 trustee filed a complaint against a mortgage creditor pursuant to § 544(a) in order to use his strong-arm powers to bring the debtor's residence into the bankruptcy estate. In conjunction with a refinance of the debtor's home, the mortgage creditor accidentally executed a release of the deed of trust while failing to simultaneously record a substitute deed of trust. The substitute deed of trust was not yet recorded when the debtor filed the Chapter 7 bankruptcy case. The release had also not been recorded at the time the case was filed, but it was recorded one day after the bankruptcy case was filed. The bankruptcy court held that the trustee's ability to recover property for the estate through its strong arm powers was established at the time the case was filed. The original deed of trust was a matter of public record when the case was filed, so the trustee's attempt to avoid it fails. The trustee argued that his rights as a BFP or a lienholder would be superior to the mortgage company at the time of filing because the underlying indebtedness securing the first deed of trust had already been satisfied by the refinance. The court rejected this argument noting that in that circumstance, the doctrine of equitable subrogation would apply to the mortgage creditor. As the court said, "what a difference a day makes."

Hutson v. Branch Banking & Trust Co. (In re Wilson), 2013 Bankr. LEXIS 535 (Bankr. M.D.N.C. February 8, 2013)(Stocks, B.J.).

The chapter 7 trustee filed a complaint against a mortgage creditor seeking to avoid a bank's lien on the debtors' residence through his § 544 strong-arm powers. The mortgage

creditor made a loan to the debtors which was evidenced by a promissory note and a deed of trust executed in April 2003. The note signed by the debtors showed an incorrect date of April 2002. The deed of trust was correctly dated April 2003 and indicated that it secured an indebtedness represented by a note of the same date. The trustee sought a ruling from the court that a deed of trust referencing an incorrect date for the underlying debt is invalid. The bankruptcy court refused to adopt such a bright-line approach and instead reviewed the specific facts of the case and underlying loan documents as a whole. The court found that the deed of trust sufficiently identified the underlying debt by referencing the "loan amount, property address, application number, 'MIN' number, names of the borrowers, and loan number, which match the information reflected on the face of the Note." The court granted the mortgage creditor's motion for summary judgment.

IV. Determination of Secured Status pursuant to 11 U.S.C. § 506(d)

McNeal v. GMAC Mortg., LLC (In re McNeal), 477 Fed.Appx. 562 (11th Cir. May 11, 2012)(*not for publication*).

A Chapter 7 debtor appealed a bankruptcy court ruling denying their motion to strip off a wholly unsecured mortgage pursuant to §§ 506(a) and (d). Relying on the U.S. Supreme Court ruling in *Dewsnup,* the bankruptcy court ruled that a Chapter 7 debtor could not use § 506(d) to strip off a wholly unsecured mortgage. The district court affirmed. In an unpublished opinion, the circuit court reversed the bankruptcy court. In doing so, the court stated that a prior circuit panel had already ruled in the *Folendore* case that a wholly unsecured lien could be stripped off pursuant to § 506(d). *Folendore* was not abrogated by the subsequent *Dewsnup* case because *Dewsnup* held that a partially unsecured lien could not be stripped down pursuant to § 506(d). Because *Dewsnup* was not clearly on point as to a wholly unsecured lien, the prior circuit precedent still controlled.
See Folendore v. U.S. Small Bus. Admin., 862 F.2d 1537 (11th Cir. 1989).

In re Young, 2012 Bankr. LEXIS 5221 (Bankr. E.D.N.C. November 7, 2012)(Humrickhouse, B.J.).

A Chapter 13 debtor moved the bankruptcy court to value her residence and to determine that a homeowner's association lien was void pursuant to § 506(d). The HOA objected on the basis that its statutory lien "runs with the land" and cannot be avoided and is not subject to discharge even if there is no value to secure its lien. Specifically, the HOA argued that the assessments are not "debts" pursuant to § 101(12) because the debtor has no liability on the claim and the HOA has no right to payment from the debtor. The court rejected this argument, found that the lien was wholly unsecured and could be avoided. The court did note, however, that the lien strip only applied to the lien established by the amount due pre-petition. The HOA could still assert its lien rights with respect to amounts accruing post-petition.

In re Plummer, 2013 Bankr. LEXIS 245 (Bankr. M.D. Fla. January 14, 2013)(Williamson, B.J.).

A chapter 13 debtor filed a motion to determine secured status of the condominium association for his residence. The debtor proposed to strip off the association's lien pursuant to 1322(b)(2) on the basis that the amount of the first mortgage exceeded the value of the residence. The association objected and argued that condo associations are granted special liens as an

operation of law and cannot be stripped from the land pursuant to Florida law. The bankruptcy court rejected this argument. Because no part of the condo association's lien was superior to the mortgage creditor's lien, either by the language of the declaration of covenants or common law regarding priority of liens, it could be stripped off. The court also noted that it does not matter that the mortgage creditor would be liable for the condo fees in the event of foreclosure pursuant to Fla. Stat. § 718.116(1) because that in itself was not a lien but rather a right to assert liability and seek payment from the mortgage creditor. The court explicitly stated that its holding only applied to the debtor's ability to strip off the lien and did not preclude the condo association from seeking payment from the mortgage company in the event that the debtor defaulted in the plan and the mortgage creditor foreclosed.

In re Bustamante, 2013 Bankr. LEXIS 994 (Bankr. M.D. Fla. March 15, 2013)(Jannemann, C.B.J.).

A chapter 7 debtor moved to void a creditor community association's wholly unsecured lien on his condo pursuant to § 506(d). The condominium association objected on the basis that association liens are different in character from all other liens treated in the bankruptcy code and that it would be inequitable to strip the lien because the debtor failed to act in good faith. The bankruptcy court rejected the condo association's argument that the provisions of 506(d) did not apply to condo associations and refused to apply the chapter 13 standard of good faith to a chapter 7 debtor. The bankruptcy court ruled that the lien would be avoided upon discharge of the debtor provided that the *McNeal* decision was not vacated by the circuit court or otherwise overruled or abrogated.

V. Chapter 13 Plan Confirmation

A. CMI, PDI, and the ACP

Beaulieu v. Ragos, (In re Ragos), 2012 U.S. App. LEXIS 22334 (5th Cir. October 29, 2012)(Davis, C.J.)

Chapter 13 debtors proposed to contribute only $200 of their monthly social security income of $1854 to repay creditors in a composition plan while retaining the remaining $1654. The chapter 13 trustee objected to the confirmation on the basis that the plan failed to pay all projected disposable income pursuant to § 1325(b)(1)(B) and the plan was not proposed in good faith under 1325(a)(3). According to the trustee, all sources of income, including social security, are used to determine projected disposable income. The bankruptcy court overruled the trustee and confirmed the plan. In a direct appeal to the Fifth Circuit, the court affirmed the bankruptcy court decision finding that Congress specifically excluded social security benefits from the definition of current monthly income, and therefore, projected disposable income. The court also relied on the Social Security Act §§ 407(a) and (b) as evidence that Congress intentionally exempted social security from bankruptcy provisions. The exclusion of social security was not evidence of a lack of good faith because the debtors were merely following the law enacted by Congress. See also **Anderson v.Cranmer (In re Cranmer)**, 697 F.3d 1314 (10th Cir. Oct. 24, 2012)(Murphy, C.J.), where the 10th Circuit reached similar results.

Drummond v. Welsh (In re Welsh), 2013 U.S. App. LEXIS 5880 (9th Cir. March 25, 2013)(Ripple, C.J.).

The trustee objected to the debtors' composition plan pursuant to the § 1325(a)(3) arguing that the plan was not proposed in good faith because (i) the debtors were deducting secured debt payments for luxury items including two ATVS, an airsteam and a third vehicle driven by their daughter and (ii) the debtors excluded their social security income from repayment to unsecured creditors. The bankruptcy court overruled the trustee's objection , and the BAP affirmed. The circuit court affirmed the BAP finding that the Bankruptcy Code in 707(b)(2)(A)(i) explicitly allowed the deduction of secured debt payments in calculating disposable income and made no provision limiting the type or amount of secured debt payments; therefore, the bankruptcy court was foreclosed from considering those payments when making a determination of good faith. Additionally, the failure of the debtors to commit social security income to repay unsecured creditors was likewise not an indication of bad faith since it was excluded from current monthly income and the calculation of disposable income.

In re Romero, 2013 Bankr. LEXIS 256 (Bankr. S.D. Fla. January 18, 2013) (Cristol, B.J.).

A self-employed truck driver filed Chapter 13 and deducted his business expenses from his gross income on Part I of the Statement of Current Monthly Income resulting in a determination that his income was below the median income. As a result, the debtor proposed a plan with an applicable commitment period of three years. The trustee objected to confirmation of the plan pursuant to 1325(b)(4) arguing that the calculation of current monthly income should include the gross income of the debtor and that he should be required to propose a plan with a five year applicable commitment period. The trustee argued the business expenses were an allowable deduction for the determination of disposable income but not current monthly income and should be taken on Part IV of Official Form 22C. The bankruptcy court disagreed with the trustee and found that there were no conflicts or inconsistencies between Official Form 22C, as promulgated by the Judicial Conference of the United States, and the provisions of §101(10A) or 1325(b)(2). Furthermore, including business expenses in the calculation of current monthly income would be prejudicial to self-employed debtors by inflating the income that they actually receive.

In re Barnes, 2013 Bankr. LEXIS 161 (Bankr. E.D.N.C. January 15, 2013)(Doub, B.J.).

A below median Chapter 13 debtor proposed a plan whereby she would make 36 payments of $99.00 for a total of $3,564. The plan did not provide any payment to unsecured creditors and secured creditors were to be paid "direct". The plan proposed to pay $2,925 to debtor's counsel for attorney fees. If the debtor made 36 payments, then unsecured creditors would receive a 2.1% dividend distribution. The plan, however, included the following language commonly referred to as an "early termination" clause:

"This Chapter 13 Plan will be deemed complete and shall cease and a discharge shall be entered, upon payment to the Trustee of a sum sufficient to pay in full: (A) Allowed administrative priority claims, including specifically the Trustee's commissions and attorneys' fees and expenses ordered by the Court to be paid to the Debtor's Attorney, (B) allowed secured claims (including but not limited to arrearage claims), excepting those which are scheduled to be paid directly by the Debtor [4] "outside" the plan, (C) Allowed unsecured priority claims, (D) Cosign protect consumer debt claims (only where the Debtor proposes such treatment), (E) Post-

petition claims allowed under11 U.S.C. § 1305, (F) The dividend, if any, required to be paid to non-priority general unsecured creditors (not including priority unsecured creditors) pursuant to11 U.S.C. § 1325(b)(1)(B), and (G) Any extra amount necessary to satisfy the "liquidation test" as set forth in11 U.S.C. § 1325(a)(4)."

The "early termination" clause would result in the case completing in 32 months instead of 36 months and only the attorney fees and trustee fees would be paid. The trustee objected to the plan on the basis that the plan did not comply with the ACP requirement of 1325(b) and was not proposed in good faith, as it only proposed to make payments for attorney fees. The debtor argued that there was an exception to the temporal requirement of the applicable commitment period for a below-median debtor with zero disposable income.

The bankruptcy court found the early termination clause to be void in violation of § 1325(b)(4)(B). The court also determined, however, that "attorney only" plans are not per se proposed in bad faith and that under the "totality of circumstances" test the plan met the good faith requirement due to the small dividend that would be now be paid to unsecured creditors due to the void early termination clause. See also **In re Tedder,** 2013 Bankr. LEXIS 144 (Bankr. E.D.N.C. January 14, 2013)(Doub, B.J.) for a similar decision for a debtor with a sixty month ACP.

In re Mack, 2012 Bankr. LEXIS 5988 (Bankr. N.D. Ga. September 11, 2012).

A chapter 13 trustee objected to confirmation of a debtor's plan based on the fact that the debtor failed to propose a sixty month applicable commitment period as required pursuant to 1325(b)(4). In calculating current monthly income, the debtor took a martial deduction on line 13 from the non-filing spouse's income for payroll deductions and 401k contributions. In other words, the debtor only included the net income from the non-filing spouse to determine the ACP. As a result, the debtor's annualized income was below the median, and the debtor proposed a plan with a three year applicable commitment period. The trustee argued that the marital deduction was not permissible in determining the debtor's applicable commitment period and that the spouse's gross income had to be included. The court, adopting the majority position on this issue, overruled the trustee's objection. In doing so, the court relied on the plain language of the definition of current monthly income in § 101(10A). The current monthly income of the debtor is all income received by the debtor from all sources including amounts "paid by" her spouse on a regular basis for the expenses of the household. By definition, CMI is income received by the *debtor*. Therefore, a non-filing spouse cannot have current monthly income, and the amount paid to the debtor is the non-filing spouse's net income not gross income. The trustee's interpretation of current monthly income would produce an absurd result because it would lead to a double-counting of the spouse's income since the current monthly income of the debtor includes amounts received from the debtor's spouse by definition.

In re Tibbs, 478 B.R. 458 (Bankr. S.D. Fla. August 31, 2012).

Chapter 13 debtors proposed to modify their plan pursuant to § 1329 and use a gift from a relative to make a single lump sum payment to creditors to pay out their case early. The trustee objected to the modification on the basis that the early payment would violate the five year applicable commitment period requirement of § 1325(b)(4) unless the debtors paid unsecured creditors in full. The debtors were proposing to pay the same dividend to unsecured creditors provided in their confirmed plan with the lump sum. The bankruptcy court overruled the trustee's objection and approved the modification holding that § 1329, which provides for plan

modification, does not incorporate the applicable commitment period provisions of § 1325(b)(4). Modified plans pursuant to § 1329 only need comply with the provisions explicitly referenced including §§1322(a), 1322(b), 1322(c) and 1325(a) including good faith. According to the court, the ruling in Tennyson, which found that the ACP was a temporal requirement only applies to confirmation and not plan modification.

B. Plan Treatment

Brown v. Branch Banking & Trust Co. (In re Brown), 2012 Bankr. LEXIS 4070 (Bankr. S.D. Ga. September 4, 2012) (Barrett, C.B.J.).

A chapter 13 debtor filed an adversary proceeding against the mortgage holder for a property surrendered in the plan alleging contempt of the confirmation order, violations of the automatic stay and sought damages pursuant to § 362(k). The debtor argued that the mortgage creditor should be compelled to "accept" the property surrendered under the plan pursuant to § 1325(a)(5)(C) and that failure to do so violated the stay and the confirmation order. The bankruptcy court rejected this argument and held that a creditor has no affirmative duty to take action to accept a surrendered property. Under Georgia law, the grantor of a security deed is the equitable owner of the property and retains all responsibilities of ownership until foreclosure. While a debtor has the option of surrender of collateral, nothing in the Bankruptcy Code requires a creditor to take steps to take possession of the property.

In re Perry, 2012 Bankr. LEXIS 4731 (Bankr. E.D.N.C. October 9, 2012)(Doub, B.J.).

Due to a reduction in income, a chapter 13 debtor filed a motion seeking modification of her confirmed plan and an order approving surrender of her residence to her mortgage creditor and requiring the creditor to be responsible for the property taxes and maintenance of the property. The mortgage creditor did not respond to the motion. The court held that § 1325(a)(5)(C) allowed a debtor to surrender collateral to a creditor and noted that the code section did not require consent by the creditor. The court entered an order requiring the mortgage creditor to commence foreclosure proceedings within sixty days and granting the debtor to authority to quitclaim her interest in the property to the mortgage creditor in the event that the creditor failed to do so.